



# From Resolution to Claim: The Legal Transformation of the Dividend Right

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## Abstract

In the last 2 years, two Hungarian regional courts of appeal have published decisions in which they examined the nature of the right to dividends. The courts had to answer whether the general meeting had the right to amend its earlier decision on the payment of dividends. The judgments were based on the premise that the decision to pay dividends does not change the legal nature of the member's right to dividends, and it does not create an obligation between the member and the company under the law of obligations. The courts therefore concluded that the decision to pay dividends could subsequently be amended by the company. In this paper, we argue that this interpretation is wrong. The decision to pay dividends creates a monetary claim (dividend claim) for the company's members under the law of obligations. It follows therefore that company law measures, such as a resolution of the general meeting, cannot affect the dividend claim, and—as with all other monetary claims—it can only be changed based on a contract between the creditor (i.e., the shareholder) and the debtor (i.e., the company), in line with the rules of the law of obligations. We also examine the question of when such a dividend claim becomes due. We argue, acknowledging the difficulties of interpretation, that the claim becomes due when the decision is taken by the general meeting, but that the company cannot make a payment if this would jeopardise the company's solvency.

**Keywords** Dividend · Dividend claim · Resolution of the general meeting · Amendment of dividend resolutions · Maturity of dividend claims

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## 1 Background

In their judgments, the Győr Regional Court of Appeal in 2022 and the Debrecen Regional Court of Appeal in 2023 examined whether it is possible for the company's general meeting to change an earlier resolution of the general meeting in which the shareholders approved the board's proposal to pay dividend. The question was whether, in a subsequent resolution, the general meeting may decide that no dividend is paid or that the amount of dividend is reduced. The courts answered this question in the affirmative.

### 1.1 Decision of the Debrecen Court of Appeal

In its decision, the Debrecen Court of Appeal stated that the company may subsequently change or repeal its previous decision to pay dividends.<sup>1</sup> The Győr Court of Appeal held that the company may change its earlier decision to pay dividends but that such a decision is ineffective against a person who was a member of the company at the time of the earlier decision but is no longer a member at the time of the new decision.<sup>2</sup>

The facts of the case examined by the Debrecen Court of Appeal were very simple: the general meeting of the company decided to pay dividends, and subsequently, the general meeting—with the plaintiff voting against—revoked its earlier decision and decided not to pay dividends. The disappointed plaintiff asked the court to order the defendant to pay dividends, and should the court reject the primary claim, to order the company to pay the same amount on the grounds of unjust enrichment.

The first instance court dismissed the claim on the grounds that there is no rule prohibiting the general meeting from annulling its earlier decision to pay dividends. The court argued that the resolution does not create a monetary claim for the company's members under the law of obligations; the relationship between the company and its members concerning the dividend is comprehensively regulated by company law. This argument was relevant in deciding the case, as this was the primary reason why the court found it possible to conclude that as the member's dividend right belonged to the sphere of company law, the company had the right to terminate it by a new resolution. The court also rejected the secondary claim. The reason for rejection was that, under Hungarian law, the rules of unjust enrichment are subsidiary in nature, which means that they are not applicable if a legal relationship exists between the parties. As the court found that the legal relationship between the parties is governed by the rules of company law, the court rejected the unjust enrichment claim.

<sup>1</sup> PJD2023. 9. PJDs are edited decisions of primarily regional courts of appeal, selected for publication by the Editorial Board of *Polgári Jog* [Civil Law], a bi-monthly Hungarian law journal, and edited by Máttyás Parlagi and Péter Gárdos.

<sup>2</sup> BDT2022. 4538. BDTs are edited decisions of primarily regional courts of appeal, selected for publication by the Editorial Board of *Bírósági Döntések Tára* [Collection of Court Decisions].

The second instance court upheld the judgment. The Debrecen Regional Court of Appeal agreed with the reasoning of the first instance court regarding the primary claim and added that the same principle had already been formulated by the Supreme Court.<sup>3</sup> As regards the secondary claim, the court added that it is logically not possible for the company to be unjustly enriched as any unpaid dividend increases the value of the plaintiff's shares.

It is beyond the scope of the present article to examine in detail the idea that unpaid dividends necessarily increase the value of the shares. In the case of public limited companies, this would imply that if the company does not pay dividends, the stock market price of its shares will automatically increase by the amount per share that could be paid out as dividends. However, no such automatic effect is found in the stock market data. In their study, Nobel laureates Miller and Modigliani show that in a perfect market, a company's dividend policy has no effect on the value of the company.<sup>4</sup> Others argue, on the basis of empirical research, that dividend policy has an impact on the value of the company, but the effect is not automatic according to these studies.<sup>5</sup>

## 1.2 Decision of the Győr Court of Appeal

The facts examined by the Győr Court of Appeal were more complex. The general meeting of the defendant company decided to pay dividends. However, in view of the liquidity situation, the company paid only part of the dividend to the shareholders. In the meantime, some shareholders sold their shares. The buyer of these shares undertook to ensure that the outstanding part of the dividend would be paid to the original shareholders. Subsequently, however, the buyer, who became the sole shareholder of the company, decided to amend the previous decision to pay the dividend and to set the amount of the dividend at the amount already paid by the company. The reason given for the amendment was that the financial situation of the company deteriorated and no longer allowed it to meet the remaining dividend payment obligation. The defendant subsequently entered into voluntary liquidation and the former shareholders sought to enforce their claims in the liquidation proceedings. They identified the right to dividends as their primary cause of action and an unspecified claim under the law of obligations as a secondary cause of action, should the court find that they are not entitled to dividends since they are no longer shareholders of the company.

The court of first instance found that as the plaintiffs are no longer shareholders of the company, they have no right to claim dividends. However, the court found

<sup>3</sup> EBH2009. 1971. The Curia's decisions on principle (in Hungarian: *elvi bírósági határozat, EBH*) were among the Curia's tools aiming to ensure uniform interpretation of the law. The Curia's panel published cases as EBH if they had great importance. The Curia could only deviate from the EBH in matters of law after a special procedure (see Sections 31 and 32(1) *b*) of Act CLXI of 2011 on the Organization and Administration of Courts).

<sup>4</sup> Miller and Modigliani (1961).

<sup>5</sup> For an analysis of the German DAX 30, see, e.g., Melching and Nguyen (2021).

that an atypical obligation with the same content was created at the same time as the termination of the claim for dividends. This obligation cannot subsequently be modified by a company resolution, since obligations can only be modified by the parties' consensus.

The second instance court upheld this judgment, but on different grounds. It argued that Act V of 2013 on the Civil Code ('Civil Code') clearly states that the right to dividends does not cease to exist even if the shareholder ceases to be a shareholder, since the shareholders entitled to dividends are those who were shareholders at the time the decision to pay dividends was taken.<sup>6</sup> The second instance court stated, without any further substantiation, that the company's decision to pay dividends could be subsequently amended, but such an amendment is not effective against those persons who were shareholders when the original decision was taken but were no longer shareholders at the time of the amendment.

### 1.3 Decision of the Supreme Court

Both the Debrecen Regional Court of Appeal and the Győr Regional Court of Appeal referred in their judgments to the judgment of the Supreme Court of Hungary published under EBH2009. 1971. Therefore, before we turn to analysing the legal nature of the right to dividends, it is also appropriate to briefly review this decision.

According to the facts of the judgment, the company decided to pay dividends and subsequently changed its decision. Under the amended decision, the company would pay the dividend only after a longer period had elapsed, but it would pay default interest to the shareholders for the period of the 'delay'. In its application, the plaintiff sought the annulment of that decision in view of the fact that the dividend to be paid to the shareholder would become due immediately. The plaintiff submitted that the time limit for payment of the dividend cannot be subsequently unilaterally modified since the legal relationship between the shareholder and the company concerning the payment of the dividend is determined by the law of obligations, and, therefore, the obligation can only be modified by mutual agreement of the parties. A resolution passed by the general meeting in accordance with the rules on quorum and majority votes required for passing the resolution cannot substitute the creditor's (i.e., the plaintiff's) legal declaration.

In the first instance, the court agreed with the plaintiff's position and annulled the contested decision. The second instance court, however, took a different view. While the court agreed that if the general meeting resolution does not specify a time limit for payment, the dividend becomes due immediately, in the present case, the company had determined when the payment should be made. The resolution provided that the payment of the dividend would depend on the company's economic situation. From this, the second instance court concluded that the company was not

<sup>6</sup> Section 3:262 of the Civil Code.

precluded from subsequently ‘clarifying’ its earlier decision by clearly specifying the time limit for the payment of the dividend to the plaintiff.

The Supreme Court shared the view of the second instance court. Its judgment contained two relevant findings. First, the Supreme Court held, as a rule but without any support, that the adoption of a resolution by the general meeting on the payment of dividends does not transform the company law relationship between the shareholder and the company into a relationship governed by the law of obligations. Second, the Supreme Court also held that

[i]f the resolution of the general meeting does not contain a time limit for payment, the claim immediately becomes due. However, there is no obstacle, in the absence of a legal prohibition to that effect, to make the payment of dividends subject to a time limit, either in the resolution of the general meeting or in the articles of association. Since the decision on the dividend falls within the exclusive competence of the general meeting, the general meeting is not precluded from either annulling or amending its earlier decision and imposing a subsequent time limit for the payment of the dividend or altering the original time limit.

This latter argument is also included in the headnote to the judgment.

Unfortunately, it is not clear from the Supreme Court’s judgment whether the company is entitled to modify the decision only if the dividend is not yet due, or even if it has already become due.

## 2 Right to Dividend v. Dividend Claim

### 2.1 Introduction

The starting point of the judgments cited here is undoubtedly correct: the right to dividends forms part of the broader category of membership rights. The judgments, however, failed to define what they exactly mean by the right to dividends, so in the following analysis, we will first address this question. We will point out that the courts have failed to recognise the difference between the right to dividends as one of the rights to which the members are entitled as part of their membership rights, and the right to dividends as a monetary claim of the member against the company. The failure to make this distinction led the courts to reach the wrong conclusion.

The analysis examines the rules applicable to limited liability companies and companies limited by shares. For ease of reading, a distinction between these two types of companies is made below only where it is essential. The term ‘shareholder’ is used for both companies, and the term ‘member’ includes ‘shareholder’ unless specifically indicated.<sup>7</sup>

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<sup>7</sup> One of the major distinguishing features between these companies under Hungarian law is that only companies limited by shares may issue negotiable instruments representing membership rights (Section 3:11 of the Civil Code). Consequently, limited liability companies do not issue shares, but their business quotas are transferable (Section 3:166-3:167 of the Civil Code).

This paper is not a comparative analysis. Answering the question under consideration does not require an examination of foreign laws. However, on some points, we refer to the solutions of German and English law to support our argument. We do not claim that German or English law solutions are directly relevant in interpreting the content of Hungarian rules, but we believe that these rules provide good support for the criticisms put forward in this article.

As the overview of legal literature will show, in line with the still prevailing position of German law, Hungarian legal literature before World War II considered a claim for the payment of dividends for a given financial year as a contractual claim separate from the dividend right that exists as a membership right. Although this position has been reflected in a recent Hungarian judgment,<sup>8</sup> the majority view seems to disagree with it and regards the right to dividends as a single, uniform right belonging to the field of company law.

Before we dive into this analysis, it seems appropriate to ask whether this is a purely academic debate or whether the answer to the question has practical significance. In this section, we argue that the question is of significant practical importance. Not recognising the distinction between the right to dividend and the dividend claim, and not noticing that upon passing a resolution for the payment of dividends a contractual relationship is established, would have a number of unintended consequences.

First, we point out below that the right to dividends, understood as a membership right, is not transferrable: it belongs to the shareholder, with the content defined by law and by the articles of association. If it were not recognised that the dividend claim is a claim belonging to the sphere of the law of obligations, the dividend claim would not be transferable and no security could be established over this claim. This result would be both wrong from a doctrinal and unfavourable from a commercial perspective.

Second, if it were not recognised that the dividend claim is a claim, it could never become time-barred. Such a consequence would be difficult to explain. Why would any claim against the company be subject to limitation, with the exception of a claim for dividend? German legal literature recognises without controversy that a dividend claim can become time-barred;<sup>9</sup> the general three-year rule of the BGB governs the limitation of dividend claims.<sup>10</sup> We believe that the same should be true under Hungarian law.<sup>11</sup>

Finally, the question of whether the dividend claim belongs to the field of company law or the law of obligations is also relevant to the issue under consideration in the present analysis. The courts have taken the view that a decision of the company's general meeting to pay dividends can be subsequently reversed because it has been argued that the decision does not result in a change in the position of the shareholder. If our reasoning is correct, it must necessarily follow that the judgments

<sup>8</sup> Metropolitan Court of Appeal Gf.40389/2021/4.

<sup>9</sup> Ekkenga (2022), para. 114.

<sup>10</sup> Bayer (2024), para. 112.

<sup>11</sup> The general limitation period under Hungarian law is 5 years (Section 6:22(1) of the Civil Code).

under review here are wrong. If we recognise that upon passing the resolution on the payment of dividend, a contractual claim is created in addition to the membership right, we have to recognise as well that a bilateral relationship is created between each individual shareholder and the company. The content of such legal relationship is nothing more than the right of the shareholder to demand the payment of money from the company and the obligation of the company to provide that service. The company's general meeting is not entitled to deprive the shareholder of this dividend claim, and therefore, a subsequent decision of the general meeting cannot reduce the amount of dividend to which the shareholder is entitled.

## 2.2 The Right to Dividends as a Membership Right

The starting point is clear: membership in companies consists of rights and obligations. The most obvious example of an obligation is the obligation to make a financial contribution upon the establishment of the company,<sup>12</sup> but German legal literature also considers, for example, the obligation of loyalty (*Treupflicht*) as such an obligation.<sup>13</sup>

In addition to their obligations, members also have rights. Some of these rights are non-pecuniary. Examples include the right to vote<sup>14</sup> and the right to information.<sup>15</sup> The other group of rights to which members are entitled consists of pecuniary rights. These rights include the residual right to the company's assets, which, as Nagy points out, 'rests during the life of the company and the individual shareholder cannot recover even the amount he has paid in during its existence', and the right to profits, which 'unlike the former, is vested in the shareholders for the life of the company'.<sup>16</sup>

The Civil Code considers rights as assets, together with things and claims.<sup>17</sup> This classification would imply, among other things, that security can be established over the right to dividends,<sup>18</sup> and the Civil Code also provides, in principle, for the transferability of the right.<sup>19</sup> However, we argue that this is not the case for membership rights in a company.

Let us first look at the transferability of the right to dividends. If this right is considered to be transferable in itself, without the shareholder's complete position in the company, it would follow that, in the event of a transfer, when the company decides to pay dividends, the dividend would go to the assignee. If this is the case, it should also be true in the case of a transfer of a share in the company. The facts in this case are as follows: the shareholder transfers her right to the dividend and then transfers

<sup>12</sup> Section 3:9 of the Civil Code.

<sup>13</sup> See, for example, Koch (2023a), pp 80-85.

<sup>14</sup> Section 3:19 of the Civil Code.

<sup>15</sup> Section 3:23 of the Civil Code.

<sup>16</sup> Nagy (1913), pp 376-377.

<sup>17</sup> Section 8:1(1) subparagraph 5 of the Civil Code.

<sup>18</sup> Section 5:86(1) and 5:101(1) of the Civil Code.

<sup>19</sup> Section 6:202 of the Civil Code.

her share in the company. Who is entitled to the dividend in such a case: the new member or the assignee?

The Civil Code considers the rights conferred on a shareholder of the company as rights which are conferred on the shareholder by the Civil Code and the articles of association. If it were conceivable that the rights regulated as membership rights by the Civil Code and the articles of association did not belong to the shareholder, the acquirer of the share would never know what the content of the share was, since she would not be in a position to identify any previous assignments. This is obviously contrary to the concept of a share as a negotiable instrument, but it also makes it very difficult to transfer business quotas in limited liability companies. The rights and obligations that make up the share or the business quota form an inseparable unit, which means that only the share or the business quota can be the subject of a transfer, and that the individual rights (such as voting rights or dividend rights) cannot be transferred separately. This also applies to creating security over these rights: security can only be established over the company share, but not over the individual rights constituting the company share. In the following, we will point out that, in addition to the right to dividends as a corporate right, the decision to pay dividends creates a claim to a contractual obligation that is distinct from the corporate right. There is, therefore, nothing to prevent the member from creating a security *in rem* on this claim.

The position expressed here is also supported by German legal literature. Together with the residual right of the shareholders exercisable at the liquidation of the company, the right to dividends is a pecuniary right deriving from the membership.<sup>20</sup> The right to dividends, understood as a membership right, is not transferable, as it forms an inseparable part of the membership relationship.<sup>21</sup> The transfer of a share in a company transfers the share to the transferee with the content provided for by law.<sup>22</sup> To put this in terms of public limited companies: the share as a security also embodies the right of the shareholder to receive dividends if the conditions for the payment of dividends are met. This right is non-transferable.<sup>23</sup> However, German legal literature uniformly recognises that the claim becomes transferable after the company's resolution regarding dividends is passed. In such a case, in addition to the abstract dividend right, a claim arises based on which the holder of the claim can demand the payment of the dividend specified in the resolution from the company. This claim can be enforced against the company after it has fallen due and can be freely disposed of by the shareholder, for example, by assigning it.<sup>24</sup> The possibility of pledging the claim is also recognised in the legal literature.<sup>25</sup>

<sup>20</sup> Ekkenga (2022), para. 38; Verse (2022), paras. 9 and 38.

<sup>21</sup> Ekkenga (2022), para. 55; Fleischer (2020), para. 44.

<sup>22</sup> Verse (2022), para. 11.

<sup>23</sup> Koch (2023b), p 369.

<sup>24</sup> For more examples from German legal literature, see Windbichler (2019), p 397; Koch (2021), p 342; Bayer (2024), para. 106. Regarding transferability, see, e.g., BGHZ 65, 230 (234); NJW 1976, 241; Ekkenga (2022), para. 118; Verse (2022), para. 11.

<sup>25</sup> Ekkenga (2022), para. 124.

On the basis of the above, it can be concluded that the right to dividends as a corporate membership right is not transferable on its own. This right merely expresses that if the company has profits and wishes to distribute them, the member may benefit from them. This is also true in general: membership rights (e.g., voting rights, residual rights) are not transferable but are transferred to the new shareholder jointly with the content laid down by law and by the company's statutes.

### 2.3 Decision on the Dividend

The right to dividends under Hungarian law does not automatically create a right for a member of the company to share in the profits of the company in a given year. This requires not only that the company has assets available for dividend payment,<sup>26</sup> but also that the general meeting decides to pay dividends from the assets available for dividend payment.

The Civil Code does not regulate how the general meeting's decision is made. The Companies Act of 2006 expressly stated that the general meeting takes its decision based on the proposal of the management.<sup>27</sup> In contrast, the Civil Code only kept this rule with regard to the decision on interim dividend.<sup>28</sup> Kisfaludi argues that this is the result of a deliberate change:

The Civil Code omits the provision that dividend payments are made upon the proposal of the executive management. However, this does not mean that the management cannot make a proposal regarding the distribution of the after-tax profit. Nevertheless, such a proposal does not have binding or limiting force. The general meeting is free to decide even contrary to the proposal of the management.<sup>29</sup>

This dual requirement requiring available assets for distribution and a decision of the general meeting is clearly expressed in the Civil Code.<sup>30</sup>

This may also seem evident from Act XXXVII of 1875 on the Commercial Code (hereinafter: Commercial Code), which regulated companies limited by shares.

Section 163 of the Commercial Code laid down the main rule of capital maintenance: 'The amount paid by the shareholders may not be reclaimed by the shareholder ..., during the life of the company the shareholder may claim only the net profit which is distributed among the shareholders in accordance with the articles of association'. In accordance with the provisions of Section 165 of the Commercial Code, '[n]o interest or dividend shall be paid to the shareholders out of the share

<sup>26</sup> For the common rules for companies, see Section 3:88(2) of the Civil Code; in the case of limited liability companies, see Section 3:184(1) of the Civil Code; and in the case of companies limited by shares, Section 3:261(1) of the Civil Code.

<sup>27</sup> Section 132(2) of Act IV of 2006.

<sup>28</sup> Sections 3:186(2) and 3:263(2) of the Civil Code.

<sup>29</sup> Kisfaludi (2020), p 454.

<sup>30</sup> In the case of limited liability companies, Section 3:185(1) of the Civil Code; in the case of joint-stock companies Section 3:262(1) of the Civil Code.

capital; only such of the net profits as remain in the annual balance sheet shall be distributed to the shareholders’.

Initially, legal literature also interpreted the Commercial Code as meaning that shareholders do not have an ‘automatic’ right to dividends:

The law thus, on the one hand, expressly declares the right to dividends, but on the other hand, it expresses that the shareholder has no general claim to the net profit as a whole, but only to the extent that it is distributed among the shareholders in accordance with the articles of association.<sup>31</sup>

Interestingly, the judicial practice of the Commercial Code in the early 20th century diverged from the strict meaning of the legal norm.

In a case published in 1915, the Curia analysed an article of association that provided that a certain part of the profit shall be used as reserves while the remaining part shall be paid as dividends. The question emerged as to whether the general meeting has the right to deviate from this provision. The Curia stated that

if the articles of association stipulate that 5% of the profits shall be used to increase the reserve fund and the remaining amount shall be distributed among the shareholders, it creates a mandatory provision. In so far as the company’s statutes so provide, the general meeting shall not be entitled, by a majority decision, to make any other disposition of the income.<sup>32</sup>

A decision of the Curia published in 1929 raised an even more interesting question. The articles of association provided that the general meeting has the right to decide about the distribution of profits. The provision stipulated that ‘of the annual net profit, 5% shall be allocated to the reserve fund, 10% to the directors’ remuneration and 2% to the remuneration of the officers’, while ‘the remaining net profit shall be decided by the general meeting on the proposal of the board of directors without any limitation’.<sup>33</sup>

The Curia, starting from the consideration that ‘the shareholder invests his money in shares in order to increase the value of his capital’, found the quoted provision of the articles of association to be unlawful, because it ‘leaves it to the discretion of the general meeting, free of any limitation, to decide whether to pay dividends to shareholders in such cases, where the payment of dividends is not prevented for any reason which is in the company’s interest, whereby a majority which is unable to enforce its calculations in the company without any other means could deprive a minority interested solely in the income from its shares of the fruits of its capital invested without any justifiable reason and could, in consequence, depreciate its shares in the market, despite their intrinsic value.’<sup>34</sup>

<sup>31</sup> Rapoch (1915), p 7.

<sup>32</sup> Decision of the Curia P. II. 7193/1915 of 21 October 1915.

<sup>33</sup> Decision of the Curia P. IV. 5796/1929 of 22 October 1929, quoted by Fenyves (1930), p 15.

<sup>34</sup> Fenyves (1930), p 15.

In the interpretation of the legal literature, in this judgment, the Curia stated that the Commercial Code provided an obligation to pay dividends. This was also the basis for the criticism of the decision. Authors argued that the Commercial Code does not impose any obligation to pay dividends but merely sets a ceiling on the dividend, leaving it up to the shareholders to decide whether to pay dividends and, if so, within the limits set by law, how much dividend to pay.<sup>35</sup>

In Ödön Kuncz's view, shareholders are essentially free to decide whether to pay dividends. He added, however, that the decision should not be taken arbitrarily by a majority of the shareholders.

Any shareholder may challenge in court a resolution of a general meeting which (a) provides for dividends contrary to the company's goals (e.g. in the case of a public limited company formed for profit, excludes shareholders from a share in profits), (b) modifies without justification the provisions of the articles of association establishing the right to dividends, or (c) is generally based on an unjust and immoral basis (e.g. the majority limits the right to dividends purely in order to exclude the minority from the company).<sup>36</sup>

Others emphasised the unviability of the requirement set by the Curia's judgments:

Whether, however, in the specific case where the balance sheet profit is available for the purpose of paying dividends, it is possible and advisable for the company limited by shares to pay dividends, whether this dividend payment does not affect the liquidation of the company, whether the appropriation of profits for dividends is not premature in view of pending and unaccounted transactions, whether the appropriation of one or another reserve is justified, etc., etc., this, in my opinion, is an important problem of the economic existence of a company limited by shares, which cannot be legislated for, and in particular cannot be so legislated for as the practice of some company courts have recently sought to require, that is, that the articles of association should lay down in a fixed figure the amount of the net profit, after deduction of the amounts used for statutory purposes, to be distributed to shareholders as dividends.<sup>37</sup>

Despite these criticisms, however, the Curia's case law seems to have recognised shareholders' right to receive dividends if profit is available.

## 2.4 *Dodge v. Ford Motor Co.*

To provide a comparison, it is worth exploring how the Michigan Supreme Court addressed the question of whether a shareholder has a legally enforceable right to have the company pay at least part of the profits to the shareholders. In the 1919 case

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<sup>35</sup> Ibid.; Oppler (1917), p 93.

<sup>36</sup> Kuncz (1928), p 399.

<sup>37</sup> Kohner (1930), p 54.

of *Dodge v. Ford Motor Co.*,<sup>38</sup> decided at the same period as the above-quoted decisions of the Hungarian Curia, the court was asked to rule on the following injunction. Ford, incorporated in 1903, had accumulated substantial annual profit due to its successful operations. While the company paid high dividends on its stock, it used the accumulated profits to devote significant resources to, among other things, the company's employees and to continually reduce the price of its cars to make its product available to the widest possible range of people. The majority of the company's shares were owned by Henry Ford, who was also the company's CEO. The minority shareholders were the Dodge brothers, who, in 1913, went into the car business themselves. In 1915, the management decided to change its dividend policy. Whereas until then, the company had paid a quarterly dividend of 5% of the nominal value of the shares per share, in addition to a substantial extraordinary dividend, the company's management abolished the extraordinary dividend. The reason given by the management for this measure was that they wanted to use this profit to further reduce the price of their cars and to build a new factory.

Dodge asked the court to prohibit the company from building the planned new factory and to order it to pay the extraordinary dividend based on its previous dividend policy. The court granted the request. On Ford's appeal, the Michigan Supreme Court partially reversed the judgment: the court upheld the decision with respect to the dividend payment but changed it regarding the proposed factory. This second issue is of little relevance to this writing, so we simply note that the court was mindful in this regard that courts are not economic experts, and therefore the management should have almost complete discretion in the company's business affairs.

In relation to the payment of dividends, the court acknowledged that the management is free to decide whether to pay dividends to shareholders. If it decides not to pay out the profits but to use them to make new investments, the shareholders cannot ask the court to order the management to pay dividends. It is perhaps surprising how the court could still order Ford to pay dividends. The reason was that Ford made a number of statements in his testimony in which he made it clear that the company had already paid so many dividends to its shareholders that it was necessary for the company to share its profits with society as well as its shareholders. It was this altruistic attitude that led the court to conclude that Ford's management had breached its duty to operate the company in the interests of its shareholders.<sup>39</sup>

So, contrary to the conclusion of the Hungarian Curia, the Michigan Supreme Court's judgment made it clear that shareholders are entitled to dividends only if the corporate body entitled to decide on the payment of dividends has decided to pay dividends. Otherwise, except in the exceptional situation of *Dodge v. Ford Motor Co.*, the shareholders of the company are not in a position to compel the payment of dividends. This is undoubtedly true in the contemporary Hungarian legal context: even if the company makes a profit, if the general meeting does not decide to pay dividends,

<sup>38</sup> *Dodge v. Ford Motor Co.*, Supreme Court of Michigan, 204 Mich. 459, 170 N.W. 668 (1919).

<sup>39</sup> The judgment of the Supreme Court describes the facts and the testimonies of the witnesses in a fascinating and very detailed manner. For the economic background to the judgment, see Bainbridge (2023), pp 27–36.

the member of the company, despite the right to dividends, will not become entitled to demand payment of dividends from the company.

## 2.5 What Is the Effect of the General Meeting's Decision on Dividends?

We have argued above that the right to dividends as a right of membership of a company does not in itself give rise to an enforceable claim against the company. The earliest point in time when such an enforceable right may arise is when the general meeting passes a resolution on the payment of dividends. We will now examine whether the general meeting's resolution indeed creates such an enforceable right and, if so, what its legal nature is.

The three recent Hungarian judgments described above have undoubtedly agreed on one issue: the decision to pay dividends does not create a legal relationship between the company and the member governed by the law of obligation. Unfortunately, as already indicated above, none of the courts has explained the basis on which it reached this conclusion, which is fundamentally at odds with the approach of both Hungarian law before World War II and German law.

German legal literature recognises that a resolution on the payment of dividends creates a claim independent of the shareholder's membership right. The legal fate of this claim must be examined according to the rules of contract law, not company law. This is not a company law claim but a classical contractual claim.<sup>40</sup> The German legal literature also analyses the possibility of the shareholders' meeting to amend a decision on dividends and takes the same position as expressed above: 'A company resolution to terminate or reduce the right to dividends would not only be unlawful and null and void, but would be ineffective as a matter of law'.<sup>41</sup> In order for the resolution to be subsequently reversed, it is first necessary that the shareholders waive their dividend claim.<sup>42</sup> The case law on this issue is also clear. For example, in a 1957 decision, the German Bundesgerichtshof ruled that the right to dividends is a membership right in a company, which is converted into a creditor's claim by a resolution on the distribution of profits, and can only be taken away from the individual shareholder with the shareholder's consent.<sup>43</sup>

Although the question has not been the focus of legal literature, it can be stated with certainty that Hungarian private law before World War II was also of the view that the right to dividends forming part of the category of membership rights should be distinguished from the claim for the payment of dividends for a given year. In the analysis below, we refer to the right to dividends as a right belonging to the sphere of company law and the dividend claim as belonging to the sphere of the law of obligations that comes into existence when a resolution for the payment of dividends is passed.

<sup>40</sup> See, e.g., Bayer (2024), para. 103; Verse (2022), para. 10; Ekkenga (2022), para. 75.

<sup>41</sup> Ekkenga (2022), para. 75; RGZ 87, 383, 387 and RGZ 167, 65, 68; Vetter (2021), p 1922.

<sup>42</sup> German Civil Code § 397; Verse (2022), p 70.

<sup>43</sup> BGHZ 23, 150 (154), NJW 1957, 588.

Győző Nitsche, examining the rule of the Commercial Code, considered it undisputed that the shareholder has a dividend claim, which he formulated as a creditor's right against the company. For him, the only question was when this dividend claim arose: when the general meeting's resolution was passed or even before that.<sup>44</sup> He argued that it follows from the rules of the Commercial Code that the dividend claim arises when the profits are declared: 'that the dividend under the articles of association, whether or not the general meeting has decided on the distribution, confers a creditor's right on the shareholder'.<sup>45</sup>

The shareholder becomes a creditor in respect of the dividend—that is to say, a third party—as soon as the balance sheet and the profit have been established, over whose rights the general meeting can no longer legally dispose of, or, if it has disposed of, this means nothing more than if it decided, for example, not to pay an undisputed claim of the seller of goods.<sup>46</sup>

We agree with this conclusion. Once we recognise that the general meeting's resolution on the payment of dividend creates a dividend claim that is not part of the membership rights of the shareholders, but a claim to which the law of obligations applies, we can only come to the conclusion that such a right cannot be taken away or amended by a subsequent decision of the general meeting. The reason for this is straightforward: the obligation exists between the company as debtor and the shareholder as creditor, and the decision of a third party can have no effect on this obligation.

It seems that the Budapest Court of Appeal has also taken a position contrary to that of the Curia in a recent case.<sup>47</sup> According to the facts, the shareholder had to request payment of the dividend within a certain period of time after the resolution on dividends was passed. As the shareholder failed to prove that he had requested payment, the court dismissed the action. However, the judgment contains a sentence relevant to the present analysis:

The shareholder is entitled to a dividend right which is an abstract property right under the provisions of the Companies Act. Upon the adoption of the general meeting's resolution this right transforms into a due shareholder claim for dividend subject to the conditions which may be further specified in the resolution of the general meeting or in the articles of association and an obligation on the part of the company to pay the dividend.<sup>48</sup>

Interestingly, while this was not the primary issue in the dispute, the court emphasised this finding as the headline of the judgment. If we understand it correctly, the

<sup>44</sup> Nitsche (1914), p 454; Kuncz (1913).

<sup>45</sup> Nitsche (1914), p 457.

<sup>46</sup> *Ibid.*, p 461.

<sup>47</sup> Metropolitan Court of Appeal Gf.40389/2021/4.

<sup>48</sup> The case was decided under Act IV of 2006 on the Companies Act. The Companies Act has since been repealed, and its rules have been incorporated into the Civil Code. The relevant rules have remained the same, and therefore, the court's arguments are also relevant under the existing legal framework.

Budapest Court of Appeal stated, in its judgment, the same as we are arguing: apart from the right to dividends, which is regulated as a membership right, when the general meeting passes its resolution on the payment of dividends, a claim enforceable against the company is also created.<sup>49</sup>

The fact that this right is of a contractual nature is also supported by the Civil Code's rule,<sup>50</sup> which stipulates that the dividend claim is conferred on the shareholder who is entitled to exercise the membership rights at the time when the resolution on the payment of dividends is passed. This rule means that if the shareholder transfers her shares after the resolution but before the dividend is paid, the company will pay the dividend to the original shareholder even though she is no longer a shareholder at the time the payment is made. By this rule, the legislator recognises that the dividend claim is not a membership right linked to the shareholder, but a claim independent of the membership rights.<sup>51</sup>

## 2.6 Conclusions: The General Meeting's Resolution Creates an Enforceable Individual Right for the Shareholders

In the introduction, we asked the question of whether our analysis has any practical relevance. We came to the following conclusions.

First of all, it should be pointed out that it is not clear what arguments can be used to support an argument that does not recognise that the decision to pay dividends creates a monetary claim between the member and the company. The company's resolution on dividends is nothing other than a decision that obliges the company to pay its shareholders a certain amount of money.<sup>52</sup> If we did not recognise that this resolution creates an obligation between the company and its members, then, in the event of non-payment of the dividend, the claim would only be enforceable under the rules of company law. As company law typically does not allow individual shareholders to enforce claims against the company, it is difficult to see how the shareholders could enforce their right to dividend. The company's resolution entitles the individual shareholder to dividends, so it does not seem logical that the claim cannot be enforced by the creditor (i.e., the shareholder) independently. We argue that once the general meeting's resolution on the payment of dividend is passed, the shareholder's claim is not different from the shareholder's claim for the repayment of a loan the shareholder provided to the company. Both claims are governed by the law of obligations and both can be enforced individually by the shareholder.

Second, we showed that shareholders do not have an enforceable right to dividend. Such a right requires that the company has distributable assets and the

<sup>49</sup> This also means that if the company becomes insolvent after a resolution on the payment of dividend is passed, the shareholders will have an enforceable creditors' claim against the insolvent company. These claims are enforceable according to the insolvency waterfall rules (see Section 57(1) of Act XLIX of 1991 on Insolvency and Bankruptcy Procedures).

<sup>50</sup> Section 3:185(1) of the Civil Code.

<sup>51</sup> András Kisfaludi takes the same view, see Kisfaludi (2007), p 404.

<sup>52</sup> The present study focuses on cash dividends and does not examine the issue of non-cash dividends.

shareholders decide to pay dividend. If the shareholders do not pass a resolution on the payment of dividends, the shareholder cannot claim dividend from the company.

The third and most important argument we made was that the right to dividend as part of other membership rights is not transferable and no security can be established over it. However, upon the general meeting's decision on dividends, in addition to the right to dividend as part of the shareholders' membership rights, a claim is created. This obligation exists between the company as debtor and the individual shareholders as creditors. As this claim exists between the company and the individual shareholders, the general meeting has no authority to amend this claim; therefore, a subsequent amendment of the general meeting's resolution should have no effect on this dividend claim.

### 3 Due Date of the Dividend Claim

We have argued above that when a resolution on the payment of dividends is passed, a dividend claim is established that is governed by the law of obligations. We have shown that the recognition of the contractual relationship is essential as it creates an enforceable claim against the company, which the member is now free to dispose of. However, one important question has not been addressed: when does the dividend claim become due? The answer to this question determines the moment when the member can take legal action if the company fails to meet its dividend payment obligation.

#### 3.1 The Solution and Judicial Practice of the Companies Act

The Companies Act regulated the payment of dividends partly differently from the Civil Code. In the case of both limited liability companies and companies limited by shares, the rule was that no dividend could be paid if the company's equity capital, as adjusted in accordance with the Accounting Act, did not reach or would not reach the company's share capital as a result of the payment.<sup>53</sup> In the case of limited liability companies, the Companies Act contained a further rule that required the director to declare in writing that the payment would not jeopardise the company's solvency or the interests of creditors.<sup>54</sup> In the case of companies limited by shares, such a declaration was only required if the articles of association contained such a provision.<sup>55</sup> The damage caused by the failure to make a payment or by making an untrue statement gave rise to the liability of the director. According to the interpretation of the Supreme Court, when making a declaration,

<sup>53</sup> Section 131(1) (limited liability company) and Section 219(1) (public limited company) of the Companies Act.

<sup>54</sup> Section 131(3) of the Companies Act.

<sup>55</sup> Section 219(2) of the Companies Act.

the managing director must take into account, in addition to the balance sheet data, the company's liquidity situation at the time of the general meeting at which the decision to pay dividends is taken, since only on that basis can he take a position on the effect of the payment on the company's solvency.<sup>56</sup>

There are several problems with the Companies Act's rule. It is difficult to find a legal policy reason to explain why such a declaration is required in the case of limited liability companies if it is only optional in the case of companies limited by shares. More importantly, however, the Companies Act has failed to state the substantive rule that payment must be refused if this would jeopardise the company's solvency. This obligation on the part of the management can only be derived indirectly from the rule. Put another way, the Companies Act did not require by a positive rule that the director should pay the dividend only if the payment would not jeopardise the company's solvency, but if he paid without having made a prior declaration or if he made a false declaration, he was liable for his conduct.

While the first two problems are essentially codification technicalities, the third problem concerns the substance of the rule. Dividends are decided by the company when it adopts its accounts.<sup>57</sup> The rules ensuring payment to the member are, by definition, creditor protection rules,<sup>58</sup> whose primary function is to ensure that the assets of the company—to put it somewhat simplistically—do not fall below the registered capital.<sup>59</sup> There is no doubt that the payment of dividends worsens the position of creditors. However, the reason why the legislation allows the payment of dividends is that the company's creditors have always had to consider that the profits made by the company are taken out of the company by its members. This would not result in an unfair situation for creditors, as when they became creditors of the company, the subsequent profits were not yet part of the company's assets and could not be factored in when assessing the risk of lending.

Returning to the question of the due date of the dividend claim, the Supreme Court, interpreting the rules of the Companies Act, held that if the general meeting does not set the date of payment of the dividend, it is due immediately.<sup>60</sup> In this context, the court referred to Section 7(1) of the Companies Act, which stated that if the GTC does not set a time limit for the making of a declaration or the performance of an act, the declaration or act must be made without delay. This interpretation is

<sup>56</sup> BH2018. 201 (BHs are selected judgments of the Supreme Court or the Curia). The same argument is found in an arbitral award, see Haitsch (2003).

<sup>57</sup> Sections 132(2) and 220(3) of the Companies Act. In the case of a limited liability company, the same rule is laid down in Section 3:185(2) of the Civil Code. In the case of joint-stock companies, there is no rule that the general meeting may decide on dividends at the time of the adoption of the annual accounts, but it can be inferred from the rule that the board of directors may decide on dividend advances between two consecutive annual accounts (Section 3:263(1) of the Civil Code) that dividends may only be decided upon at the time of the adoption of the annual accounts.

<sup>58</sup> For an example, see Davies (2020), p 251.

<sup>59</sup> See Article 56 and related Recital 40 of Directive (EU) 2017/1132 of the European Parliament and of the Council on certain aspects of company law.

<sup>60</sup> BH2018. 201.

also in line with German legislation,<sup>61</sup> which provides that dividends are due immediately in the case of GmbHs,<sup>62</sup> and on the third working day following the general meeting's decision<sup>63</sup> to pay dividends in the case of companies limited by shares.<sup>64</sup>

We note that it is difficult to answer the question of whether the due date of the claim is determined by the Companies Act or the Civil Code. The difficulty of the question arises from the fact that the company's resolution creates the obligation to pay, thus giving rise to the application of the company law rules, but at the same time, as pointed out above, the resolution creates an obligation and the question is about the maturity of that obligation, which gives rise to the application of the rules of the law of obligations. We are inclined to think that the correct application in this context is the application of the rules of company law, since it is company law that is responsible for determining the conditions under which dividends are due to members. Thus, for example, if the articles of association lay down a rule on the maturity of dividend payments, this cannot be overridden by the Civil Code's rule on the due date of obligations.<sup>65</sup> However, this issue is of little relevance in the sense that the two rules should lead to the same result, as the company law rule lays down the obligation to perform without delay,<sup>66</sup> whereas the law of obligations imposes the obligation to perform after the time necessary for the preparation of the act has elapsed.<sup>67</sup> Although the wording is different, we believe that the requirement is identical in substance, since the decision to pay dividends cannot come as a surprise to the management, which must be ready to perform immediately.

### 3.2 The New Rule of the Civil Code and Its Possible Interpretations

The Civil Code changed the Companies Act's rule described above and provides a positive rule for both types of companies that payment must be refused if it would jeopardise the company's solvency.<sup>68</sup> The change is undoubtedly correct in the sense that it remedies the problems that arose from the Companies Act described above. It removes the unjustified distinction between limited liability companies and companies limited by shares, and provides, not only indirectly, by deduction from the liability rule, but also by a positive rule, that no payment may be made if it would jeopardise the company's solvency. However, the new rule raises the important question of when the dividend claim becomes due. In our view, there are two ways of answering this question, but both interpretations are problematic.

<sup>61</sup> There is also no requirement for solvency protection in the UK Companies Act (see Sections 830-831 of the Companies Act (2006)).

<sup>62</sup> Ekkenga (2022), para. 90.

<sup>63</sup> AktG § 174.

<sup>64</sup> AktG § 58(4).

<sup>65</sup> For a contrary view, see Metzinger (2021), p 350.

<sup>66</sup> Section 3:91(3) of the Civil Code.

<sup>67</sup> Section 6:35(3) of the Civil Code.

<sup>68</sup> Sections 3:184(1) and 3:261(1) of the Civil Code.

According to the first interpretation, under the new rule of the Civil Code, the decision of the Supreme Court quoted here, according to which the dividend becomes due immediately, cannot be upheld. This interpretation may be based on the fact that the Civil Code has made the payment of dividends *conditional* on the company's solvency not being jeopardised. Two major problems can be identified with this interpretation. The first is that it is uncontrollable for the member when the claim is due. The member is not in a position to determine the impact of a particular payment on the company's liquidity. The second problem is that the threat to solvency is not a static but a dynamic issue. It is possible that at the time of the decision on the dividend, a situation may already exist where the payment threatens solvency. It is also possible that, although the decision is made at a time when the payment would not jeopardise the company's solvency, for some reason the payment is not made. By the time the shareholder goes to court, the payment may already jeopardise solvency. Such a dynamically changing situation cannot be conceptually interpreted in the context of the due date. A claim is either due or it is not, but it is not possible to recognise that the maturity of a claim changes, and a claim that became due, later becomes undue. This interpretation can, therefore, be rejected.

The second interpretation is that solvency is not a maturity issue. Under this interpretation, in line with the aforementioned decision of the Supreme Court, the dividend claim becomes due upon the adoption of the decision, but under the Civil Code, the payment of the due claim is not possible when it jeopardises the solvency of the company. This is, therefore, an objection which temporarily prevents the enforcement of the claim. This temporary nature does not, of course, alter the fact that the company is liable to pay default interest from the due date. It also allows members to enforce their claim in court. If the company, as a defendant, claims that its solvency does not allow it to pay and proves this claim in the lawsuit, the court will dismiss the claim but otherwise will order the company to pay the dividend. The fundamental problem with this interpretation is that it recognises as due a claim that is temporarily unenforceable, whereas being due means that the claim is enforceable. This interpretation, therefore, does not seem to fit easily into the civil law system.

Unfortunately, both interpretations seem problematic. Two logical solutions are possible: (i) to recognise that the rule that takes into account the company's solvency when paying dividends is flawed and thus propose to abolish it, or (ii) to try to create a coherent system by choosing the less problematic of the two options presented above.

### 3.3 Is It Justified to Check the Solvency of the Company at the Time of Payment?

First, we examine whether the rule in the Civil Code that no payment may be made if it jeopardises the company's solvency is justified. Such a case is easily conceivable. For example, even if there is a profit according to the previous year's figures, it is possible that by the time a decision is taken, the financial situation of the company has changed in such a way that the payment would jeopardise the company's solvency. It is also possible that the articles of association stipulate that the dividend

must be paid within a certain period of time following the date of the general meeting of the company's governing body and that the financial situation of the company may change within that period of time in such a way that the payment of the dividend would jeopardise the company's solvency.

In such a situation, two types of rules can be envisaged: the payment can be made irrespective of the situation of the creditors, or the payment to shareholders can only be made if the payment does not jeopardise the solvency of the company. The argument in favour of the former is that, as already explained above, the creditors have always been aware that a dividend payment could be made; so, the creditors must bear the risk that a legitimate dividend payment could lead to the company's insolvency and that in such a situation the shareholders would rank ahead of the creditors. The other interpretation is based on the premise that, as pointed out above, the dividend claim is nothing more than a claim by the shareholders on the company. The insolvency rules do not recognise a situation where, in the event of liquidation of the company, the claim of the shareholders of the company ranks ahead of the claims of the creditors of the company.<sup>69</sup> In such a case it may be appropriate to subordinate the dividend claims of the shareholders of the company and to favour the creditors by ensuring that the dividend is paid only if the payment does not jeopardise the solvency of the company.

There is no 'right' answer to this policy question. We do not see any compelling argument to justify the preferential treatment of shareholders and, therefore, consider it correct that the Civil Code expressly provides for the requirement of solvency as a condition for payments to shareholders.

It is interesting to note that a review of English company law has suggested that a similar rule should be enshrined in the Companies Act. The Company Law Review's suggestion was that the Companies Act should state that if there is an adverse change in the financial position of the company between the adoption of the annual accounts and the declaration of a dividend, the dividend payable under the accounts should be reduced in light of that change. Ultimately, the Companies Act (2006) does not contain the proposed provision, but this does not alter the fact that if the directors propose to pay the full dividend payable under the accounts in such circumstances, this may give rise to liability on the part of the directors.<sup>70</sup>

### 3.4 Can the Threat to Solvency Be Examined in the Context of the Maturity of the Claim?

Since the above leads us to the conclusion that the rule of the Civil Code which requires that no payment be made if the payment would jeopardise the company's solvency is correct, it is necessary to choose between the two options outlined above. The first solution makes the requirement that the payment does not jeopardise

<sup>69</sup> Cf., Section 57(1) *f* and *h* of Act XLIX of 1991 on Bankruptcy and Winding-up Proceedings.

<sup>70</sup> Davies and Worthington (2016), p 286.

the solvency of the company a condition of the due date, whereas the second solution examines this in the context of the payment rather than the due date.

As we have pointed out above, the problem necessarily inherent in the first solution is that the claim is sometimes due and sometimes not, depending on the solvency of the company. In our view, this solution is not applicable, as a claim has either become due or not, but it cannot fluctuate.

The second interpretation recognises that the dividend claim becomes due when the decision is taken, but taking into account creditor protection considerations ensures that dividends already due cannot be paid if this would jeopardise the company's solvency. The disadvantage of this solution, as pointed out above, is that it handles a claim as due, even though in the event of an adverse change in the company's financial situation, the claim cannot be enforced. However, it has the advantage of striking the right balance between the interests of shareholders and those of non-shareholder creditors. The creditor is protected by the rule that prevents payment if this jeopardises the company's solvency, but the shareholder is protected by the fact that the dividend claim is due from the date of the dividend resolution, so members are entitled to interest until the dividend is paid.

Both solutions outlined here are problematic. However, we believe that the second solution, which considers the problem of whether the company has the necessary funds to pay dividends in terms of payability rather than maturity, leads to a more workable solution overall.

## 4 Summary

This paper has pointed out that court decisions that recognise the possibility for a company's general meeting to subsequently change a dividend decision that has already been taken, are wrong.

The adoption of the resolution regarding the payment of dividends creates a dividend claim between individual shareholders and the company, whereby the shareholder can claim payment of the dividend from the company under the traditional rules of the law of obligations. The Civil Code does not grant the general meeting the right to change the resolution on dividends and reduce the amount of dividends to which the shareholders are entitled.

Finally, we examined the question of when the dividend claim thus defined arises and argued that it becomes due immediately upon the adoption of the company resolution. If the payment of the dividend jeopardises the company's solvency, it should not be paid. However, this only provides the company with a temporary exemption during which the member's dividend claim against the company will accrue interest, so that once solvency is restored, the company will be liable to pay the dividend as set out in the resolution, together with interest.

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