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# The Legal 500 Country Comparative Guides

## Hungary

# AVIATION FINANCE & LEASING

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This country-specific Q&A provides an overview of aviation finance & leasing laws and regulations applicable in Hungary.

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# HUNGARY

## AVIATION FINANCE & LEASING



### 1. What international aviation conventions has your jurisdiction signed and/or ratified?

- The 1933 Convention for the Unification of Certain Rules Relating to the Precautionary Arrest of Aircraft (the 1933 Rome Convention);
- The 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention);
- The Chicago Convention of 1944 on International Civil Aviation (the Chicago Convention);
- The 1948 Convention on International Recognition of Rights in Aircraft (the Geneva Convention);
- The 1999 Convention for the Unification of Certain Rules relating to International Carriage by Air (The Montreal Convention)

### 2. If your jurisdiction has signed and ratified the Cape Town Convention: a. Which qualifying declarations (opt-in and opt-out) has your jurisdiction made under the Cape Town Convention? b. Does the Cape Town Convention take priority over conflicting national law?

N/A

### 3. Will a court uphold the choice of a foreign governing law in respect of the following contracts and if so, please also state any conditions or formality requirements to this recognition a. Lease and b. Security document (for example, mortgage)?

#### a. Lease

A validly stipulated foreign choice of law in respect of a lease agreement is generally upheld by Hungarian courts.

Conflicts Law and the Rome I Regulation confer on the parties to an international contractual transaction almost total autonomy in choosing the law which is to govern such a contract, provided that the presence of a “foreign” (i.e. non-Hungarian) element in the transaction can be proven, e.g. at least one of the parties is a non-Hungarian resident.

#### b. Security document (for example, mortgage)

It is untested how a Hungarian court would proceed with the recognition and enforcement of a foreign court judgment relating to the enforceability of a foreign law governed mortgage or other similar security interest over an aircraft.

Given the practical as well as legal risks, creditors usually opt for having a Hungarian law mortgage.

Under Hungarian conflicts law, Hungarian courts have exclusive jurisdiction over (i) procedures relating to the registration of rights, facts and data in authentic registries kept in Hungary (e.g. the aircraft registry), or (ii) domestic enforcement procedures. In the absence of judicial practice, it is unclear what is the exact scope of the reference to “domestic enforcement procedures” and thus there is a risk that a Hungarian court would find its exclusive jurisdiction on the basis that aircraft is registered in Hungary and flies under the national flag.

Hungarian conflicts law prescribes that the “in rem” rights attached to an asset (e.g. the creation, maintenance and termination of a mortgage) shall be governed by the law prevailing on the location of such asset. In case a (non-Hungarian law governed) mortgage is registered in the aircraft registry, the enforcement of the mortgage in respect of an aircraft registered in Hungary could be challenged by the mortgagor or any affected third parties e.g. on the basis that the mortgage was not in compliance with mandatory Hungarian laws applying to mortgages.

**4. Please confirm whether it is (i) customary and (ii) necessary to also take a local law mortgage and if so, why?**

As

- i. Hungary is not a party to the Cape Town Convention, and the
- ii. enforceability of a foreign law governed aircraft mortgage is untested under Hungarian law (see more in detail under B 3. b),

it is market practice and customary to take a local law mortgage in respect of Hungarian registered aircraft to ensure the enforceability.

**5. Are foreign judgments recognized and enforceable by courts of your jurisdiction and if so, please also state any conditions or formality requirements to this recognition (for example, do you require a local court order confirming such recognition)?**

A judgment taken by a foreign court in proceedings should be recognised and enforced by a Hungarian court, insofar as such judgment:

- is not contrary to public policy in Hungary;
- complies with the requirements relating to the form and content of foreign judgments as set out in Hungarian law; and
- the jurisdiction of such foreign court was stipulated by the parties in the manner prescribed by Hungarian conflicts law.

In the event that any party to the transaction documents seeks to enforce its rights before the courts of Hungary, all relevant transaction documents need to be translated into Hungarian.

**6. Is your aircraft registry an owner-register (registering ownership interests) or an operator-register (registering interests as operator)? Please also state any conditions, procedural steps or formality requirements for such registration and explain how this is evidenced (for example, the issuance of a Certificate of Registration)**

The Hungarian aircraft registry is an owner-register.

The Hungarian Aviation Authority (“CAA”) requires certain documents for registration of aircraft as follows:

- the original documents certifying the ownership of the aircraft and the legal grounds of being registered as lessee in case of the lessee;
- an original official document that certifies the existence of the lessor and representation rights;
- signatory specimen signatures; and
- powers of attorney.

All documents are to be presented in Hungarian (accompanied by Hungarian translation). Documents should be originals or notarised copies and be legalised in the country in which they were signed.

**7. Is there a security document register in your jurisdiction where a mortgagee’s interests will be recorded? If so, please also state any conditions, procedural steps or formality requirements for such registration and explain how this is evidenced (for example, the issuance of a certificate or official stamp on the security document)**

A mortgagee’s interests in respect of aircraft are registered with the Hungarian Aircraft Registry and indicated on the certificate of registration of the relevant aircraft. Security interests over engines are registered separately with the Security Interest Register.

**8. What is the effect of registration of: a. Ownership interest (for example, proof of title to third parties of ownership) b. Lease (for example, perfects the status of the Lessor under the Lease) c. Security document (for example, secures priority over later registered security). If there are any interests that could rank prior to the security document please state these**

- a. The registration has declarative effect, i.e. the Hungarian Aircraft Registry evidences the existence of the owner’s title to the aircraft, but does not create it.
- b. The registration has declarative effect, i.e. the Hungarian Aircraft Registry evidences the existence of the lessor’s title to the Aircraft, but does not create it. A statutory presumption is established that the person so

registered is the lessor. The presumption is rebuttable, but in such cases the person making such a challenge must demonstrate that the information registered in the registry is inaccurate.

c. Mortgage created in a Hungarian law governed security document over aircraft is perfected upon registration in the Hungarian Aircraft Registry.

### **9. What types of lease are recognized in your jurisdiction (for example, translation, notarization, apostille, legalization etc.)?**

The lease agreement under which the aircraft will be operated is registered in the course of the process of registering the aircraft with the Aircraft Register. In practice, notwithstanding the above, in order to avoid the need for obtaining a costly official translation of the lease agreement, the CAA accepts a short form, bilingual or officially translated joint declaration, executed by the relevant parties and submitted to the CAA together with the copy of the lease in its original language.

The lease needs to meet the following basic requirements: it should include valid governing law and jurisdiction clauses, and it should duly identify the lessor and lessee, the leased asset and the consideration for the transaction.

### **10. What formalities are required to perfect Lessor's rights under a lease in your jurisdiction?**

Registration of leases is mandatory, as the CAA needs to see all the interested parties and the legal relationships between them, and in particular, the legal grounds of registration and operation of the aircraft by the lessee in Hungary. As there is no separate register for leases, a lease will be registered in the course of the aircraft registration procedure in case of a new aircraft. In the event of a title transfer, the new lease agreement or transferred novated (as applicable) will be registered simultaneously with the new owner.

### **11. Are the ownership rights relating to engines recognized as separate and distinct from the ownership of the rest of the aircraft in your jurisdiction? Please highlight any separate registration, filing or additional formalities that are required to be completed to perfect Lessor's**

### **interest in the engines**

Applicable Hungarian laws are somewhat ambiguous (and it is untested before courts) as to what constitutes "aircraft" (i.e. whether the definition of an aircraft includes both the airframe and the engines or the airframe only), and in particular whether engines installed on an airframe qualify as accessories or as components.

In short, a component of an asset shares the fate of the asset itself (i.e. if title to the asset is transferred, such transfer will automatically cover the component also; similarly, if an asset is encumbered, the encumbrance shall cover all components of such asset), whilst an accessory shares the fate of the given asset only if there are doubts as to whether it is intended or not.

In accordance with international practice, an engine most likely qualifies as an accessory. This risk could be effectively mitigated by making clear vis-à-vis third parties that the engines are not owned by the owner of the airframe registered in the Aircraft Registry.

The mortgage over engines is also recommended to be separately registered in the Hungarian Security Interest Register.

### **12. What form does security over aircraft generally take in your jurisdiction?**

Typical forms of security in financing transactions are as follows:

- an aircraft mortgage (i.e. a charge on the title to the aircraft);
- a security assignment (e.g. lease or insurance payments);
- a share pledge / parent company guarantee;
- an account pledge;
- airframe and engine warranties arrangements/assignments;
- a security deposit; and
- deregistration powers of attorney.

### **13. Are there any particular terms or characteristics that such a security document must take (for instance, a cap on the secured liabilities)?**

Typically, most of the security documents in aircraft financing transactions including Hungarian registered aircraft are not governed by Hungarian law, except for a local law governed mortgage agreement over the aircraft / engines of the aircraft.

Such mortgage agreement should be in writing, the aircraft and the secured liabilities should be properly specified.

The asset may be described by type and quantity, or by description, making the asset clearly identifiable. The description may also pertain to certain assets which do not yet exist, or over which the mortgagor has not yet got the right to dispose.

The underlying claim shall be determined in a way by which it may be identified, with an indication of the – one or more – underlying relationship and showing the amount, or in any other way suitable for the identification of the secured claim. The description may also pertain to certain claims which do not yet exist.

**14. Are there any perfection requirements for such security document? If so, please state any conditions, procedural steps, formality requirements or documentation (for example, corporates, list of directors etc.) required to effect this**

The mortgage over aircraft is perfected upon registration in the Hungarian Aircraft Register. Mortgage over engines is perfected upon registration in the Hungarian Security Interest Register.

**15. Summarize any captive insurance regime in your jurisdiction as applicable to aviation.**

N/A

**16. Are cut-through clauses under the insurance and reinsurance documentation legally effective in your jurisdiction?**

Enforceability of “cut-through” clauses depend on the governing law of the relevant documents, but are normally enforced by Hungarian courts.

**17. Are there minimum requirements for the amount of third-party liability cover that must be in place in your jurisdiction?**

No.

**18. Can a mortgagee (or equivalent**

**security interest holder) or lessor following an event of default under a mortgage (or equivalent security document) or lease, respectively, take possession of the aircraft without judicial intervention in your jurisdiction? Please also state any conditions, procedural steps, formality requirements or documentation (for example, original, legalized, translated Lease/Mortgage, corporates etc.) required to effect this**

Enforcement can be judicial enforcement or out-of-court enforcement under Hungarian law, depending on the agreement and the level of co-operation of the parties, in particular the owner/ lessee.

**I. Leases**

If a lease is terminated on the basis that an event of default has occurred thereunder, the lessor will be entitled to take physical possession of the aircraft without any problem.

In this case, the most effective way to take back the physical possession of the aircraft is to sign a redelivery agreement by all the relevant parties, and simultaneously proceed with the application for deregistration from the Aircraft Register.

Repossession of the aircraft should not cause a problem, if the lessee is willing to deliver it back to the lessor.

**II. Financing**

Out-of-court enforcement is possible in respect of aircraft.

This includes the

- i. sale of the secured asset by the mortgagee/secured creditor or the
- ii. acquisition of the secured asset itself. Furthermore, special judicial enforcement methods are also available, subject to certain requirements, including
- iii. notarial enforcement or
- iv. simplified enforcement procedure.

In practice, it is not feasible under Hungarian law to take possession of the aircraft and enforce the security agreement or aircraft mortgage without the consent of the lessee or operator. Accordingly, a court order may have to be sought to obtain access to the aircraft or the engines. The court may require apostilled, notarized and

translated corporate documents and transaction documents.

It is standard procedure in Hungary that both the owner and the operator/lessee of the aircraft issue a deregistration power of attorney to the relevant secured creditor that contains prior consent to the repossession and deregistration of the aircraft: the use of such deregistration power of attorney is, however, untested in Hungary.

**19. How can a mortgagee (or equivalent security interest holder), lessor under a lease or designee/beneficiary of an IDERA deregister the aircraft? Please also state any conditions, procedural steps, formality requirements or documentation (for example, original, legalized, translated Lease/Mortgage/IDERA etc.) required to effect this**

Use of IDERA are untested in Hungary, it is market practice to use deregistration powers of attorney granted by lessor and operator/lessee, instead, in favour of the

- i. lessor and/or the
- ii. secured creditor, respectively.

The enforceability of such deregistration powers of attorney also remains untested under Hungarian law, although the concept is in line with Hungarian law and therefore, we believe it should be enforceable in front of Hungarian courts.

**20. Can the government or the lessee lawfully prevent the repossession or deregistration and if so, in what circumstances**

I. Government prevention:

Typically, no government prevention is applicable. A specific insolvency regime applies, however, in respect of "strategic companies". If the lessee/owner is considered by the Hungarian Government as a company of special importance to the national economy, and declared as a "strategic company", specific rules may apply to any liquidation or bankruptcy proceedings initiated against it.

Under this regime, the Hungarian Government may mandate a state-owned liquidator for procedures involving companies of special importance to the

national economy, and a special moratorium period applies, which circumstances may slow down / hinder repossession or deregistration of aircraft owned / possessed by a strategic company.

II. Lessee's prevention

The lessee may try to impede the exercise of repossession of the lessor, and may turn to the court for judicial remedy pursuant to the terms of the lease.

This may happen if the lessee claims that either it has acquired the title of the aircraft or it has other valid legal title to remain in possession of the aircraft (e.g. the lease was not properly terminated). The relevant English (or other non-Hungarian) court having jurisdiction in respect of the lease will then render a judgment which will be enforceable in Hungary.

**21. If judicial intervention is required, please describe the process? Please also state any procedural steps, length of time to complete and advise as to documentation required**

If the lessee is uncooperative regarding repossession, it is likely to challenge the lawfulness of a termination or otherwise claim that it still has the right to possess the aircraft. Under Hungarian law there is an assumption that the person possessing an asset has the right to do so. Any claim to the contrary has to be brought in front of a court.

The lessor may file a lawsuit against the lessee and request the Hungarian courts to compel the lessee to hand over the asset on the basis that it is no longer entitled to lease/possess it. Court proceedings in Hungary are generally lengthy, and it may take years to obtain judgement.

The court may require (i) apostilled, notarized corporate documents and (ii) certified translation of the underlying transaction documents.

The Hungarian court will only make a decision in respect of the possession of the aircraft as a consequence of the lease having been undisputedly terminated. Otherwise, if the acting Hungarian court deems that the dispute does in fact concern an agreement governed by foreign law (as most lease agreements in respect of aircraft are), it will likely declare that it does not have jurisdiction.

In such case the best way for the lessor to proceed is to obtain the judgement of the appropriate courts and then having it enforced in Hungary in accordance with the provisions of applicable laws.

**22. How is legal title transferred under the laws of your jurisdiction? Please also state any conditions, procedural steps, formality requirements or documentation (for example, corporates etc.) required to effect this**

Pursuant to applicable local laws, as long as the aircraft is registered in Hungary at the time of transfer of title, the aircraft can only be sold by fulfilling mandatory Hungarian law requirements relating to transfer of title. These mandatory rules require that (i) an underlying agreement to transfer (e.g. contract of sale) be concluded and (ii) the possession of the aircraft shall be transferred to the new owner.

Applicable law also provides that the parties are free to agree on the governing law of a contract of sale (being the underlying agreement to transfer required as set out above). The practice of the CAA is based on this, thus it will accept a sale agreement (and a bill of sale) governed by a law other than Hungarian (as long as the above requirements are fulfilled, including the requirement of transferring possession, as described below).

**23. Are there any restrictions on the sale of an aircraft following enforcement (for example, the requirement to obtain a court order or conduct a public auction or other action in order to sell the aircraft upon enforcement)**

Both judicial enforcement and out-of-court enforcement have restrictions as to sale of the aircraft, but generally judicial enforcement includes more limits. Please see in more detail regarding each method below:

I. Judicial enforcement procedure

Judicial enforcement requires obtaining an enforceable document by the secured creditor (most often this is a court order) and it also includes public sale organized by a bailiff. The overall process is strictly regulated and secured creditors have limited control. Costs of enforcement and employee related costs have priority from the sale proceeds, but all other claims rank behind the claim of the secured creditor. Judicial enforcement procedures are the most time consuming (can take between 1 – 3 years or more) and most expensive of all methods of enforcement and thus generally avoided by creditors. Notarial enforcement and simplified enforcement procedure are sub-types of judicial enforcement with certain benefits, but still remain restricted as compared to out-of-court enforcement

methods.

II. Out-of-court enforcement procedure

Out-of-court enforcement is based upon mutual agreement and is a preferred and smoother process than judicial enforcement, without involvement of a court bailiff. Out-of-court enforcement methods include (i) sale of the secured asset by the secured creditor, (ii) the acquisition of the secured asset by the secured creditor, and (iii) collecting the secured receivables from the third party debtor in the name of the security provider, however, item (ii) is available to a limited extent only, requires a strict notification process of any third party having interest in the secured asset, and may also result in a distress value being paid.

**24. Would lease rentals be subject to tax (for example, withholding or income tax)? Please also state if there are any conditions for such tax to be imposed and any steps usually taken to mitigate this**

Upon the lease of an aircraft or an engine, the lessor can be subject to Hungarian corporate income tax (CIT), levied at a flat rate of 9% of the positive tax base (which is the pre-tax profit of the lessor adjusted by various items) if the lessor is either a Hungarian tax resident entity or has a permanent establishment in Hungary to which the lease can be related. The lessor may opt to apply another tax regimes (first, and foremost, KIVA (tax for small enterprises)).

The revenue from the lease can also be subject to local business tax (LBT) levied by the Hungarian municipalities at the maximum rate of 2%

No withholding tax applies to lease fee or similar payments if the recipient is a foreign corporate entity under the currently applicable Hungarian tax laws.

**25. Would a sale of an aircraft in your jurisdiction incur sales tax? Please also provide details of amount or calculation and any steps usually taken to mitigate this**

In general, the sale of an aircraft located in Hungary or transit to Hungary is subject to VAT (the general rate is 27%). Where the aircraft is to be transported abroad in connection with the sale, no Hungarian VAT should apply.

However, the sale of an aircraft, operated by an entity

engaged in international air traffic, is exempt from VAT under the currently applicable VAT laws.

**26. Are there any restrictions on the import or export of aircraft in your jurisdiction and would such importation or exportation incur any liability as to customs or taxes? Please also state if any consents or approvals are required and the procedural steps taken to obtain these, and any procedural steps or formality requirements to mitigate any taxes**

In general, no export licence is necessary for exporting (ie, transferring out of Hungary) the aircraft, but consent of the owner is required. If the aircraft is exported to a jurisdiction outside the EU, customs restrictions may apply. Unless the importation of the aircraft is exempt from VAT as it is used by an entity engaged in international air traffic, import VAT liability may arise.

Upon the exportation of an aircraft to outside the EU, customs fees apply depending on the jurisdiction the aircraft is being exported to.

As a response to the ongoing war in Ukraine, the EU adopted certain sanction packages against Russia affecting the aviation industry as well. Airplanes registered in Russia or leased to Russian citizens/company are not allowed to land at EU airports and banned from flying over any EU countries.

The European Union also prohibited the export of goods /technology in the aviation industry to Russia.

**27. Are there any foreign exchange restrictions on transfers of funds**

Currently, there are no foreign exchange restrictions on transfer of funds.

**28. How successful have foreign creditors and lessors been in enforcing their security and lessor rights over and successfully repossessing aircraft in a timely manner?**

Precedents of repossession of aircraft are not common in Hungary, and success of repossession depends on multiple factors, e.g. whether creditors are secured and terms of the underlying contractual relationship. Generally, repossession should not cause extraordinary issues if the lessee is cooperative. Please see this more

in detail under section G, 18.

We note that creditors of a lessee do not have any rights with respect to the aircraft under Hungarian law, as a lease does not constitute title to the aircraft, and the only rights of disposition lessee may exercise are based on the terms included in the lease agreement.

There have been precedents where third parties detained aircraft located in the territory of Hungary, and thus impeded repossession, without having any specific legal title to the aircraft. The lessee in such case, did not redeliver the aircraft to the lessor, but parked it with a Hungarian third party service provider. At the end, in order to realize the repossession of the aircraft from the Hungarian third party service provider, the latter had to be provided with evidence on the legal title of the lessor to the aircraft (e.g. an English court order obtained by the lessor which could be then enforced directly under Hungarian law).

Other experience shows that service providers not paid by the lessee detain the aircraft until payment is received or until the above referred court order forces them to release the aircraft.

The above risks may be mitigated in lease agreements by way of

- i. inserting a clause authorizing the lessor to act on behalf of the lessee, and repossess the aircraft from, third party service providers should such event occur or
- ii. the parties may agree in the lease to have a separate power of attorney signed by lessee at the time of the lease is executed, limited to cases of repossession and only vis-à-vis third party service providers.

It is also market practice that the lessee provides the lessor/owner with an Eurocontrol letter and potentially an Air Traffic Control and Airport Authorities letter to prevent later disputes.

**29. What government led reforms affecting creditor and lessor rights are currently underway in the aviation sector in your jurisdiction?**

N/A

**30. Please describe any interesting legal development in your jurisdiction (for**



**instance, decided court cases or arbitral awards) which affect creditor and lessor rights?**

Up until 2021, there were no formal pre-insolvency proceedings available in Hungary.

As part of extraordinary legislation adopted by the Hungarian Government in response to the COVID-19 pandemic, a new temporary pre-insolvency reorganisation procedure was introduced on 17 April 2021, which may affect creditor and lessor rights equally. The procedure is currently regulated under Act XCIX of 2021 on the State of Emergency.

The purpose of the reorganisation procedure is to give distressed companies the option to implement a plan to restructure financial indebtedness.

If the court finds that a company is suitable for reorganisation, the creditors specified by the company are notified and will be subject to reorganisation protections (including a moratorium) for up to 170 days while the reorganisation plan is developed and presented to the specified creditors. The existence of a reorganisation procedure is not public unless the distressed company opts for this.

In addition, a new act on restructuring proceedings was recently adopted in order to implement the European Union's directive on restructuring, with restructuring proceedings available from 1 July 2022 in Hungary.

**31. Please discuss any relevant governmental regulations implemented in your country to help alleviate the financial and other difficulties faced by airlines in**

**your jurisdiction caused by CoVid 19 and whether that will impact rights of lessors (who lease aircraft to the airlines) and lenders (who finance such aircraft which are mortgaged in favour of the lenders)? Are such governmental regulations expected to be in place until the difficulties faced by airlines caused by the CoVid 19 subside or are they more long term?**

No regulations were implemented in Hungary to help alleviate financial and other difficulties faced specifically by airlines.

Due to the COVID-19 pandemic, a state of emergency was declared in Hungary, in effect between 11 March 2020 and 18 June 2020, which was reinstated from time to time, and terminated with effect from 1 June 2022. As a general reaction to economic difficulties during the pandemic, a payment moratorium was introduced, suspending the payment obligations in terms of commercial loans, purchase agreements or lease agreements until the end of October 2021, and is still available until 31 December 2022 only for some social groups and distressed companies previously involved as well.

By way of background, a state of emergency was re-introduced with effect from 25 May 2022, appointing the Hungarian Prime Minister as responsible for preventing/remedying the negative consequences of the state of emergency caused by the ongoing war in the neighboring country. The government is required to terminate the state of emergency when the circumstances giving rise to its declaration no longer apply.

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