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Balázs Bodzási*

Development of the Regulation of Lien in Hungary, and the Factors Affecting Regulation**

I Relationship Between Securities In Rem and the Economy

1 Economic Background

Economic research has shown that there is a close relationship between securities in rem and the economy. Securities in rem are of particular importance for the functioning of lending.[1]

The core economic function of securities is to strengthen keeping contractual promises. Securities seek to reduce the risks arising from legal transactions. As such, there is a close correlation between risk aversion and the provision of securities.

Entering into an agreement on the application of securities can be considered as a secondary, accessory transaction, which presupposes a main transaction i.e. a credit agreement.[2] The security transaction remains in the background until the transaction containing the credit element is properly completed. However, should any defect occur in the course of fulfilling the primary transaction, especially if the fulfillment by the debtor fails to come about, securities then come to the fore. In that case, the security transaction will supersede the primary transaction.[3]

Securities also play an important role in making a decision on lending. The existence and value of securities affect the primary service itself, which is the provision of a loan in the majority of the cases. Accordingly, non-existent or incomplete securities may even preclude lending in reality, or make it extremely difficult and expensive.[4]

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1 Josef Duttle, *Ökonomische Analyse dinglicher Sicherheiten* (Marchal und Matzenbacher Wissenschaftsverlag 1986, Krefeld) 9–150; Bernd Rudolph, 'Zur Funktionsanalyse von Kreditsicherheiten' (1985) 10 Die Bank – Zeitschrift für Bankpolitik und Bankpraxis 503–507; Eberhard Dorndorf, *Kreditsicherungsrecht und Wirtschaftsordnung* (C.F. Müller Verlag 1986, Heidelberg) 75.

2 In legal terminology, it is called 'ancillary principle'. See the details of ancillary principle in Dieter Medicus, 'Die Akzessorietät im Zivilrecht' (1971) 10 Juristische Schulung (JuS) 497–504.

3 Peter Bülow, *Recht der Kreditsicherheiten* (C.F. Müller Verlag 1984, Heidelberg) 1.

4 Ulrich Drobnig, *Empfehlen sich gesetzliche Maßnahmen zur Reform des Mobiliarsicherheiten?* (Verhandlungen des 51. Deutschen Juristentages. Band I [Gutachten], Teil F., C.H. Beck'sche Verlagsbuchhandlung 1976, München) 15.

From an economic perspective, besides the decision to provide a loan, securities also have an important role in determining the conditions of lending. There is a link between the securities applied, and the price of the loan and the rate of interest. This close connection is also demonstrated by the fact that the loans covered by security (secured loans) and unsecured loans have different rates of interest. The level of interest depends on several factors but the size of the risk of the debtor's insolvency to be taken into account by the creditor has an important role in determining the interest rate. Because of that risk, creditors charge a risk premium.[5]

2 Regulation of Lien and the Various Forms of Lending

A distinction should be made also at the legislative level between business (commercial) loans and the cases of lending outside that scope. This dichotomy is also reflected in the regulation of liens. However, all this does not mean that loans for consumers would have provided a regulatory template for the civil codes of Europe.

As regards the regulation of liens, the main priority is to secure the loans or credits provided by banks (credit institutions). Commodity loans have substantially different characteristics. The economic role of commodity loans is also significant but they require other types of securities. Retention of title is a form of security that is typical for commodity loans, while lien is linked to money loans. Hence, the form of the security to be applied depends not only on the nature of the loan concerned, but also on the creditor providing it.

Since the 1850s, the regulation of lien in Hungary has always focused on commercial and business lending, where the typical creditor is a bank. However, in addition to that, legal regulations must also cover non-business loans.

II The Role of Agriculture

Agriculture should be highlighted in the economic background of the regulation of lien. Agriculture continues to play a key role in Hungary; therefore, agriculture also has a key role in lending.

Because of the dominant role of agriculture, proposals for economic reform at the beginning of the 19th century were also primarily connected to agriculture. In his work published in 1829, *János Balásházy* analyzed the problems arising from the scarcity of credit. Moreover, *István Széchenyi* gave the title 'Credit' to his book published in 1830. The latter work is of great importance because it was the first modernization program in Hungary to encompass the whole of society and the economy. He was the first to provide a comprehensive economic and legal program, and to recognize correlations between the economy and law.[6]

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[5] Hans-Bernd Schäfer, Claus Ott, *Lehrbuch der ökonomischen Analyse des Zivilrechts* (4th edn, Springer Verlag 2005, Berlin–Heidelberg) 591.

[6] Horváth Attila, 'Széchenyi István modernizációs programjának hiteljogi vonatkozásai' (1991) 7 Jogtudományi Közlöny 35.

The decisive role of agriculture also appears in the explanations accompanying the drafts of the Civil Code worked out at the beginning of the 20th century. However, in addition to creating investment opportunities attracting capital to agriculture, the protection of the interest of landowners of the time was also an important factor. In addition, it precluded the renewal of rules of lien for several decades.

It took World War I and the subsequent economic collapse to urge Hungarian legislators to give a completely different answer to the issue of agricultural reform than before. Act XXXV of 1927 on Lien (hereinafter referred to as 'Lien Act') incorporated all the lien instruments that the draft civil codes had been reluctant to accept. In the economic environment of the 1920s, Hungarian legislators aimed at creating legislation that promotes lending. Boosting lending in agriculture was an especially important aim. The legal regulations of the time relating to lien were adopted in order to satisfy that economic need.

The Lien Act, aimed at improving the conditions of lending. The ministerial explanatory memorandum for the Lien Act explicitly stressed that, after World War I, loans were scarce and economic transactions were lacking the money that would have been necessary for creating a healthy crediting environment. Hungary made efforts to remedy that situation through measures accelerating the circulation of money. By doing so, they were able to achieve the same economic results with a relatively smaller amount of money. One of the main goals of the Lien Act was to facilitate capital flows also with regard to loans provided for the purchase of real estate. To this end, security lien was provided on a wider scale; it was also made transferable, and the legal institutions of land debt and land debenture bond were also established.[7]

In the early days of the political changeover after 1989, when the two-tier banking system was established, lending in agriculture came to the fore again. The transformation of the banking system and capital shortages had a particularly strong impact on agriculture. The collapse of the markets of the former socialist countries, as well as compensation for land taken into state ownership under socialism, led to a sharp decline in agricultural production as a consequence of the newly-fragmented structure of agricultural land.[8] The establishment of an independent agricultural bank was also suggested. All the above could mainly be justified by the characteristics of agricultural production and financing. No independent agricultural bank was established after all; however, traditional commercial banks could not respond adequately to the specificities of agriculture. In order to cover the increasing risk attributable to price volatility, financial institutions asked for additional securities from producers, e.g. by obliging their family members to undertake a guarantee, too.

[7] Nizsalovszky Endre, *A jelzálogjog jogszabályainak magyarázata* (Grill Károly Könyvkiadóvállalata 1929, Budapest) 2–5.

[8] According to the data of the Hungarian Central Statistical Office (KSH), agricultural production in Hungary decreased by more than 30 % between 1989 and 1993. *Magyarország 1989–2009. A változások tükrében* (KSH 2010, Budapest) 39–40.

According to a study published in 2010, as a result of the above, a large part of agricultural investments had not resulted in any improvement in efficiency. Traditional financial institutions give credit to agricultural companies only under strict conditions; because of the characteristics of agricultural production they consider it very risky to grant loans, and for this reason the majority of the loan applications submitted are rejected upon assessment.[9]

Due to the role of agriculture in the Hungarian economy and the characteristics of agricultural production, closer attention is paid to agriculture in the course of regulating securities.

III Reforms of the Regulation of Lien in Hungary after the Political Changeover

1 Background: Ownership and Economy in the Socialist Era

After 1945, Hungarian private law changed radically. Compared to the previous era, state control covering society and the entire economy made a substantial difference, entailing the infiltration of public law elements into private law. The change in the system of property ownership after 1945 had far-reaching consequences up to nowadays.[10]

The Civil Code that was specific to the socialist circumstances was adopted in 1959. Though Act IV of 1959 on the Civil Code kept a few provisions on lien, it only remained a relic of the past in socialist civil law for several decades.

In the 1959 Civil Code, the regulation of lien was not adapted to economic needs; rather, it reflected the respect of the legislators for the old Hungarian private law when drafting the Code. However, such a decline can be observed not only regarding securities in rem but also in the case of personal securities. Guarantee was also rarely used; in reality, it was connected almost exclusively to the consumer credits of private individuals.

Change took place only in the 1980s. On the one hand, this is closely related to the fact that the first forms of enterprise appeared in Hungary in that decade and, on the other hand, the monopoly of state ownership and the planned economy loosened.

2 Changes in the Economic Conditions in the 1990s

Dismantling state ownership and establishing a social structure based on private property had already started in the 1980s. The former socialist system of property ownership was fundamentally changed by a few factors:

[9] Gór Arnold, *Miért van szükség egy magyar agrárbankra?* (2012. augusztus) Hitelintézeti Szemle (Különszám) 5.

[10] Harmathy Attila, 'Jogpolitika – polgári jog' (2010) 12 Magyar Jog 709.

– dismantling state ownership i.e. privatization;
– restitution a part of the nationalized property or the countervalue thereof i.e. compensation;
– offering state property to local governments, churches, civil society organizations and political parties.

As a result of the fundamental transformation of the property system, the share of the private sector increased from 15-20% of GDP to 40-45% between 1989 and 1993. The number of private enterprises increased from 393,000 (1990) to 745,000 (1996). Following the adoption of the first Act on Business Organizations in 1988, partnerships and business associations were established across the country. The number of private companies increased from 45,770 (1990) to more than 280,000 (1997). In parallel, the number of state-owned companies decreased; while in 1990 there were 1859 state-owned companies operating in Hungary, by 1997 their number had fallen to three. Simultaneously with the increase in the number of private companies, the number of insolvency proceedings increased as well.[11]

As regards the credit environment, the most important change was that the value of foreign investments increased significantly. In 1988, the value of foreign investments amounted to USD 23 million. By 1998, this value had exceeded USD 8.1 billion. Due to the capital shortage in the country, foreign investments were of utmost importance.[12]

In parallel with the inflow of foreign capital, the banking system was also reorganized. The restructuring of the banking system began as early as 1984 but the most important milestone was 1987. The so-called two-tier banking system was established in that year, i.e. commercial banks appeared at that time (since the socialist era began there had been only one retail bank in Hungary). Thereafter, the National Bank of Hungary no longer financed enterprises directly; this task was taken over by commercial banks. In 1987 there were already nine commercial banks operating in Hungary. In the 1990s, specialized credit institutions also appeared on the market and the first mortgage credit institutions started to operate in 1997.

3 Amendments on Lien

The transition to private property and capital shortage forced the legislators in all the former socialist countries to reregulate the legal instruments of corporate financing.[13]

After 1989-1990, the comprehensive reform of the laws on security interest was driven primarily by changes in the system of property ownership and the transformation covering the banking sector as well. In addition, lending was also hindered by incomplete and outdated

[11] Harmathy Attila, 'Das Recht der Mobiliarsicherheiten – Kontinuität und Entwicklung in Ungarn' in Karl F. Kreuzer (Hrsg.), *Mobiliarsicherheiten – Vielfalt oder Einheit?* (Nomos 1999, Baden-Baden) 84.

[12] Harmathy (n 11) 85.

[13] Pistor Katharina, 'Aktien und Kredite als Mittel der Unternehmensfinanzierung und Unternehmenskontrolle in Transformationsländer' in Ulrich Drobning, Klaus J. Hopt, Hein Kötz, Ernst-Joachim Mesmäcker, *Systemtransformation in Mittel- und Osteuropa und ihre Folgen für Banken, Börsen und Kreditsicherheiten*. (Mohr Siebeck 1998, Tübingen) 109–134.

insolvency rules. The harmonization of the rules on lien and insolvency proceedings was also needed. It is no coincidence that the main reason underlying the 1993 draft to amend the rules on lien as set out in the Civil Code was in order to boost the economy.[14]

Act XXVI of 1996 (the first amendment on lien) was intended to adapt the regulation of lien to the conditions of a market economy based on private property. The main objective of the amendment was to promote obtaining credit through new solutions, both for consumers and for the business sector so that lien instruments would provide both effective cover and security for creditors.

The most important new features of the amendment were the following:

- establishing the instrument of mortgage on movable property;
- mortgage on assets;
- enlargement of the scope of application of general collateral mortgage;
- legal instruments related to ranking;
- expanding the rules of lien on rights or claims;
- independent lien (non-accessory lien);
- amending the rules of judicial enforcement.

The new legal instruments – mainly lien on movable property – served the purpose of facilitating access to capital, primarily for small and medium-sized enterprises. A wider scope of lien on rights or claims also made it possible to establish a lien on holdings in companies.

The economic arguments for lien on movable property had already appeared in the legal literature at the beginning of the 20th century. It means that possessory lien alone was not sufficient to respond to economic needs. It seemed appropriate to legitimate the interests of debtors who only had their movables to pledge in order to secure the loan they applied for. However, encumbering movables with possessory lien prevented the owners of pledged property from carrying out their gainful activities. They could not obtain a loan on security because it would have prevented them from using their movables. Another argument was that someone who has already encumbered their movables – contrary to the owner of real estate –was only allowed to take out any further loan secured on the same pledged property from the same creditor.[15]

The idea of establishing lien on movable property was put into practice 80 years later. An authentic public register for that purpose was also established then; the Notarial Chamber undertook to maintain a register of liens on movable property as well as liens on assets.[16]

In spite of several new features introduced by the first amendment on lien, it did not provide an adequate solution to a number of issues. One such issue was that legal practice failed to incorporate the 1996 amendment on lien entirely, and that regulation was rather vague.

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14 The 1993 draft was signed into Act XXVI of 1996 (the first amendment on lien).

15 Bozóky Géza, 'Ingó jelzálogjog' in *Emlékkönyv Grosschmid Béni jogtanári működésének harminczadik évfordulójára* (Rényi Károly Bizománya 1912, Budapest) 88, 95.

16 Harmathy Attila, 'Kreditsicherheiten im sozialistischen System' in Drobning, Hopt, Kötz, Mesmäcker (n 13) 314.

That is why the legislature amended the rules of lien set out in the Civil Code again, in 2000. Act CXXXVII of 2000 on amending the Acts related to lien (the second amendment on lien) aimed at addressing the issues arising in the meantime. No new instruments were introduced by the second amendment on lien; it only clarified and detailed the amendments adopted in 1996.

IV Provisions of the Civil Code of 2013 relating to Lien

Act V of 2013 on the Civil Code (hereinafter referred to as the 'Civil Code') introduced a further reform on lien, which was the third one in two decades.

The new Code considered it as an important legal policy objective to make lien as the primary security in rem while putting the prohibition of *lex commissoria* into the focus of regulation.[17] Closely relating to that the prohibition of fiduciary securities was declared (Section 6:99 of the Civil Code).[18]

One of the most controversial new features of the Civil Code was – relating to the nullity of fiduciary securities – the cancellation of independent lien. Instead, the new Civil Code regulated the instrument of seceded lien (Section 5:100 of the Civil Code). However, the legal instrument of seceded lien was heavily criticized by the banking sector. According to critics, that new legal instrument was not suitable for use in connection with more complex banking refinancing techniques.

The regulatory concept of the Civil Code concerning securities in rem, which was based on new grounds, is logical and reasonable in doctrinal terms. However, the main problem was that the Civil Code was adopted at a time when the Hungarian economy still experienced the negative impact of the lending crisis that started to become increasingly severe in 2008. Borrowing from a bank became more and more difficult, especially for small and medium-sized enterprises. However, the whole Hungarian economy was affected by the credit crunch and the dramatic fall in the lending activity of domestic financial institutions. The Civil Code was adopted in that economic-financial environment, canceling well-established legal instruments, hitherto widely used in domestic corporate lending (fiduciary securities, independent lien, lien on assets).

In the light of all the foregoing, it is important to explain in detail the developments that have taken place in the Hungarian economy, and in the sector of financial intermediaries in particular, in the last few years, and the expectations of the legislative bodies created thereby.

[17] Menyhárd Attila, 'A dologi jog szabályozásának sarokpontjai a Polgári Törvénykönyvben' (2013) 1 Jogtudományi Közlöny 527.

[18] That ban was mitigated by legislative bodies in 2016.

V The Hungarian Economy and Banking Sector after 2008

We should start our analysis by stating that the Hungarian economy and financial system have remained bank-centred (or, rather, financial institution-centred) to date. Capital markets play second fiddle in financing Hungarian businesses. Therefore, the lending activity of the financial institution system is pivotal to the development and growth of the Hungarian economy.[19] In particular, lending to small and medium sized enterprises (hereinafter the SME sector) is critical. Dysfunctions in the financial mediation system are to a great extent manifested in shrinking domestic corporate lending, which harms the SME sector first of all.

Bank lending practically collapsed in Hungary after 2008. This meant that corporate and retail lending equally faced several years of depression. Private sector loans continued to decrease even in 2013.[20] The credit crunch resulted in declining investments, with many companies forced to delay their capital expenditure projects due to lack of credit. National Bank of Hungary (hereinafter 'NBH') figures suggest that all this stymied Hungary's economic growth by 1% on average.[21]

Tightening lending restrictions did not, however, affect the Hungarian corporate sector to the same degree. Large – overwhelmingly foreign-owned – companies had easier access to loans provided by foreign banks or their own foreign owners. By contrast, Hungarian-owned enterprises having to rely on domestic bank financing were far more adversely affected by the credit crunch, which often made their operations impossible.[22]

Large domestic enterprises increasingly sought foreign loans and domestic borrowing by this sector significantly decreased. At present, large undertakings borrow either from foreign banks or from their own foreign parent companies, and hardly if at all from domestic banks. As a result, the total volume of Hungarian corporate loaning from domestic banks had fallen to EUR 19 billion by the end of July 2016 (the low point last recorded in 2005).[23]

At the same time, the overall debt of domestic companies did not decrease. Hungarian companies merely shifted from domestic bank loans to – increasingly and to a significant degree – borrowing from foreign banks or their own foreign parents. According to NBH figures, the total volume of Hungarian corporate debt amounted to EUR 93 billion in March 2016. In other words, the share of domestic bank loans in corporate borrowing shrunk to 20%. Having said that, corporate borrowing from other (overwhelmingly foreign-owned) companies now totals EUR 27 billion, while the volume of Hungarian companies' foreign

19 Balog Ádám, Matolcsy György, Nagy Márton, Vonnák Balázs, 'Credit crunch Magyarországon 2009–2013 között: egy hiteltelen korszak vége?' [Credit crunch in Hungary between 2009 and 2013 – End of an Era without Credit?] (2014) 4 Hitelintézeti Szemle 4, 15.

20 Balog, Matolcsy, Nagy, Vonnák (n 19) 15–16.

21 Balog, Matolcsy, Nagy, Vonnák (n 19) 16.

22 Balog, Matolcsy, Nagy, Vonnák (n 19) 19, 22.

23 <http://www.vg.hu/penzugy/hitel/tobb-kolcsont-vesznek-fel-a-cegek-kulfoldrol-mint-magyarorszagrol-475012> accessed 7 September 2016.

bank debt reached EUR 39 billion.[24] Accordingly, over 40% of domestic corporate debt is now made up by foreign bank loans. In total, the share of foreign debt in overall Hungarian corporate borrowing has grown to 65%. As a consequence, the balance sheet structure of the Hungarian banking sector has changed drastically since 2008.

At the same time, the amount of EUR-denominated loans taken out by Hungarian enterprises grew to some extent. NBH figures suggest Hungarian companies borrowed EUR 1.4 billion in EUR-denominated loans between January and August of 2016, representing a year on year increase of 14%.[25] Foreign currency-denominated loans are primarily extended to large enterprises and mostly by foreign banks. The amount of foreign currency-denominated loans provided by foreign banks far outweighs those provided by domestic banks.[26]

This picture becomes somewhat more refined when we look at small or medium-sized enterprises without considering large undertakings. That is because the share of loans offered by foreign banks to SMEs is significantly smaller, even if the volume of foreign currency-denominated borrowing by the SME sector has increased in the recent period. However, in the first half of 2016, the aggregate value of SME debt decreased by about 4%. In July 2016, total SME borrowing stood at EUR 11.6 billion, reflecting a decrease of EUR 300 million since March 2016.[27] As a consequence, the lending gap has widened between large undertakings and SMEs.[28]

As opposed to corporate lending, the decrease in retail (consumer) lending halted in the meantime and growth in foreign currency-denominated retail borrowing, especially the volume of mortgage loans,[29] picked up again following the conversion of foreign currency-denominated consumer loans into HUF[30]. This indicates a growing housing loan portfolio primarily driven, for the time being, by significantly increased demand for used housing. The main reason for this is low interest rates bound to stimulate further significant volume growth in housing loans.

The low interest rate environment is an unprecedented challenge for the Hungarian banking system. The Hungarian banking sector incurs a loss of EUR 65-100 million annually

24 <http://www.vg.hu/penzugy/hitel/tobb-kolcsont-vesznek-fel-a-cegek-kulfoldrol-mint-magyarorszagrol-475012> accessed 7 September 2016.

25 <http://www.vg.hu/penzugy/hitel/viszik-az-eurohitelt-476200> accessed 4 October 2016.

26 <http://www.vg.hu/penzugy/hitel/viszik-az-eurohitelt-476200> accessed 4 October 2016.

27 <http://www.vg.hu/penzugy/hitel/tobb-kolcsont-vesznek-fel-a-cegek-kulfoldrol-mint-magyarorszagrol-475012> accessed 7 September 2016.

28 For more details see: MNB Hitelezési folyamatok [National Bank of Hungary Lending Processes], May 2016, <http://www.NBH.hu/letoltes/hitelezesi-folyamatok-2016-majus-hu.pdf> accessed 11 August 2016.

29 Act LXXVII of Act LXXVII of 2014 on the settlement of matters relating to the currency conversion of certain consumer loan agreements and to interest rate rules set forth the provisions about the conversion of foreign currency-denominated consumer loans to HUF.

30 <http://www.portfolio.hu/finanszirozas/hitel/uj_orulet_magyarorszagon_mindenki_szemelyi_kolcsont_akar.235426.html> accessed 29 July 2016.

due to low interest rates alone.[31] The low interest rate environment rendered the former business model untenable, as it depended heavily on net interest income (which poses a very serious problem to the savings cooperative sector in particular).

Low interest rates cause also a serious headache for clients seeking lucrative investment opportunities. Even so, retail savings rose by 25% in 2015.

As regards bank lending, the concurrent steady decline of amounts deposited by commercial banks with the National Bank of Hungary is another overarching factor. However, the government security portfolio is simultaneously increasing.

Also linked to low interest rates are banks' diminishing short-term external resources, well-illustrated by changes in the loan-to-deposit ratio, which shows a falling trend from 160% in recent years to 85% by 2016. The situation is even worse in the savings cooperative sector, which plays a key role in agricultural lending, where the same ratio is barely 40%.[32] This is a very low level, clearly pointing to the need to increase lending, which, however, cannot be financed from ever-decreasing bank deposits. As such, financial institutions must seek long-term resources (including, for example, mortgage bonds).

Bear in mind that the continued tightening of domestic and EU banking supervision rules forces banks to exercise increasing prudence in their operations. An indication of that is the banks' obligation to reach a capital adequacy ratio of 16% in the future. In addition, the rules of consumer lending have also become stricter.[33]

As a result, the Hungarian banking system has been facing several challenges in recent years. In addition to having to adjust to the low interest rates mentioned above, the growing volume of non-performing loans presents an increasingly serious issue. These bad loans should be purged from banks' balance sheets as soon as possible, along with concurrently improving domestic banks' profitability.

The amendment of the Civil Code in respect of lien has been most influenced by economic policies designed to stimulate the mortgage bond market. It was to this end that the National Bank of Hungary issued Decree No. 20/2015 (VI. 29) on the forint maturity match of credit institutions. Consistent with this is the fact that, in 2016, three new actors appeared in the domestic mortgage banking market.[34]

[31] It has been said at the conference 'Lending 2017' on 25 April 2017 in Budapest.
[32] Source: National Bank of Hungary (MNB).
[33] Act LXXVIII of 2014 amending Act CLXII of 2009 on consumer loans and certain related Acts.
[34] <http://www.vg.hu/penzugy/harom-jelzalogbank-johet-455693> accessed 16 August 2015.

VI Reregulated Independent Lien

1 Circumstances Determining the Reregulation of Independent Lien

Two important items of legislation need to be highlighted separately in connection with the reregulation of independent lien:
– Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (hereinafter 'CRR Regulation'); and
– Decree No. 20/2015 (VI. 29) by the National Bank of Hungary on the forint maturity match of credit institutions.

In relation to minimising exposure resulting from mortgage lending, Article 402 (3) of the CRR Regulation, which is directly applicable in EU member states, specifies non-accessory independent mortgage liens. This fact alone encouraged Hungarian legislators to reregulate independent lien.

However, an even more compelling argument was the uncertainty arising under the CRR Regulation as regards the assessment of separated lien, created by the Civil Code, since it was unclear whether or not domestic mortgage lenders could invoke the CRR Regulation's clause on exemptions from 'limits to large exposures'[35] in applying separated lien. Invoking the exemption clause of the CRR Regulation for the purposes of providing mortgage loans to financial institutions for which they refinance securities is an important competitive advantage for mortgage banks. The CRR Regulation does not recognise the concept and institution of separated lien, which used to be an accessory mortgage arrangement. Accordingly, mortgage banks applying separated lien in their refinancing activities were running the risk of violating the 'limits to large exposures'.

The need to introduce the other item of legislation, namely Decree No. 20/2015 (VI. 29.) of the National Bank of Hungary, arose after the compulsory conversion of long-term foreign currency-denominated consumer mortgage loans into HUF,[36] which resulted in the Hungarian banking sector's need to secure stable long-term HUF resources. Since the term to maturity of the overwhelming majority of consumer mortgage loans converted to HUF was over 10 years, a maturity mismatch between mortgage loans and deposits gave rise to a systemic risk, due to deposit-financed lending. That was because banks had no other choice after HUF conversion than to finance their existing mortgage exposures from deposits placed with them. The National Bank of Hungary intended to manage the resulting liquidity risk by requiring banks to secure stable funding in HUF.

35 Based on this, the exposure of an institution falling under the CRR Regulation to another institution must not exceed 25% of its eligible capital.

36 Mandatory conversion to HUF was laid down by Act LXXVII of Act LXXVII of 2014 on the settlement of matters relating to the currency conversion of certain consumer loan agreements and to interest rate rules.

Decree 20/2015 (VI. 29.) of the National Bank of Hungary provides that banks are required to secure stable HUF funds of up to 15% relative to their total mortgage exposures. They are also obliged by the Decree to comply with this requirement in respect of existing mortgage loans. The Decree thereby prescribes the duty to engage adequately stable funds to cover the financing of long-term retail mortgage loans.

The NBH Decree seeks to strengthen the Hungarian banking system by ordering banks to cover long-term assets with long-term liabilities. Reducing the mismatch between maturities in this manner encourages banks to finance their exposures by issuing mortgage bonds or from refinancing loans secured by mortgage bonds rather than from deposits, as the former two are recognised as long-term liabilities. That is because the criteria laid down in the Decree are at present only met by mortgage bonds and refinancing resources obtained from mortgage banks. All this can also reduce the costs of domestic credit institutions, since the interest on mortgage bonds and refinancing loans tends to be lower than the costs of the funds used at present. In this way, price competition in the mortgage loan market can intensify, which can in turn improve the availability of funds and increase lending volumes.

Since separated lien was not an adequate form of security in relation to the transactions that the NBH Decree identified as desirable, the need to reregulate independent lien appeared.

2 Major Hallmarks of the Reregulated Non-Accessory Lien

It was justified by economic needs that, in 2016, Hungarian legislators amended the rules on lien laid down in the Civil Code. Those amendments were made in Act LXXVII of 2016 on amending Act V of 2013 on the Civil Code.

The most significant new feature of the 2016 amendment is the reregulation of independent lien.[37] It is important to emphasize that it is not identical to the independent lien regulated by Section 269 of the Civil Code of 1959. In the course of the reregulation, the instruments contributing to the protection of the pledger owner (e.g. limitation of the restriction of objection, codification of the collateral agreement) while maintaining the advantages of independent lien (transferability, flexibility) again came to the fore. It is an important guarantee rule that an independent lien may only be established by financial institutions, and it can be transferred only to financial institutions. It is also a substantial change compared to the rules of the 1959 Civil Code that an independent lien may only be established in the form of a real estate mortgage. It corresponds to foreign models (*Grundschuld* in Germany, *Schuldbrief* in Switzerland), and also to the traditions of Hungarian legal history (land debt).

The amendment of the Civil Code also allowed financial institutions to transform their existing accessory liens into non-accessory liens. Special rules apply to non-accessory lien

[37] For more details on the reregulated non-accessory lien see Balázs Bodzási, 'Reregulated Non-accessory Lien in the New Hungarian Civil Code' (2017) 58 (2) Hungarian Journal of Legal Studies – Acta Juridica Hungarica 206–223.

created by transformation, which is not identical to the independent lien created by conversion as regulated in Section 5:100 (9) of the Civil Code. First, it may not be used subsequently for any purpose other than the original purpose of the security.

The independent lien reregulated by the 2016 amendment of the Civil Code differs from the former independent lien in several aspects. The major differences are summarized as follows:

– only financial institutions may be holders of a reregulated non-accessory lien;
– only real estate may be the subject of a reregulated non-accessory lien;
– the non-accessory lien encumbers the real estate up to a specific sum in any event, but does not extend to the associated costs in excess of that amount;
– no limitation of objection may be applied i.e. the pledger may enforce his objections also against the *bona fide* buyer of the non-accessory lien;
– the new provisions protect personal debtors as well;
– the parties entering into a security agreement, the mandatory substantive elements of which are laid down by the Civil Code, is a precondition of exercising the right to obtain satisfaction associated with the non-accessory lien ;
– the owner's non-accessory lien is also recognized by the Civil Code as a valid instrument.

In our opinion, the reregulated independent lien is an appropriate legal instrument to promote lending, aiming at responding to economic needs for boosting the domestic market of mortgage bonds. However, the application of non-accessory lien has greater potential, e.g. in combination with the instrument of trust and, as a result of that, in offering new refinancing techniques to the Hungarian banking sector.

VII Summary

Overall, when examining the regulation of lien in its entirety, analyzing the economic background and taking economic needs into account are unavoidable.

Business and commercial lending has been the regulatory model for the modern regulation of lien for 150 years, though credits provided to consumers have also been taken into account.

However, a distinction should be made – even within corporate lending – between credits provided to large international companies, to the domestic small and medium-sized enterprises and to farmers. The types of credit belonging to various groups differ significantly, and thus require different securities.

One of the most important differences between business and non-business credits is the extent to which the legal system allows the marketability of the securities associated with them. Consequently, the two main legal policy objectives are to increase the marketability of lien, and to protect the owner of the pledged property.

It is an important economic expectation in the field of business and commercial lending to make it as easy as possible to transfer the claims secured by lien. Furthermore, the legal instruments serving the purpose of increasing the marketability of lien should be established. By contrast, as regards the retail and consumer loans, the interests of the owner providing the security come to the fore, consistently with the increased protection of personal debtors qualifying as consumers.

Legislators should aim to facilitate the conditions of obtaining credit i.e. to make lending cheaper and faster. Hungarian legislators have been guided by that economic policy objective since the second half of the 19th century. It is closely associated with the fact that, traditionally, the Hungarian economy requires capital. However, this legal policy objective also takes into account the general economic experience that a 1percent corporate credit growth results in a GDP increase of between 0.5 and 2 percent.[38]

[38] Kovács Levente, 'A bankszektor helyzete és kihívásai 2013-ban' in Kerekes György (főszerk.), *Magyar Pénzügyi és Tőzsdei Almanach 2013–2014* (XXIII. évfolyam, TAS-11 Kft. 2013, Budapest) 72.

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