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tax audit advisory

guidelines to taxation 2021

hungary

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guidelines to taxation in

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I TAX FRAMEWORK FOR DOING BUSINESS IN HUNGARY

A LEGAL FORMS

Business activities in Hungary may be carried on both by private entrepreneurs and companies. Act No. V of 2013 on the Civil Code provides for the following types of companies (the sole proprietorship is regulated in Act No. CXV of 2009 on Private Entrepreneurs and Sole Proprietorships); which are usually used for carrying on business activities in Hungary:

- Limited liability company – korlátolt felelősségű társaság (Kft.)
- Joint stock company – részvénytársaság (Rt.)
- Limited partnership – betéti társaság (Bt.)
- Unlimited partnership – közkereseti társaság (Kkt.)
- Sole proprietorship – egyéni cég (Ec.)

The following table indicates the most important characteristics of the abovementioned legal entities:

FORM	LIABILITY OF SHAREHOLDERS	MINIMUM CAPITAL (HUF)	MINIMUM OF FOUNDERS AND SHAREHOLDERS	REGISTRATION IN COMMERCIAL REGISTER
Kft.	limited	3 million	one	required
Rt.	limited	5 million for private, 20 million for public	one legal entity or at least two individuals	required
Bt.	unlimited and limited		at least two (general and limited)	required
Kkt.	unlimited		at least two	required
Ec.	unlimited or limited		one only	required

Foreign investors may also engage in business in Hungary by establishing a branch office (»fióktelep«). A branch office is the Hungarian-registered part of a foreign undertaking that operates in Hungary with economic independence but without legal personality. A branch office may carry on business activities, acquire property, exercise certain rights and assume liabilities in its own name.

A commercial representative office (»kereskedelmi képviselet«) is registered in Hungary as part of a foreign undertaking, without legal personality. A commercial representative office may represent the foreign undertaking and carry on solely preparatory and auxiliary activities for the benefit of the foreign undertaking. The commercial representative office may conclude contracts necessary to its operation, but only in the name of the foreign undertaking. The mere existence of a commercial representative office does not render the parent company subject to Hungarian corporate taxation.

Both the branch office and the commercial representative office shall be registered by the court into the commercial/company register.

B INCOME TAX ASPECTS

1 Private entrepreneurs

Partnerships (Bt. and Kkt.) are treated as non-transparent taxable persons in Hungary and taxed as corporations; for details, see I.B.3.

The taxation of private entrepreneurs is determined by Act No. CXVII of 1995 on Personal Income Tax (PIT Act). The rules for their taxation are a combination of principles applicable for private persons and corporations. A general overview is provided below.

1.1 UNLIMITED TAX LIABILITY

Hungarian tax residents are liable to Hungarian personal income tax on their worldwide income (unlimited tax liability; for details, see III.A.1).

1.2 BUSINESS INCOME

Private entrepreneurs are taxed at two different levels.

First, the entrepreneurial activity itself is taxed as business income (for details, see I.B.1.3-7). The following persons are considered to exercise business activities and are subject to business income tax: persons with a business license (Act No. CXV of 2009 on Private Entrepreneurs and Sole Proprietorships), public notaries, private legal executors, individual patent agents, lawyers and veterinarians.

The individual can establish a sole proprietorship, which has to be registered by the Court of Registry. An individual who has established a sole proprietorship is no longer taxed under the Hungarian personal income tax regime, rather, his sole proprietorship is subject to the corporate income tax rate of 9% (see I.B.3.5).

Secondly, at the level of the individual two income types may be taken into account: »salary« and »dividend«. The money taken out of the business by the private entrepreneur is considered to be »salary«. This income is part of the consolidated tax base, taxed at a flat rate of 15%, and social security contribution is due. »Dividends« are also taxable at a rate of 15%, plus a social tax amounting to 15.5% (but only up to HUF 599,000; approx. EUR 1,660) must be paid.

Coming back to the first level of taxation, according to Hungarian tax law, private entrepreneurs (as well as agricultural entrepreneurs and small agricultural entrepreneurs) may choose between the business income tax base method and the lump-sum method. These methods are described in the following sections.

1.3 PRINCIPLES OF DETERMINATION OF THE BUSINESS INCOME TAX BASE

Business income is calculated as the difference between gross income earned and related expenses. The taxable amount comprises any amount received in connection with the activity performed (including sale of products, rendering services, interest income, income from the realization of products, compensations, income from the sale of materials, tangible assets, etc).

In addition to the expenses that may generally be deducted according to the payments to the private entrepreneur as a consideration for his services are treated as income from independent activity and are included in the consolidated income tax base, see III.A.1.3. Due to the fact that these payments are taxable as part of the consolidated tax base of the individual, the payments are considered to be costs at the level of the entrepreneurial activity in order to avoid double taxation.

In addition to the expenses that may generally be deducted according to the rules applicable to companies, the income may be further reduced – inter alia – by the following expenses:

¬ remuneration paid to disabled employees up to the minimum wage, if the disability of the employee is at least 50%;
¬ social tax paid by the entrepreneur for a trainee (for a period of up to 12 months), if the trainee is subsequently employed after having successfully passed his professional examination, or if an unemployed person is employed; and
¬ research and development costs within the private entrepreneurial activity: up to three times the actually recorded R&D expenses may be deducted, but no more than HUF 50 million (approx. EUR 139,000).

1.4 DEPRECIATION

Depreciation is part of the expenses an entrepreneur may take into account when calculating his tax base. The actual acquisition costs (or costs of production), as well as certain expenditures incurred prior to initial start-up form the depreciation base of assets. However, the assets with an acquisition cost of less than HUF 200,000 (approx. EUR 555) may be fully deducted in the year of their acquisition. Depreciation starts when the asset is capitalized and it ends on the day on which it is no longer used in the taxpayer's business (e.g. it is sold, contributed, etc.), or its book value has become zero.

The PIT Act permits depreciation keys to be used:

- depreciation of buildings
  - buildings with long economic life: 2% per year;
  - buildings with medium economic life: 3% per year;
  - buildings with short economic life: 6% per year;
- depreciation of machinery, equipment and accessories: 33%, 20% or 14.5% per year, depending on their customs tariff number classification;
- for the purpose of determining the depreciation rate, the investment costs of intangible assets and certain tangible assets are divided by the years during which the private entrepreneur is expected to use them for entrepreneurial activities (i.e. useful life of the assets); and
- a flat depreciation rate may be applied in respect of machinery, equipment and accessories that are not exclusively used for business purposes. This may not exceed 1% of the annual revenues or 50% of the book value of the tangible asset(s).

1.5 CARRY-FORWARD LOSSES

Entrepreneurs may carry forward losses for five years (new rule as of 2015) without requiring permission from tax authorities. As a transitional provision, losses accumulated up to 2014 may be utilized until 2030. Loss utilization is also capped at 50% of the entrepreneur's positive tax base. Special provisions apply to agricultural entrepreneurs.

1.6 TAX RATES

The entrepreneurial activity itself is taxed as business income at a tax rate of 9%. Moreover, a minimum tax base amounting to 2% of the adjusted entrepreneur's income is applicable if the calculated tax base of the entrepreneur falls below this target.

The entrepreneur's salary is subject to a flat tax rate of 15% plus social security contributions; his business dividend is taxed at 15% personal income tax plus 15.5% social tax (which is capped at HUF 599,000, i.e. approx. EUR 1,660).

1.7 LUMP-SUM BUSINESS TAXATION AND LUMP-SUM TAXATION OF CERTAIN OTHER CATEGORIES OF INCOME

An entrepreneur may opt for lump-sum business taxation, provided also that his annual income does not exceed HUF 15 million (approx. EUR 41,700) or HUF 100 million (approx. EUR 278,000) in case of retailers.

If the option is exercised, expenses are deductible on a lump-sum basis. The deduction amounts to 40% of the gross amount of income in general and is increased to 80% for income from special activities (i.e. agricultural, processing and building industries, taxi services, photo industry, hairdressing and cosmetic services, laundry and cleaning), to 87% for income derived by retail traders and to 93% for income derived by retail traders from exclusively performing the above listed special activities. Small agricultural entrepreneurs are entitled to deduct 85% and/or 94% from that part of their income which is derived from stock farming. Lower percentages are applicable if a private entrepreneur is qualified as engaged in auxiliary activities.

The tax is levied at a tax rate of 15%.

1.8 OTHER TAX

Private entrepreneurs are also subject to local business tax because they carry on business activities on the territory of a municipality. The rate is set by the municipalities but may not be more than 2%. Moreover, municipalities may levy taxes on property located within their territory, see I.E.1.

1.9 TAX ASSESSMENT

Income tax is generally levied by self-assessment. Thus, the taxpayer is obliged to compute his income and the tax due on it, to prepare and file the tax return, and to pay the tax. Private entrepreneurs, farmers, and persons renting private accommodation must prepare and file tax returns at the end of every calendar year, irrespective of whether they derive any income or not. The annual tax return of private entrepreneurs must be filed by 20 May of the following year. A taxpayer deriving income that belongs to the consolidated tax base must make income tax prepayments on a quarterly basis (until the 12th day of the subsequent month), unless a paying agent is required to withhold the income tax (taxes withheld must be transferred to the tax authorities by the 12th day of the following month). Any difference between the annual tax liability and the prepayments must be paid by the taxpayer by the filing deadline. Any excess tax payments must be refunded by the tax authorities within 30 days of the date the tax return was received.

2 Itemized tax of small businesses

The itemized tax of small businesses (»KATA«) is available for private entrepreneurs, sole proprietorships and limited/unlimited partnerships with exclusively private members. If they meet certain criteria, they may opt for the itemized tax, which amounts to HUF 50,000/month/person, or optionally, for higher social security coverage HUF 75,000month/person (these amounts are equivalent to approx. EUR 140 and EUR 210, respecti- vely) contributing to the activity of the taxpayer with a contract other than an employment contract for full-time entrepreneurs, and HUF 25,000/month/ person (approx. EUR 70) for part-time entrepreneurs under the condition that the yearly revenue of the taxpayer does not exceed HUF 12 million (EUR 33,300). In the event that his revenue does exceed this limit, the taxpayer must pay 40% tax on the exceeding amount in addition to the itemized tax. Regarding transactions between affiliated parties, the payer shall pay a tax amounting to 40% and file the respective tax return. Further, if, within one tax year, the taxpayer who opted for KATA receives income from one domestic disburser exceeding the limit of HUF 3 million (approx. EUR 8,300), then the disburser shall pay 40% tax on the amount that is in excess of the HUF 3 million limit. If the KATA taxpayer receives income from one non-Hungarian disburser exceeding the limit of HUF 3 million (approx. EUR 8,300), then the KATA taxpayer shall pay 40% tax on 71.42% of the amount that is in excess of the HUF 3 million limit. This option may be exercised by the eligible taxpayers at any time of the year. The itemized tax status starts in the month following the notification of this option. After cessation of the itemized tax status, it cannot be opted for again within twelve months.

The itemized tax replaces

- the entrepreneurial income tax;
- the corporate income tax;
- the personal income tax and contributions;
- the social tax and the vocational training contribution.

Full-time entrepreneurs are considered to be insured in the state system and entitled to receive all benefits according to Act No. CXXII of 2019 on the Entitlements for Social Security Benefits and on Funding These Services and Act No. IV of 1991 on Job Assistance and Unemployment Benefits.

Part-time entrepreneurs are not insured in the Hungarian state insurance system and are not entitled to receive any of the abovementioned benefits in relation to the tax for small businesses itemized above but are assumed to be covered by the insurance for their other relations.

Taxpayers may apply simplified accounting and record keeping rules. To avoid hidden employment relationships, turnover exceeding HUF 1 million (approx. EUR 2,800) with a taxpayer opting for the itemized tax in a calendar year must be reported to the tax authority subsequent to the calendar year by both parties (i.e. by the entrepreneur and his principal).

3 Corporations

3.1 SIMPLIFIED TAXATION FORM FOR SMALL BUSINESSES: SMALL-SIZED ENTERPRISE TAX

The small-sized enterprise tax (»KIVA«) is regulated by Act No. CXLVII of 2012, which was introduced for the purpose of simplifying taxation and reducing the tax burden of small businesses. Certain small-sized enterprises (partnerships, limited liability companies, cooperatives, housing cooperatives, lawyers', notaries', patent attorneys' and executors' offices and foreign entities that have their place of management in Hungary) with an annual income and balance sheet total not exceeding HUF 3 billion (approx. EUR 8.3 million) and with a staff of up to 50 employees in the prior tax year may opt for the small-sized enterprise tax. If the income cap of HUF 3 billion is exceeded on the first day of the quarter, then the company may still apply the small-sized enterprise tax, provided that the income does not exceed HUF 6 billion. Similarly, small-sized enterprise tax may still be applicable if the headcount limit of 50 employees is exceeded, provided that it remains under 100 employees. If these latter limits (i.e. HUF 3 billion income and 100 employees) are exceeded, the small-sized enterprise taxpayer status can no longer be applied. In calculating the required upper limits, the data of affiliated enterprises must be added. The company can only reapply for the small-sized enterprise tax after a period of 24 months following the termination. Certain further requirements must also be met (e.g. not falling under cancellation of the tax number, tax debts: not exceeding HUF 1 million i.e. approx. EUR 2,778, financial year must be equal with the calendar year and the reporting must be kept exclusively in HUF). As of 23 August 2019, the taxpayer may only opt for small-sized enterprise tax if he did not have a CFC in the previous tax year and the positive difference between the financing costs occurred for business purposes (defined by the CIT Act) and the interest income in the preceding tax year does not exceed HUF 939,810,000 (approx. EUR 2.6 million).

Enterprises opting for the small-sized enterprise tax must electronically notify the tax authority of their intention in the month preceding the commencement of the small-sized enterprise tax status.

The tax rate is 11% on the adjusted cash-flow balance but at least the disbursement related to the personnel costs. Losses may also be carried forward and depreciation is also possible. If a company changes from the regular CIT taxation to the small-sized enterprise tax, then the losses from the CIT period can be carried forward and used in the KIVA regime.

The small-sized enterprise tax replaces

- the corporate income tax;
- the social tax; and
- the vocational training contribution.

There is no monthly advance-tax liability; all taxpayers are subject to a quarterly payment obligation.

3.2 TAXPAYERS AND RESIDENCE

Entities established according to the Act on the Civil Code (including corporations and partnerships) are deemed to be non-transparent taxable persons under Hungarian corporate income tax law. Therefore, income generated by these entities is taxable at the level of the entities.

A corporation or partnership having its statutory seat or place of effective management in Hungary is subject to unlimited corporate income tax liability, which provides for a taxation of the worldwide income (subject to the applicable tax treaties).

As of 1 January 2019, corporate group taxation is available in Hungary, covering all domestic taxpayers that are related parties linked with at least 75% voting rights (directly or indirectly through one or more domestic or foreign entity). Voting rights of close relatives (defined by the Act on the Civil Code) shall be aggregated. Even two companies may form a group, but a taxpayer may only be a member of one group at any given time. Taxpayers starting their business during the year may also be a member of a tax group if the conditions are met. Opting for the group taxation scheme for the next year shall be notified in advance, between the 1st and 20th day of the penultimate month of the current tax year (i.e. by 20th November if the tax year is equivalent to the calendar year). Any members of the tax group may be appointed as the head of the tax group, who is then liable to represent the group towards the tax authorities in corporate income tax matters.

3.3 PRINCIPLES OF DETERMINATION OF THE TAX

Taxable income is based on the financial statements prepared in accordance with the Hungarian accounting standards as provided for by Act No. C of 2000 on Accounting (Act on ACC), which is to a large extent based on the EC directives. The corporate income tax (CIT) base is then calculated by adjusting the accounting pre-tax profit by increasing and decreasing items described in Act No. LXXXI of 1996 on Corporate Income Tax (CIT Act).

In particular, the corporate income tax base and the CIT are calculated as follows:

	Pre-tax profit according to the Act on ACC
+	Tax base increasing items
–	Tax base decreasing items
=	Tax base
–	9% CIT decreased by tax allowances
=	After-tax profit

The tax base of corporate tax groups is calculated differently, according to special rules, as follows:

+	Sum of individually defined non-negative tax bases
–	Sum of individually defined negative tax bases (plus loss carried forward from previous years on group level)
=	Loss carried forward from previous years on group level: max. 50% of individually calculated positive tax bases (without the utilization of losses carried forward) minus the sum of individually utilized losses
=	Group level tax base (if negative may be carried forward for 5 tax years)
	9% tax liability
=	Calculated group level tax liability
	Tax liability will be shared among group members in proportion with their positive tax bases
	Calculating development tax allowances of the group members (80% of the individually defined tax liability) and energy-efficiency tax allowances of group members (70% of the tax liability remaining after the development tax allowance)
–	Individual tax allowances of group members
–	Other tax allowances of group members (max. 70%)
=	Group level tax liability
	Tax liability will be shared among group members in proportion with their positive tax bases

The most important tax base adjustment items are listed in the following section:

Business and non-business expenses

Business expenses are generally deductible for CIT purposes. Moreover, expenses for certain benefits in kind and for the private use of a company car are also acknowledged costs of a company. Costs of representation and business gifts are deductible for CIT purposes (however, representation costs and gifts are subject to personal income taxation).

A qualified deductibility is valid for expenses incurred concerning controlled foreign companies (see I.C.3) at a value including VAT deriving from uncompensated financial or other support (covering the free-of-charge provision of assets and services) that would not be deductible if provided to foreign persons and foreign tax residents or to domestic persons the financial result of whom would be negative without the above support. Certain further administrative conditions must be applied as well.

Tax and accounting depreciation

Assets may be depreciated for accounting purposes over their useful life. The CIT Act, however, contains a list of depreciation rates that, for tax purposes, override the accounting depreciation rates. As the accounting rules do not provide for specific depreciation rates, usually the rates stipulated by the CIT Act are applied for accounting purposes as well. The taxpayer has the possibility to opt for a lower depreciation rate compared to the rates included in the CIT Act; however, the rate applied for CIT purposes should not be less than the depreciation rate applied for accounting purposes.

In general, accounting depreciation increases the tax base, while depreciation determined for tax purposes is deductible from the tax base.

Depreciation rates applicable for CIT purposes are as follows:

- depreciation of buildings:
  - buildings with long economic life: 2% per year;
  - buildings with medium economic life: 3% per year;
  - buildings with short economic life: 6% per year;
- depreciation of machinery, equipment and accessories: 33%, 20% or 14.5% per year, depending on their customs tariff number classification; and
- 50% depreciation rate may be applied for certain unused assets, for IT assets, equipment solely used for film and video production and for intellectual property, research and development assets.

Provisions

Provisions accounted for as expenditure (for expected liabilities and future costs) must be recognized as tax base increasing items, while previous provisions accounted for as revenues may be treated as corporate income tax base decreasing items.

Impairment and bad debts

In general, the impairment of receivables and the amount of bad debts calculated according to the company’s accounting policy increase the tax base and are only deductible for tax purposes if they fulfill the conditions set out in the Act on ACC. In addition, 20% of the bad debts which do not necessarily fulfill the abovementioned conditions but are overdue for more than 365 days may also be deducted (provided that the statutory limitation period has not expired).

The waiver of still recoverable receivables increases the tax base only if the debtor is a related party (not including a natural person).

Interest limitation rules

As of 1 January 2019, new thin capitalization rules shall be applied in Hungary. If the amount of net financing costs (i.e. interest expenses less interest revenues) exceeds 30% of EBITDA or HUF 939,810,000 (approx. EUR 2.6 million) – whichever is higher – the excess part will not be acknowledged in the CIT base of the given tax year. However, the not acknowledged exceeding borrowing costs may be carried forward for future periods without any time limitation and in the subsequent tax years a tax base decrease is available in the amount of 30% of the EBITDA of that tax year. The positive difference between the 30% of the EBITDA and the net financing costs may be carried forward to offset the potentially non-deductible net financing costs of the subsequent tax years. These provisions are basically applicable to interests deriving from all kind of loans – including loans from financial institutions – irrespective of the related party status of the lender. Special exemption rules apply to companies belonging to company groups drawing up a consolidated financial statement. If the taxpayer can demonstrate that the ratio of its equity over its total assets is equal to or higher than the equivalent ratio of the group, then net financing costs are fully deductible. Alternatively, the net financing costs of the group towards non-related parties may be deductible at the Hungarian taxpayer, in proportion to its EBITDA compared to the consolidated EBITDA of the group.

Dividend income

The Hungarian tax legislation provides for a widely applicable participation exemption for dividends. In general, dividend income earned by Hungarian companies is deductible from the tax base, except for the dividends received from a controlled foreign corporation (notional dividend distributions from controlled foreign corporations are also an exception), see I.C.3.

Development reserve

Companies are entitled to set up a tax-deductible reserve of up to 100% of the pre-tax accounting profit, subject to a maximum of HUF 10 billion (approx. EUR 31 million). Assets acquired using this »development reserve« may not be depreciated for tax purposes up to the value of the reserve used. Therefore, the development reserve has the effect of an accelerated depreciation. The reserve must be used for investments within four financial years; otherwise it must be repaid (tax due must be calculated at the tax rate effective in the year of setting up the reserve) with late payment interest (the Hungarian prime rate +5 percentage points). As the depreciation rates applied for immovable property are quite low, the use of development reserves could generate a tax-effective investment structure.

Research and development costs

Research and development (R&D) expenses are not only accepted accounting costs decreasing the accounting profit before tax, but also constitute a tax base decreasing item with respect to CIT. These costs may be deducted therefore twice for tax purposes. However, the advantage is applicable solely for R&D costs incurred by the taxable person's own activities (including R&D based on an R&D agreement), which precludes additional deductibility of outsourced service fees.

The direct expenses for basic research, applied research, and experimental development may be deducted in the year in which the expenses are incurred or in the year of accounting the depreciation if the costs of the experimental development were capitalized.

The above R&D advantages may be shared among Hungarian related parties. As of 2018, the tax base allowance may be shared even between the domestic R&D service provider and the customer; however, this allowance cannot be forwarded to related parties.

Four-time deductibility is available (up to HUF 50 million, or approx. EUR 153,846) for R&D projects carried out jointly with universities or scientific institutions.

Donations

Cash or asset donations granted to non-profit organizations may – subject to certain conditions – qualify for a tax base reduction of 20% or 50% (and an additional 20% in case a permanent donation contract exists) of the donation capped by the pre-tax accounting profit. Donations granted to higher education institutions in a long-term agreement may also be a tax base decreasing item with a rate of 50%, subject to meeting certain preconditions.

Royalty exemption

Under special legislation, a 50% tax base decreasing item is available on royalty income, capped at 50% of the pre-tax accounting profit. The benefit for old IP assets may be taken into account according to the grandfathering provisions until 30 June 2021 at the latest. Special restrictions apply to intangibles acquired from a related party entity in the period of 1 January to 30 June 2016.

The above royalty exemption rules however, were amended to new IP assets acquired or developed beginning from July 2016. Instead of the 50% decreasing item on the royalty income as described above, a certain proportion of royalty profits is available as a tax base decreasing item, whereby the Hungarian implementation of the Nexus ratio shall be applied for calculating the amount of the tax base decreasing item. By performing own R&D activities with own assets and personnel at group level, the nominator of the Nexus ratio may be increased by 30%; however, the ratio itself shall not exceed 100%. The application of the tax base deduction is capped at half of the positive pre-tax accounting profit as well. A reversal of the above reduction is necessary if the respective intangible asset generates a loss in the next tax year; i.e. 50% of the loss would increase the tax base then.

Carry-forward of losses

Basically, loss utilization is capped at 50% of the annual tax base. From 2015, losses generated may be carried forward for a period of five tax years only, and losses generated prior to 2015 may be utilized in the tax year including the date of 31 December 2030 at the latest. Regarding corporate transformations and quota transactions, the utilization of tax losses may fall under further restrictions. Special loss carry-forward rules apply for corporate group taxpayers.

Further tax base decreasing items

The cost of recharging points for electric cars and the cost of a long-life structure built for the purpose of providing rental units for workers may also be tax base decreasing items in accordance with the conditions laid down in the CIT Act. The costs of operating a kindergarten are considered incurred in the interest of the business operation of the company, as well as the costs of a daycare facility.

3.4 TAX ALLOWANCES

Numerous subsidies and tax allowance forms partially backed by European Union aid resources are still available in Hungary. The first call for proposals for the 2014-2020 developing period was launched in the second half of 2015. For investment projects, however, we also highly recommend considering the taxation impacts carefully and not to forget about the potential related tax allowances – for which LeitnerLeitner offers its professional assistance for tax optimization and allowance claims.

It is laid down in the CIT Act that tax allowances are available for taxpayers even in the course of self-revision.

The tax payable by corporations may be reduced by 70%; 80% by means of tax credits. In case of corporate group taxpayers, special provisions shall be applied regarding tax allowances.

Development tax allowances (80%) may be granted for investment projects (depending on the investment volume, the geographical location, and also the status of the investor), research and development activities, independent environmental projects, investments in the film industry, and creating new jobs. In general, a portion of the investment value (determined by the intensity ratio given by the EU) may be credited from the corporate income tax payable within 16 tax years after the finalization of the investment in 13 tax years, including the year of capitalization of the investment or the subsequent tax year. Commitments pertaining to the increase in or stabilization of headcount and salaries have become more favorable to the taxpayers regarding certain development tax allowance schemes as of 2020.

Since 2017 development tax allowances may be granted for investment projects in the Central-Hungarian Region valued at HUF 6 billion (approx. EUR 16.67 million) or more at present value and for investment projects that create new workplaces valued at HUF 3 billion (approx. EUR 8.33 million) or more at present value, if the investment project results in product diversification or new process innovation. These provisions aim to widen the scope of businesses (large businesses) that may apply for development tax allowances.

A separate tax credit scheme that is connected to investments aiming at increasing energy efficiency is also available. Investments resulting in any minor decrease in energy consumption may be sufficient for such a tax allowance. Application in parallel to the development tax allowance scheme is not allowed. A certain portion (30–45%) of eligible costs of the investment may be deducted from the CIT payable, depending on the geographical location of the investment (a higher rate by 10 or 20 percentage points may be applied for SMEs). The tax allowance is capped at EUR 15 million and 70% of the CIT payable. The tax credit is available in the year of capitalization of the investment and in the subsequent five tax years.The tax incentive for investment projects aimed at energy efficiency is available for renovations as well. This tax credit is not available in connection with electric passenger vehicles, unless they are convertible for freight transportation purposes.

Further CIT allowances (70%) and other in-cash credits may also be available in the case of granting support to film production and certain team sports such as soccer, handball, basketball, water polo, ice hockey, and volleyball. As of 2020, the grant can also be used for measures to combat the COVID-19 pandemic in the abovementioned sport teams (in practice aiding the purchase of disinfection materials, COVID-19 tests, etc.).

As another potential tax credit, subsidies may also be granted to film production and certain team sports (such as soccer, handball, basketball, water polo, ice hockey, and volleyball) by redirecting the CIT advance payment obligations of the taxpayer. For such funding, a further proportional cash credit (7.5% or 2.5%, depending on the timing of the grants) may be received to the tax account of the taxpayer.

Also within the scope of de minimis support[1] 100% of the interest paid by SMEs to financial institutions on loans financing tangible assets may be taken as an allowance, decreasing the CIT payable.

1 Subsidies of less than EUR 100,000 granted to an undertaking over a period of three years do not constitute »state aid« within the meaning of the EC Treaty's ban on aid liable to distort competition (Art. 87).

3.5 TAX RATES AND TAX PAYMENTS

Corporate income tax

As of 1 January 2017, the CIT rate is 9%, instead of the preceding 10%/19% progressive rates.

A minimum CIT is levied on the tax base amounting to 2% of the total adjusted income. Nevertheless, the minimum tax obligation may be avoided by submitting a special declaration to the tax authorities. The total income cannot be reduced by the purchase price of goods sold and by the value of mediated services. Members of corporate tax groups shall also apply the rules of minimum tax.

Tax assessment and filing obligations

The CIT should be assessed on a financial year (calendar or business year) basis. All business entities are obliged to make tax prepayments based on their business result and their tax liabilities of the preceding year.

Growth tax credit

If the difference between the taxpayer's adjusted pre-tax profit in the given tax year and his pre-tax profit in the previous tax year exceeds at least five times the absolute volume of his pre-tax profit of the previous tax year, then the taxpayer may opt for deferral of the tax payment due on such positive difference. The deferred payment may be fulfilled in six equal installments throughout the subsequent two tax years. Certain types of income, such as dividend and interest income or cash received from a related party without repayment obligation may not be included in such tax deferrals. The taxpayer applying growth tax credit is obliged to pay interest for the deferred tax. The interest shall be calculated on the basis of the prime rate of the National Bank of Hungary.

The taxpayer is eligible to the growth tax credit if the following conditions are met:

- the taxpayer has been a taxable person for CIT purposes for three or more years preceding the tax year;
- the taxpayer did not participate in any transformation, merger or de-merger in the three tax years preceding the tax year;
- the taxpayer submits a declaration about using the growth tax credit by the deadline of the annual CIT return.

The taxpayer may reduce the remaining amount of payable tax on growth tax credit by implementing fixed-asset investments and raising the headcount in the year of the submission of his declaration about using the growth tax credit and the following tax year. Strict conditions need to be fulfilled for this reduction.

Growth tax credit is not available for corporate group taxpayers.

4 Reorganizations

The most feasible means of reorganization is transformation. Transformation is regulated by the civil law, which provides for the following types: merger by forming a new company (fusion), merger by acquisition (absorption), demerger by splitting off sections of a company as a separate business entity (spin out), and demerger when a single company splits into two or more separately running companies by legal succession (split up).

According to the applicable accounting rules, a corporation undergoing transformation may revalue its assets and liabilities recorded in its books. In general, this revaluation difference is taxable at the time of the merger. Naturally, the companies may also decide to perform a merger at book value, without any revaluation. In this case no taxable revaluation difference arises; only the difference between the tax and accounting book value of assets (due to the different depreciation methods for tax and accounting purposes) becomes taxable in the course of the merger.

Nevertheless, a tax-neutral transformation (both for corporate and transfer tax purposes) may also be achieved by the use of the special rules on preferential transformations. Transformation may only qualify as preferential if the transaction is based on valid business and commercial reasons, where the burden of proof lies with the taxpayer. If the shareholders decide to perform a preferential transformation and all the conditions stipulated in the relevant Acts are met, neither the revaluation difference nor the difference resulting from the different depreciation methods for tax and accounting purposes are taxed at the time of transformation. For income tax purposes the preferential transformation provides for a deferred tax liability, not a real tax exemption. The revaluation difference is taxable upon the alienation of the revalued asset or at the time of dissolving the company.

According to the Act on VAT, the receipt of goods and rights with pecuniary value in the course of a transformation is not subject to VAT, provided that certain administrative conditions are met.

The Act on Duties provides that the transfer of assets (including immovable property or shares in real estate holding companies) other than by preferential transformation is subject to transfer taxes (for special provisions, please see I.E.2). The intra-group transfer of shares held in real estate holdings is exempt from transfer taxes.

5 Special treatment of non-resident individuals

An individual who is not resident in Hungary (i.e. non-resident) is subject to limited tax liability with the following Hungarian-source income:

- income from independent personal services if the business is carried out through a permanent establishment in Hungary;
- income resulting from the leasing or rental of real estate located in Hungary;
- income from employment if the regular place of work is in Hungary or the non-resident performs the activity under an employment relationship with a permanent establishment, a branch or a commercial representation office of the employer located in Hungary;
- income from domestic dividends;
- income from royalties;
- interest income;
- income earned by executives and members of the supervisory board of legal persons established in Hungary; and
- income from services such as those of an artiste or sportsman as well as from exhibitions and fairs if these activities are carried on in Hungary.

The tax treatment of income derived by non-residents follows the rules applicable to residents. Income derived from those activities is subject to personal income tax at the same rates applicable for resident taxpayers; i.e. 15%.

6 IFRS implementation

Standalone IFRS (International Financial Reporting Standards) accounting is possible in Hungary. However, the IFRS financials need to be adjusted to the Hungarian Accounting Standards (HAS) in order to serve as a basis for tax calculations.

The principal aim of the legislator was for companies applying IFRS accounting to ultimately arrive at the same tax base as those who keep their accounts according to the HAS. The tax base according to the IFRS cannot be lower than the tax base determined on the basis of the HAS. For this reason, the IFRS implementation package follows the principle that first the accounting results for the IFRS need to be adjusted in comparison with the HAS, then the tax base calculation is always based on these adjusted financials.

Practically speaking, this means that companies applying IFRS accounting need to keep separate detailed records according to the HAS to be able to prepare a tax balance, or more preferably to perform separate HAS accounting at least for the first few years. This is especially true because, although the legislator admits that there could be certain differences between the two standards not specifically regulated in the IFRS implementation package, this fact does not relieve the company applying the IFRS of considering such in its tax calculations. This deregulation results in a higher general tax risk.

The following table illustrates the CIT calculation principles for companies keeping their books under the IFRS in Hungary:

	IFRS result
+/–	Accounting adjustments compared to HAS
=	Adjusted pre-tax profit
+/–	Further special IFRS adjustments
+/–	Normal tax base adjusting items according to CIT
=	Tax base

After having the IFRS result modified by the listed adjustments, the resulting tax base will serve as a basis for calculating the CIT in the general manner.

C INTERNATIONAL BUSINESS-RELATED ISSUES

1 Tax treaties

Hungary has concluded nearly 100 tax treaties in the area of income and capital taxation, two of which have not yet been ratified; the new treaties with the United States and Iraq are not yet applicable. The most recent treaty, which was concluded with the Sultanate of Oman, became effective on 1 January 2018.

The majority of the treaties concluded by Hungary do not include anti-avoidance clauses and can often be used highly efficiently in international tax structures.

The treaty with the USA was revised in 2010 to include a LOB provision; however, the new treaty has not yet entered into force. The United States of America enacted provisions commonly known as the Foreign Account Tax Compliance Act (FATCA), which was signed by Hungary in February 2014. This treaty can be the solution for the proper information exchange between the two countries until the original treaty is signed by the Senate.

In most of the treaties the exemption (with progression) method applies, except for dividends, interest and royalties. Almost 30 of the tax treaties concluded (e.g. with Australia, Ireland, Canada, China, Sweden, Malta) include a real estate clause which is of relevance in respect of the income tax schemes for real estate holding companies (see II.B). Any international treaties that have been approved, ratified and promulgated prevail over the Hungarian domestic tax provisions.

A new regulation on international administrative cooperation entered into force on 1 July 2019 based on Chapter III/A of Act No. XXXVII of 2013 in the field of taxation and other fiscal burdens. This new law is intended to comply with Council Directive (EU) 2017/1852 on European Union Tax Dispute Settlement Mechanism.

The law shall apply to certain matters relating to the assessment of taxes, the collection of taxes and other charges, and the avoidance of double taxation between the Member States of the European Union and other international administrative cooperation. The law also contains the European Union Dispute Settlement Procedure.

In 2021, the tax information exchange network continued to expand, both in terms of financial account information and country-by-country reports relevant to transfer pricing. The Annex of Act No. CXC of 2015 on promulgation of the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information lists the jurisdictions that have acceded to the information exchange agreement. The Annex of Act No. XCI of 2017 on promulgation on the Multilateral Competent Authority Agreement on the Exchange of Country-by-Country Reports includes the jurisdictions participating in the information exchange agreement.

2 Transfer pricing

Hungary has adopted some of the most stringent regulations in Europe in terms of transfer pricing covering not only cross-border but also domestic related party transactions, including the requirements for the pertinent documentation thereof. In general, the Hungarian transfer pricing rules follow the OECD Transfer Pricing Guidelines.

Apart from general business transactions, transfer pricing regulations apply to contributions in kind, decrease of capital by withdrawal, in the case of dissolution without succession, to payment of shares in kind and to dividends in kind. The regulation also covers cases when business shares acquired by the taxpayer for consideration are transferred to the shareholders free of charge, or when retired, with any payment of share by means other than money in the event of dissolution without succession.

Transfer pricing regulations also apply when dividends are provided by means other than money, if the non-monetary contribution is paid or the share is received by an affiliated company or a member (shareholder) who makes a non-monetary contribution to become an affiliated company.

2.1 TRANSFER PRICING REGULATIONS

According to the rules provided for in Sec. 18 of the CIT Act, the taxpayer has to adjust the tax base if prices applied in related party transactions are not at arm's length. This adjustment has to be implemented independently from any other tax base adjustment items.

Adjustment of the tax base is obligatory if the transfer price is not in line with the arm's length principle which results in a reduction of the pre-tax accounting profit. Otherwise, if the pre-tax accounting profit is higher due to the non-arm's length transfer price, a tax base reduction is available upon the fulfilment of certain conditions.

2.2 METHODS

The CIT Act, in compliance with the OECD Transfer Pricing Guidelines, provides as methods for determining the arm's length price the comparable uncontrolled price method, the resale price method, the cost-plus method, the transactional net margin method, the transactional profit split method or any other methods if the arm's length price cannot be determined by either of the methods referred to above.

2.3 DOCUMENTATION REQUIREMENTS AND PENALTIES

On 18 October 2017, the Ministry of National Economy issued its decree on the documentation obligation for the determination of arm's length price (»NGM Decree«), replacing the prior relevant rules. The NGM Decree reflects the compulsory changes triggered by BEPS Action 13 in the domestic law. The new regulations may also be applied to the financial year of 2017 on a voluntary basis and have become compulsory for the business years commencing on 1 January 2018 or thereafter.

In accordance with the provisions of the CIT Act and the rules laid down in the NGM Decree, taxpayers are obliged to keep records with regard to the transfer prices applied in their related party transactions.

The documentation obligation applies to all contracts concluded between related parties, provided that the transactions were actually implemented (i.e. goods were sold or services were rendered) based on the respective contract in the given tax year and the yearly transaction value exceeds HUF 50 million (approx. EUR 139,000). In accordance with the rules, the transfer pricing documentation consists of a masterfile and a local file. The local file should be prepared by the filing date of the CIT return for the first tax year in which revenues were received/expenses paid under the respective contract. The requirements of the local file can be included via cross-reference in the masterfile. Such reference shall be sufficient if the masterfile contains the information defined in the NGM Decree and it is available by the filing date of the Hungarian CIT return of the taxpayer. If the masterfile for the relevant financial year is not yet available on the basis of the deadline applicable on the group's ultimate parent company, then it is sufficient to prepare it by that deadline, but no later than 12 months after the last day of the taxpayer's tax year. A yearly update of the documentation is required.

A special default penalty of HUF 2 million (approx. EUR 5,556) per contract (or per transaction type) may be levied if the taxpayer fails to prepare the appropriate documentation. After the above deadline, the taxpayer should be able to present the transfer pricing documentation to the tax authorities within three days, upon request. In the case of recurrent infringement of the documentation, a penalty of up to HUF 4 million (approx. EUR 11,111) may be levied. Moreover, if the taxable person fails to complete the same documentation, the default penalty may be four times as much as it was the first time. The provisions applying to repeated infringements of a record preparation or keeping obligation related to the determination of the arm's length price or related to transactions concluded by a CFC, as well as the provisions applying to repeated infringements of keeping the same record, shall not apply if more than two years have passed between two consecutive infringements.

The Hungarian ultimate parent company that belongs to an MNE group exceeding the consolidated annual turnover of EUR 750 million is affected by the compulsory »country-by-country reporting« (CbCR) according to Section 1(8) of Act No. XXXVII of 2013. The Hungarian subsidiaries will have to support their parent companies to fulfil the CbCR.

The implementation of the CbCR obligation is final according to the BEPS-related Action Plans, and the legislation has been in force since 1 January 2016. The Hungarian CbCR model adopted the data content of the OECD template. Each ultimate parent entity of an MNE group that is resident for tax purposes in Hungary has to file a CbCR conforming to the requirements of the legislation with the Hungarian tax authority with respect to its reporting fiscal year.

A constituent entity of an MNE group that meets the following criteria is considered an »ultimate parent entity«:

(i) it owns directly or indirectly a sufficient participation in one or more other constituent entities of such MNE group, such is required to prepare consolidated financial statements under accounting principles generally applied in its jurisdiction of tax residence, or would be required if its equity participation were traded on a public securities exchange in its jurisdiction of tax residence; and

(ii) there is no other constituent entity of such MNE group that owns directly or indirectly a participation described in (1) in the first mentioned constituent entity.

The surrogate parent entity is considered one constituent entity of the MNE group that has been appointed by that MNE group as a sole substitute for the ultimate parent entity to file the CbC report in that constituent entity's jurisdiction of tax residence on behalf of that MNE group, when one or more of the conditions set out in the legislation applies.

The term »constituent entity« (or MNE group member) means

(i) any separate business unit of an MNE group that is included in the consolidated financial statements of the MNE group for financial reporting purposes, or would be so included if equity participation in such business unit of the MNE group were traded on a public securities exchange;

(ii) any such business unit that is excluded from the MNE group's consolidated financial statements solely on grounds of size or materiality; and

(iii) any permanent establishment of any separate business unit of the MNE group included in (1) or (2) above, provided the business unit prepares a separate financial statement for such permanent establishment for financial reporting, regulatory, tax reporting, or internal management control purposes.

The term »surrogate parent entity« means one constituent entity of the MNE group that has been appointed by an MNE group, as a sole substitute for the ultimate parent entity, to file the CbCR in that constituent entity's jurisdiction of tax residence, on behalf of such an MNE group, when one or more of the conditions set out above applies.

Where there is more than one constituent entity of the same MNE group, resident for tax purposes in Hungary, and one or more of the conditions mentioned above applies, the MNE group may designate one of these constituent entities to file the CbCR to the Hungarian tax administration with respect to any reporting fiscal year to notify the Hungarian tax administration that the filing is intended to satisfy the filing requirement of all the constituent entities of such an MNE group that are resident for tax purposes in Hungary.

In order to comply with the reporting obligation, the surrogate parent entity shall request the necessary information from the ultimate parent entity. In case the surrogate parent entity is not able to collect all the information, a CbCR shall be filed to the tax authority based on the available data. Concurrently, the surrogate parent entity shall notify the tax authority that the filing is intended to satisfy the filing requirements of the MNE group. Concerning incomplete reporting, the tax authority shall notify the competent tax authorities and shall examine if penalties are applicable.

The CbCR shall include:

¬ for each state in which the MNE group carries on business, the amount and currency of its revenue, its pre-tax profit, the amount of paid income tax, the amount of payable income tax, the amount of its subscribed capital, and tangible assets and cash, cash equivalents – amounts shall be presented in different categories according to Annex 3 of Act No. XXXVII of 2013; and

¬ the identity of the MNE group members, including the country of residence of the group members and, if different from the country of residence of the taxpayer, the law and the name of the principal business or activities of that group member.

In accordance with Section 43/O of Act No. XXXVII of 2013, any constituent entity of an MNE group that is resident for tax purposes in Hungary shall notify the Hungarian tax administration whether it is the ultimate parent entity or the surrogate parent entity. Where a constituent entity of an MNE group that is resident for tax purposes in Hungary is neither the ultimate parent entity nor the surrogate parent entity, it is a legal obligation to notify the Hungarian tax administration of the identity and tax residence of the reporting entity. The constituent entity shall notify the Hungarian tax administration no later than the last day of the reporting fiscal year of such an MNE group.

According to Section 43/S of Act No. XXXVII of 2013, in case of any default in filing the declaration, a penalty of a maximum of HUF 20 million (EUR 55,556) may be levied by the tax authority. The general rule is that the report has to be filed within 12 months from the last day of the financial year of the group.

2.4 ADVANCE PRICING AGREEMENT

In the framework of »Advance Pricing Agreements« (APA), on the basis of the facts and the precisely introduced circumstances of the related party transaction, the appropriate transfer pricing method and the arm's length price or price range (fair market value) will be determined by the tax authorities. In Hungary the APA is not an agreement between the tax authority and the taxpayer, but a resolution of the tax authority. As a general rule, applicants could be any taxpayers who are obliged to prepare TP documentation. The procedure may be unilateral, bilateral, or multilateral; the official filing fees for an APA, payable to the Hungarian Tax Authority, are HUF 2 million (approx. EUR 5,556) for a unilateral statement. In case of a multilateral statement, the fee is HUF 2 million multiplied by the number of competent authorities involved.

The arm's length price set by the tax authorities is valid for a period of three to five years. This period may be extended by an additional three years upon request, provided that the facts and the circumstances of the transaction are unchanged or affected by minor changes only. The only acceptable form is electronic, which can be the basis of the application and can be downloaded from the tax authority's website.

The administrative time limit for an APA procedure is 120 days, which may be extended on two occasions by 60 days; the procedure can thus last up to 240 days. This deadline does not include the time of discussions with the competent foreign authority, the time of the verification audit, nor the time elapsed for supplying missing information.

There is a new rule according to element 2.7 of the Action 14 minimum standard which states that countries with bilateral APA programmes should provide for the roll-back of APAs (to previous filed tax years not included within the original scope of the APA) in appropriate cases, subject to the applicable time limits (such as domestic law statutes of limitation for assessments) where the relevant facts and circumstances in the earlier tax years are the same and subject to the verification of these facts and circumstances on audit (OECD Guidelines Annex II to Chapter IV 69).

3 Controlled foreign corporations

As of 1 January 2019, the rules of the controlled foreign corporations (CFC) have been amended again compared to the previous years. Following the new rules, a foreign entity taxed with a lower effective tax rate as computed with the Hungarian rules may only qualify as a CFC if:

- (a) a Hungarian resident taxpayer holds a direct or indirect participation of 50% or more in such foreign corporation (together with the participation held by related party entities) (the respective rules as described above are still valid); and
- (b) non-genuine transactions are performed, which means that the principal aim of the transactions performed by the foreign corporation is to gain tax advantages and at the same time the important functions are performed and the risks are assumed by a Hungarian entity for the purposes of the foreign entity, while the foreign corporation formally holds both assets and personnel for the purposes of conducting business activities.

Regardless of the above, the foreign entity does not qualify as a CFC if:

- the pre-tax profit established according to the law of the foreign person's state of tax residence or of the foreign business establishment's state of location represents profits of no more than HUF 243,952,500 (approx. EUR 677,646), and from 24 July 2019 the non-trading income represents profits of no more than HUF 24,395,250 (approx. EUR 67,765); or
- if the pre-tax profit established according to the law of the foreign person's state of tax residence or of the foreign business establishment's state of location amounts to no more than 10% of its operating costs.

Additionally, those foreign persons and foreign business establishments that are settled in a fiscally non-cooperative state cannot be exempted from being qualified as a CFC. A decree issued by the Minister of Finance has established the list of fiscally non-cooperative states (so-called »blacklisted states«).

The following are non-trading income: interest; income from financial assets; income from intellectual property rights; income arising from the holding and derecognition of stocks and shares; income from finance leasing; income from insurance, banking and other financial activities; income received from a person earned by the supply of goods and services to, or by purchasing goods and services from, affiliated companies, if the activity of such person does not represent any added economic value, or the added economic value is insignificant.

The operating costs shall not include the cost of goods sold outside the country where the foreign person is resident or where the foreign business establishment is situated, and the costs, expenditures accounted for in the books of the company on the basis of payments to affiliated companies.

Furthermore, the foreign entity does not qualify as a CFC if situated in a state other than any Member State of the European Union or the European Economic Area, with which Hungary has an agreement granting exemption from corporate taxation in Hungary with respect to the foreign business establishment's income, and if it qualifies as a business establishment according to said agreement.

The burden of proof lies with the Hungarian taxpayer connected to the CFC regulation. The taxpayer should keep detailed documentation on every transaction carried out with a CFC. Failure to provide this documentation results in similarly strict penalties (HUF 2 million, HUF 4 million or up to four times the first penalty in case of repeated offence) as for the lack of transfer pricing documentation (see I.C.2).

The CIT Act contains the following provisions with respect to CFC.

3.1 DIVIDENDS

According to the CIT Act, dividends received are generally tax exempt under the participation exemption rules that are equally valid for domestic and foreign shareholdings. This exemption, however, is not applicable for dividend income received from a CFC. However, dividends received from a CFC may, in part, be exempted from tax as a deductible item. Dividends from a CFC are exempted from taxation to the extent that they are associated with a genuine arrangement carried out by the CFC. As a result, if a CFC has both genuine and non-genuine arrangements, only the non-genuine arrangement will be subject to Hungarian corporate income tax liability. Thus, the dividend of the CFC arising from the genuine arrangement receives the same benefit as the dividend from the company which does not qualify as CFC.

The special rules concerning the exemption of foreign-source income are summarized in II.A.1.

3.2 COSTS AND EXPENSES

According to Hungarian tax law, costs and expenses paid to a CFC are generally not tax deductible, except if the taxpayer proves that the costs and expenses are for the purpose of its business activity (qualified deductibility). The business nature of costs and expenditures cannot be justified in the case of provision of assets or services free of charge, other donations provided to foreign entities or entities managed outside of Hungary or liabilities taken over from such entities free of charge.

3.3 REPORTED PARTICIPATION

The tax exemption on capital gains for the alienation of reported shares is not available in connection with CFC. However, capital gains in connection with a CFC are exempted from taxation to the extent that the income arises from a genuine arrangement of a CFC.

4 Exit taxation

Hungary has implemented the exit tax rules for CIT purposes based on the EU »Anti-Tax Avoidance Directive« (ATAD). In accordance with the new legislation, exit tax is imposed in the following cases:

¬ transfer of the place of management to another country along with the tax residence of the taxpayer (except for assets that remain effectively connected to a domestic permanent establishment);
¬ transfer of assets from the domestic head office to the permanent establishment in another country, or from the domestic permanent establishment to the head office/permanent establishment in another country, provided that the assets do not trigger any tax liability in Hungary after the transfer;
¬ transfer of the business of the domestic permanent establishment to another country, provided that the assets do not trigger any tax liability in Hungary after the transfer.

In case of the above, 9% CIT shall be paid on the difference between the fair market value of the transferred assets (business) and their book value calculated for tax purposes. These values of the assets are to be determined at the time of the transfer.

If the place of management, assets, or business carried on by the permanent establishment in Hungary are transferred to another EU or EEA country, the taxpayer is entitled to opt for a deferral of the exit tax liability. Accordingly, the exit tax shall be paid in 5 equal installments over 5 years. However, in certain cases the deferred tax liability will be due immediately (e.g. if the taxpayer alienates the transferred assets or business); such events shall be notified to the Hungarian Tax Authority within 15 days.

Nevertheless, exit tax rules are not applicable to transactions connected to collateral or security financing, or if the assets are transferred for the fulfillment of prudential capital requirements or for the purpose of liquidity, if the assets return to Hungary within 12 months.

5 Hybrid mismatches

Restrictive rules with respect to the taxation of hybrid instruments were introduced as of 1 January 2020 in accordance with the implementing obligations laid down by the ATAD. Based on new regulations, if the income is not taxable in either country due to the different characterization of payments or entities in the countries' tax systems, the tax base shall be adjusted to avoid double non-taxation (i.e. deduction is denied). The provisions on hybrid mismatches are applicable to intra-group transactions and structured arrangements.

6 DAC 6 reporting obligation

On 25 May 2018, the Economic and Financial Affairs Council adopted a sixth amendment to the Directive on Administrative Cooperation (DAC 6) which requires so-called tax intermediaries to report, on a mandatory basis, specific cross-border arrangements (besides companies, permanent establishments may be affected). Cross-border arrangements are only subject to the reporting obligation if defined characteristics, »hallmarks«, are fulfilled, e.g. buying a loss-making company to exploit its losses in order to reduce tax liability, converting income into capital in order to obtain a tax benefit, deductible cross-border payments between associated enterprises where the recipient is essentially subject to no tax, zero, or almost zero tax, or specific hallmarks concerning transfer pricing like use of unilateral safe harbours, the transfer of hard-to-value intangible assets when no reliable comparables exist and the projection of future cash flows or income is highly uncertain.

DAC 6 has been implemented in national Hungarian law through Act No. XXXVII of 2013. The disclosure obligations only apply to cross-border ar- rangements with retroactive effect from 25 June 2018. VAT, excise duties and social security contributions are excluded from the scope of the reporting obligation, while all other taxes are covered. However, lawyers benefit from a waiver. For professionals other than lawyers, a waiver because of a »tax secret« or »business secret« can probably not be applied, because a »tax secret« is only defined in the relation between the tax authority and the taxpayer. According to the legislation, the taxpayer himself may also be liable for reporting.

With regard to the DAC 6 regulation, in 2020 Hungary used the possibility of a deadline extension allowed by Council Directive EU 2020/876, amending Council Directive EU 2011/16 to defer certain time limits for the filing and exchange of information in the field of taxation because of the COVID-19 pandemic. Accordingly, the related DAC 6 reporting deadlines have been postponed or extended by 6 months. For cross-border arrangements started between 25 June 2018 and 30 June 2020, the original deadline of 31 August 2020 for reporting was changed to 28 February 2021. For cross-border arrangements between 1 July 2020 and 31 December 2020, the 30-day reporting deadline started on 1 January 2021. The reporting obligation for marketable arrangements must be met for the first time by 30 April 2021.

In case of DAC 6, a procedural rule has been introduced to allow the tax authority to provide the reporting intermediary with a unique Member State reference number for the reportable cross-border arrangement. Where more than one intermediary or relevant taxpayer is required to provide information, each transaction in the same arrangement must bear a single reference number in order for those transactions to be linked to a single agreement. This is ensured by the rule prescribed by the domestic law that the first data provider must forward the reference number received from the tax authority to the other data providers known to him. The notification obligation of the intermediary exempted from the reporting obligation also covers the Member State reference number of the cross-border arrangement subject to the reporting obligation. The scope of the identification data of the intermediary and the relevant taxpayer has been expanded with the address, in order to make the identification based on the widest and most accurate data possible.

While DAC 6 proposes a uniform mandatory disclosure rule framework, it can be expected that national implementation will result in a non-uniform set of rules, which calls for an adequate coordination amongst involved intermediaries. Please be aware of the DAC 6 obligation in case of any cross-border transaction, especially if a restructuring, merger, or acquisition is planned. Failure to comply with DAC 6 could mean facing significant sanctions (penalty ranging from EUR 1,400 to EUR 14,000) and reputational risks for businesses, individuals, and intermediaries.

D VALUE ADDED TAX

1 Taxable persons

In general, taxable transactions carried out by a taxable person in Hungary are subject to VAT. »Taxable person« within the meaning of the Hungarian Act on VAT covers individuals and entities (with or without legal personality) that carry on business activities in their own name, regularly or on a professional basis, irrespective of the activity's place, purpose, and result. Also, non-resident persons (persons without a seat or fixed establishment in Hungary) may be subject to VAT if they carry on taxable transactions in Hungary.

Associated persons/enterprises having their fixed establishment or habitual residence in Hungary are allowed to form a VAT group. By joining the VAT group, the independent taxpayer status of each individual member ceases and the group will become a single taxpayer from a VAT perspective. Transactions among the members qualify as out-of-scope items from a VAT perspective, while members act under one single tax number in their external business relations. This, however, will not affect other taxes. A company may join only one VAT group at the same time and the VAT Act does not require all associated enterprises to become members of such a group. Nevertheless, associated enterprises may be jointly and severally liable for the VAT of the group.

Private persons may be subject to VAT if goods from countries outside the European Community are imported into Hungary (i.e. import VAT) or if passenger cars are acquired in the European Union (intra-Community acquisition). Private persons may also be subject to VAT upon the supply of certain real estate on a regular basis.

2 Taxable transactions

2.1 SUPPLY OF GOODS AND SERVICES

The concept of supply of goods implies a transfer of the (economic) ownership of tangible property. Performing construction work is also regarded as a supply of goods.

Supply of services means any transaction that does not constitute a supply of goods. Services may consist in a positive action (e.g. the rendering of services) or tolerating actions of other persons (e.g. the leasing of immovable property, use of rights and patents).

A supply is also the withdrawal of goods or the use of goods by a taxable person for his private use or for that of his staff if the goods form a part of the business of the taxable person.

Irrespective of the above, donations for public purpose, and provision of samples or small value items (below a market value of HUF 5,000 (approx. EUR 14) including VAT) for business purposes do not constitute a supply for VAT purposes.

2.2 WITHDRAWAL (SELF-SUPPLY)

Self-supply within the meaning of the Act on VAT comprises (i) the use of business assets for private purposes or for the use of the staff or their disposal free of charge; (ii) the supply of services carried out free of charge by the taxable person for his private use, or for that of his staff, or to third parties for non-entrepreneurial purposes (e.g. donation).

Self-supply is taxable only if the acquisition of the goods that are the object of self-supply entitled to an input VAT deduction.

2.3 IMPORT

The transfer of goods from a country outside the Community to Hungary is subject to import VAT. The Hungarian system generally does not allow for the postponed assessment of import VAT; in certain cases, however, self- assessment of import VAT or self-assessment by means of an indirect customs representative may be applicable. In the absence of such, under the general rules, import VAT paid is refundable within the framework of the VAT return. Further, VAT exemption is applicable for services related to the supply of imported goods (e.g. packaging, freight, etc.), if they will be provided directly to the person who imports, supplies, or acquires the actual goods.

2.4 INTRA-COMMUNITY ACQUISITIONS

An intra-Community acquisition is the acquisition of goods transported from an EU Member State to Hungary, provided that both the supplier and the recipient are taxable persons for VAT purposes. The supplier carries on a tax-exempt intra-Community supply, while the recipient effects an intra-Community acquisition upon which he must pay VAT and may deduct it under the general conditions.

A transfer of goods forming part of business assets by a taxable person from an EU Member State to Hungary must also be treated as intra-Community acquisition of goods for consideration (deemed supply of goods), unless further conditions are met.

3 Place of supply

3.1 SUPPLY OF GOODS

The supply of goods and services will only be taxed under the Act on VAT if the place of supply is considered to be Hungary.

According to the general rule, the place of supply of goods is deemed to be the place where the goods are located at the time the right to dispose of them as an owner is transferred to the recipient.

If the goods are dispatched or transported by the supplier, by the recipient or by a third person (carrier), the place of supply is the place where the goods are located at the time when dispatch or transport of the goods to the recipient begins.

Special rules are – inter alia – applicable for »distance selling« where goods are supplied to private customers and are dispatched by the supplier from one EU Member State to another EU Member State (special administrative rules apply). In the case of distance selling, the place of supply is not the place of departure of the goods, but the place where the goods are located at the end of transport. Intra-Community acquisitions are, in general, taxable where the dispatch or transport of the goods ends.

3.2 SUPPLY OF SERVICES

The Hungarian provisions on the place of supply of services are in line with the periodic amendments of the EU VAT Directive (2006/112/EC). Therefore, the place of supply of services must be determined depending on the taxable status of the recipient (B2B or B2C transactions).

B2B transactions
In general, the supply of services to taxable persons is taxable at the place where the recipient is established (has a seat or a fixed establishment to which the service is supplied; in the absence of such a place, domicile or habitual residence). If the taxpayer has several permanent establishments, the place of supply will be the place of permanent establishment mainly concerned or the seat.

However, there are several particular regulations for determining the place of supply of services, as well (see the table below).

B2C transactions
If the services are supplied to non-taxable persons, they are generally taxable at the place where the supplier has established his business or has its fixed establishment. However, there are again some exceptions (as indicated in the table below).

In the case of telecommunications, broadcasting and electronic services, the place of B2C supply is where the customer is established (resides). The MOSS (Mini One-Stop-Shop) system has been introduced in Hungary accordingly.

The following table provides a brief overview of how the place of supply is determined in 2021.

	B2B SERVICES	B2C SERVICES
main rule	where the customer is established	where the supplier is established
special rules		
connected with immovable property	where the property is located	where the property is located
passenger transport	where the transport takes place	where the transport takes place
services in respect of admission to cultural, scientific and similar events	where physically carried out	where physically carried out
restaurant and catering services	where physically carried out, or place of departure (during transport)	where physically carried out, or place of departure (during transport)
short-term hire of means of transport	where put at disposal	where put at disposal
long-term hire of means of transport	where the customer is established [1]	where the customer is established [1]
agency services	main rule: where the customer is established	the place of the underlying supply
transport of goods		where the transport takes place
intra-community transport of goods		place of departure
work on goods, valuation of goods		where physically carried out
cultural, artistic, scientific, educational, leisure and sport services		where physically carried out
catalog services		where the customer is established, provided that it is outside of the EU
telecommunications, broadcasting, e-services	where the customer is established	where the customer is established

1 The hire of ships for leisure purposes in B2C relations is to be taxed where it is put at disposal.

4 Taxable amount

In general, the taxable amount is determined by the consideration received for the supply of goods and services, excluding the VAT itself. The taxable amount may be adjusted if the consideration significantly differs from the market price and the supplier or the customer is not entitled to full deduction of input VAT. Previously, no VAT adjustment was granted if losses were caused by the insolvency of the customer, but as of 2020 it is possible to request a refund of VAT paid in connection with »bad debts« directly from the tax authority if the special requirements defined by law are met (valid for losses occurred after 2016).

5 Tax rates

In Hungary the following VAT rates are applicable:

27%	standard VAT rate
18%	reduced VAT rate for basic foodstuffs (milk and dairy products except mother's milk and products taxed under the rate of 5%, cereals, flour), accommodation
5%	reduced VAT rate, which applies, in particular, to certain kinds of pharmaceutical products for use by humans, medical equipment, aids, other appliances normally intended to alleviate the treatment of disability, books, sheet music, newspapers, periodicals and the district heating of households, pork industry and certain other meat products (e.g. various parts of beef, sheep and goat) and pork products specified by law. As of 2016, for a temporary period of four years, the reduced VAT rate was also applicable to new and unused real estate under certain conditions. As of 2018, the meals and food prepared in restaurants and the supply of non-alcoholic beverages as well as internet-access services and fish for consumption are also taxed at a rate of 5%. Furthermore, a unified VAT rate is applied to the different types of milk, i.e. a 5% VAT rate is chargeable to ESL and UHT milk as well. Transitional rules were applicable for flats (apartments), as the special reduced rate ceased to apply from 2020; however, transitional provisions are only available until the end of 2023 for construction projects that are already underway. As of 2021, the applicable tax rate for newly built flats with a floor area of max. 150m² and houses with max. 300m² is 5%. Further, 5% is applicable to commercial accommodation services.

6 Exemptions

The numerous exemptions from VAT can be classified in two categories, depending on whether or not they preclude the deduction of input VAT. The most important exemptions are listed below.

VAT exemptions including the right to deduct input VAT:

¬ export of goods (goods are transported outside the Community);
¬ intra-Community supply of goods;
¬ cross-border transport of export goods;
¬ cross-border transport of passengers regardless of the means of transportation (either on the public highways, by vessels, or aircraft); and
¬ work on and processing of goods to be exported outside the Community.

VAT exemptions, precluding the deduction of input VAT, include:

¬ banking and financial transactions as well as insurance transactions;
¬ the supply of buildings older than two years and land plots other than construction sites, see II.B;
¬ leasing or letting of immovable property or parts thereof;
¬ certain educational services;
¬ services supplied by dentists, doctors or paramedical professions;
¬ cooperating partnerships; and
¬ a special exemption for small businesses.

In accordance with the EU VAT Directive (2006/112/EC), a further type of tax exemption exists with regard to the activity of the cooperating partnership. The services provided by the cooperating partnership to its members (the members can only be non-taxable persons, or a person – recipient of the service – acting as a non-taxable person) are tax exempt without the right to deduct the VAT. Additionally, detailed criteria have to be fulfilled in order to be able to apply this tax exemption rule.

Under special conditions the sale of an existing business division can fall outside the scope of VAT (transfer of business in a going concern, »TOGC«). These conditions are:

¬ the division has been acquired with the purpose of its further operation;
¬ the alienator is regarded as a taxable person in Hungary and assumes the liability for the rights and obligations deriving from the business division as legal successor;
¬ the business division should not carry out activities, in respect of which VAT is not deductible (even a minor portion leads to the application for the outside-the-scope treatment being refused).

7 Input VAT deduction

A taxable person is entitled to deduct the VAT paid on goods and services, importations and intra-Community acquisitions if the following conditions are fulfilled:

¬ the supply of goods or services is carried out in Hungary;
¬ by another taxable person;
¬ for the business purposes of the recipient;
¬ a properly issued invoice is available; and
¬ no VAT exemption precluding VAT deduction is applicable.

Finally, the amount of the VAT liability in a taxable period consists of the VAT due on taxable transactions carried out by the taxable person less input VAT paid in the same period. The assessed VAT must be paid to the tax authorities, while the aggregated deductible VAT may be (1) carried forward to future tax periods or (2) be refunded by the tax authorities. The right to deduct input VAT is open during the statutory limitation. However, as of 2016 a taxable person may only account for the VAT deduction in the actual VAT assessment period for two years. Over this limit, the VAT deduction right may only be exercised by a self-revision of the original period when VAT became deductible.

The refund of VAT may be claimed, irrespective of the financial settlement status of the underlying invoices (result of Case C-274/10). The claim for VAT refund by a creditable taxpayer is possible within 30 days. In case of public limited companies with creditable taxpayer status, the tax authority executes the payment of a VAT refund within 20 days. The claim for VAT refund of other taxpayers is possible within 45 days or 75 days. The reclaimed VAT will only be refunded within the shorter period if all the invoices regarding input VAT have been paid. Failing the payment condition but reclaiming the shorter term may be penalized by 5% default penalty, or at least HUF 500,000 (approx. EUR 1,390).

8 VAT liability

In general, a taxable person carrying out a taxable transaction is liable to pay the invoiced VAT to the tax authorities.

Exceptions apply – inter alia – for intra-Community acquisitions, where the recipient of goods is subject to VAT. Further, in the case of supply of goods with installation/assembly and of supply of services carried out by a foreign taxable person (no seat or fixed establishment in Hungary) to another taxable person, the VAT liability shifts from the supplier to the recipient (reverse-charge mechanism).

Nevertheless a cash accounting scheme may be opted by the taxable person provided that the below conditions are fully met. This means that VAT becomes payable at the supplier only when the respective payment was effected by the customer. This also means that the recipient of the goods/services may only deduct the VAT charged in the invoice if the financial settlement has been completed. In such a scheme, a special indication and reference is necessary on the invoice.

Small-sized enterprises according to the terms of the respective act may only opt for the cash accounting if they fulfill the following conditions:

¬ the place of establishment is in Hungary (for lack of such, the domicile or habitation);
¬ do not fall under liquidation or voluntary dissolution procedures;
¬ did not opt for tax exemption;
¬ the net value of sales revenues on supply of services and goods did not exceed HUF 125 million (approx. EUR 347,220) in the previous year nor is likely to exceed this threshold in the given year. When calculating this threshold, not only domestic but all transactions must be considered.

9 Tax assessment

9.1 RESIDENT TAXABLE PERSONS

Any taxable person who starts or carries on business activities in Hungary must register for VAT purposes with the tax authorities, irrespective of any turnover thresholds. A taxable person carrying out taxable transactions has to file either monthly or quarterly VAT returns depending on the level of their activity. In general, the VAT return filing deadline is the 20th day of the month following the VAT assessment period. A VAT return may also be filed on an annual basis; however, this is not relevant for persons carrying out intra-Community activities. Tax due must also be paid by the deadline for filing the VAT return.

In addition, taxable persons carrying out intra-Community supplies and acquisition of goods or services have to file recapitulative statements on their intra-Community supplies and acquisition of goods and services indicating the VAT identification number of the other party.

Both the supplier and the recipient are subject to a detailed reporting obligation (so-called »domestic itemized reporting«) for invoices. However, at the same time, the outgoing invoices do not fall under the domestic itemized report liability, as the seller reports via the so-called »electronic on-time data submission system«. The mentioned domestic itemized reporting obligation must be applied to all invoices issued by a domestic supplier.

The domestic VAT ID number of the recipient is to be indicated on all domestic invoices without any limitation.

Electronic on-time data submission is required for invoices issued, without any limit in value at the time of invoicing. However, at the same time, the outgoing invoices do not fall under the domestic itemized report liability. Consequently, the tax authority has immediate information about outgoing invoices throughout the direct connection; further, control data is also available based on the domestic itemized report of the recipient which still remains applicable for incoming invoices. For manual invoices, weekly or daily data reporting must be provided to the tax authority via a dedicated webpage depending on the amount of VAT. Taxpayers are required to provide data on a daily basis in case the VAT amount is equal to or exceeds HUF 500,000 (approx. EUR 1,390) data reporting every four days is prescribed if the amount of VAT is charged between HUF 100,000 and HUF 500,000 (approx. EUR 280 and 1,390).

Resident taxable persons fulfill their filing obligations electronically.

After a transitional period, from 1 July 2018 an electronic on-time data submission is required for issued invoices over a VAT amount of HUF 100,000 at the time of invoicing. However, at the same time, the outgoing invoices do not fall under the domestic itemized report liability. Consequently, the tax authority has immediate information about outgoing invoices throughout the direct connection; further, control data is also available based on the domestic itemized report of the recipient which still remains applicable for incoming invoices. The electronic on-time data submission will be extended as of 1 July 2020 to all outgoing invoices issued to a domestic client (issued with VAT without any threshold, issued with reverse charge mechanism, or issued without VAT). As of 1 January 2021, the reportation obligation will cover all outgoing invoices (i.e. invoices for IC supplies as well as export supplies). For manual invoices, weekly or daily data reporting must be provided to the tax authority via a dedicated webpage depending on the amount of VAT. Taxpayers are required to provide data on a daily basis in case the VAT amount is equal to or exceeds HUF 500,000 (approx. EUR 1,540) data reporting every five days is prescribed if the amount of VAT is charged between HUF 100,000 and HUF 500,000 (approx. EUR 308 and 1,540).

Resident taxable persons fulfill their filing obligations electronically.

9.2 FOREIGN TAXABLE PERSONS

Foreign taxable persons (no seat or fixed establishment in Hungary) carrying out taxable transactions in Hungary have to register for VAT purposes at the Directorate of Exclusive Taxpayers of the tax authorities and submit monthly VAT returns, domestic itemized reports and respective recapitulative statements electronically.

Moreover, foreign taxable persons who do not have their permanent residence, seat or fixed establishment in the European Community must have a fiscal representative if they carry out supplies subject to Hungarian VAT. The engagement of a fiscal representative is not obligatory if the foreign taxable person already has at least one VAT registration number in one of the EU Member States.

Foreign taxable persons who do not carry out taxable transactions in Hungary may claim a cross-border refund of input VAT incurred in line with the provisions of the EU VAT Directives. Taxable persons established in another Member State may initiate the refund by filing an application with their competent national tax authorities. The cross-border VAT refund scheme is also availble for taxable persons established in Norway, Switzerland, Liechtenstein, Serbia, or Turkey – due to their bilateral reciprocity agreements concluded with Hungary – by way of a reclaim application sent directly to the Hungarian Tax Authorities.

As of 2020, a so-called »special tax refund procedure« has been introduced, whereby a taxable person may initiate a refund of input tax paid if, for any reason beyond his control, it was not otherwise recovered/reimbursed in accordance with the principle of fiscal neutrality. The procedure is time barred and subject to several conditions.

10 Quick Fixes

10.1 PROOF OF TRANSPORT RELATED TO INTRA-COMMUNITY SUPPLIES

As of 2020, if the seller is responsible for the transport of the goods, in order to consider the transport as proven, the seller has to have two documents from the list of type 1 documents, or one from the list of type 1 documents and one from the list of type 2 documents issued by independent parties,

- Type 1 documents are the following: signed CMR document or CMR note, bill of lading, airfreight invoice, invoice issued by the carrier of goods.
- Type 2 documents are the following: insurance or bank documents, documents issued by a notary confirming the arrival of the goods in the Member State of the destination, a receipt issued by a warehouse keeper confirming the storage of the goods in that Member State.

If the goods are transported by the customer, the seller should obtain a written statement from the customer for the purposes of raising the presumption that includes data on the name and address of the customer, on the quantity and nature of the goods, and on the date and place of the arrival of the goods.

10.2 APPLICABILITY OF TAX EXEMPTION IN CASE OF INTRA-COMMUNITY SUPPLIES

As of 2020, a formal condition of the tax exemption of intra-Community supplies is that the seller has to know the customer's valid EU VAT ID number. Another condition for tax exemption is that the seller submits an EC sales list with the supply.

10.3 CALL-OFF STOCK SIMPLIFICATION

The simplification rules regarding consignment stocks are applicable to the goods delivered into the stock after 1 January 2020. This also requires proper administration from the parties. As of 2020, Hungary has also adopted the changes incorporated in the VAT Directive; the VAT Act is therefore modified according to the so-called »quick fixes«. The modified version of the Hungarian VAT Act is in line with the Directive. The simplification regarding consignment stocks was available in Hungary to date; however, taxable persons having a Hungarian VAT ID number were excluded from this regime. As of 2020, in line with the VAT Directive, the existence of a Hungarian VAT ID number does not exclude the applicability of the simplification; however, in case of a Hungarian fixed establishment of the supplier, the simplification is no longer available.

10.4 RULES OF CHAIN TRANSACTION

The standardized rules affect those supply chain set-ups where the goods are directly transported from the first supplier to the final customer, and the transport is organized by a party (intermediary) who is involved in the chain, both as a customer and as a seller.

As regards the determination of the sale of goods to which the transportation is linked, the presumption remains the same, i.e. that the intermediary party arranges the transport as a customer. In order to rebut this presumption, this customer should inform its seller about the VAT number declared by the Member State from which the goods were dispatched.

If the parties cannot provide the authorities with any proof of communication of the VAT number during a tax audit, but they consistently treated the acquisition of the intermediary party as a domestic supply, the presumption can also be rebutted.

E OTHER BUSINESS-RELATED TAXES

1 Local taxes

Municipalities may levy taxes on property located or on business activities performed by individuals or legal persons within their territory.

Individuals or legal persons carrying on business activities in the territory are subject to local business tax (»trade tax«) and the owners of property situated there are subject to municipal property tax. A non-resident individual or legal person is also subject to the municipal property tax or local business tax, unless a treaty is applicable or an exemption is granted on the basis of reciprocity. The maximum tax rates are generally regulated by law, but the local municipalities may provide for lower tax rates or in restricted cases even for tax exemptions.

Municipalities are allowed to levy self-defined municipal taxes as well. The potential tax objects and subjects can be determined by the local government with regard to the legal restrictions.

A list of all local and municipal taxes imposed by municipalities is available on the following website: https://hakka.allamkincstar.gov.hu

1.1 TRADE TAX (LOCAL BUSINESS TAX)

Business activities are subject to trade tax levied annually on the adjusted net sales revenues. The trade tax amounts to a maximum of 2%. As a part of the COVID-19 relief measures, the local business tax rate of SMEs is capped at 1% for the business year ending in 2021.The adjusted net sales revenues for local business tax purposes comprise the total accoun- ting net sales revenues reduced by the costs of materials, the sum paid to subcontractors, the purchase price of the goods sold, the costs of interme- diated services and the direct R&D costs. Further, the income from business activities carried on by a foreign permanent establishment is also part of the net sales revenues whereas royalty income is not. As of July 2016, the Act on local taxes was amended by the term »royalty«, which does not entirely correspond to the modification of the term in the CIT. If more beneficial, the old term can be applied by determining the tax liability even until 2021 under the grand-fathering provisions in case the respective legal conditions are met.

As of 2018, solar power stations also constitute a permanent establishment for local business tax purposes and are subject to local business tax if the local government has introduced the local business tax on business activities in its jurisdiction.

When calculating the tax base for trade tax purposes, the deduction of the purchase price of goods sold and the value of intermediate services may only be deducted from the net sales revenues at progressive rates. The reduction of the net sales revenues with the items mentioned above may be

- 100% up to the net sales revenues of HUF 500 million (approx. EUR 1.39 million) – tax exemption;
- 85% between HUF 500 million and HUF 20 billion (approx. EUR 1.39 million and EUR 55.5 million);
- 75% between HUF 20 billion and HUF 80 billion (approx. EUR 55.5 million and EUR 222 million);
- 70% exceeding HUF 80 billion (approx. EUR 222 million).

In the case of related parties according to the CIT Act, whereas the related party status was established as a consequence of a demerger carried out after 1 October 2016, if the purchase price of goods sold and the value of intermediate services together exceeds 50% of the net sales revenue, group taxation must be applied, and the tax base is calculated by cumula-ting this data from the related parties. This method shall be applied only to the period of the year that is affected by the related company status after the demerger.

Freight forwarding companies may deduct 7.5% of all the Hungarian and foreign road toll fees.

In addition, the local municipality may grant the deduction of 10% of direct R&D costs to all taxpayers from the tax payable.

Special rules must be applied by taxpayers who choose to prepare their annual report based on the IFRS regulations.

As trade tax is payable to each municipality on the territory of which an enterprise carries on a business, the tax base payable is divided by a special split calculation among the respective municipalities.

Tax returns on local taxes shall be submitted electronically on a standardized form to the Hungarian tax authority.

Prepayment of the local business tax is due twice a year.

1.2 MUNICIPAL PROPERTY TAX

In particular, the list of property taxes includes building tax levied at HUF 1,100 per m² (approx. EUR 3 per m²) or 3.6% of the market value of the real estate, and land tax due to HUF 200 per m² (approx. EUR 0.5 per m²), or 3% of the market value of the real estate. Municipalities may also apply lower tax rates. The tax base is either the size or the adjusted market value of the real estate, depending on the decision of the respective municipality.

Advertising media deployed on any real estate property located in the area of the jurisdiction of any municipal government are also taxable at the ma-ximum of HUF 12,000 per m² (approx. EUR 37 per m²) as a second type of the building tax.

1.3 OTHER MUNICIPAL TAXES

Local governments are allowed to define and levy new local taxes (»other municipal taxes«) within their territory. Other municipal taxes can be levied on any taxable objects that are not subject to any other local/central taxes or duties. Taxable persons cannot be local governments, states, organizations or entrepreneurs, but private individuals. In addition, local governments cannot introduce any municipal taxes that are prohibited by law.

The law does not declare any limitations concerning the potential tax rate and the maximum number of the municipal taxes that can be introduced by one municipality.

2 Duties

In Hungary the Act on Duties determines transfer, inheritance and gift taxation. Procedural fees and fees for administrative and court proceedings are also incorporated in the Act on Duties.

2.1 TRANSFER TAX ON SALES

Transfers of immovable property and of certain movable property such as cars, trailers are subject to transfer tax, based on the market value of the transferred property payable by the acquirer. Market value is precisely defined by law. In this connection the Hungarian Tax Authority may apply different real estate appraisal methods. The purchase of immovable property and cars within the framework of financial leasing contracts also triggers tax liability. Real estate transfer tax is levied on the transfer of immovable property (land and buildings) located in Hungary, on the transfer of certain rights related to immovable property and on the transfer of shares held in a real estate company. Taxable transactions include – inter alia – the sale, contribution in kind, and exchange of immovable property. The transfer of the right for pursuit of private medical practice, however, is exempted from transfer tax.

Transfer tax is levied on the acquisition of shares of a real estate company if the acquisition results from a non-preferential restructuring (preferential restructuring: preferential reorganizations, preferential exchange of shares and preferential transfers of assets determined by the CIT Act are exempt if the conditions are met) and if due to that transaction a shareholding of at least 75% in the respective company is obtained. The acquisition must be reported to the competent tax authorities even in cases where tax exemption is applicable.

As of 1 January 2014, the transfer tax liability no longer depends on the main activity of the company owning real estate.

The definition of a company owning real estate is very similar to the definition introduced by the CIT Act (see II.B). For transfer tax purposes, a company qualifies as a real estate company:

¬ if more than 75% of the cumulated asset value in the balance sheet of the company consists of immovable properties located in Hungary; or
¬ the company holds (directly or indirectly) a share amounting to at least 75% in a company whose immovable properties located in Hungary make up more than 75% of the cumulated asset value in its balance sheet.

The transfer tax base is the market value of the real estate owned by the company and depends on the participation of the respective shareholder in the real estate company. However, the transfer of the share held in a real estate company between related parties is exempt from transfer tax, if the main activity of the acquiring company is the rental or management of own or rented real property, or the sale and purchase of own real property.

The general rate for transfer tax is 4%. Special rules are applicable for shareholdings in a real estate company, for transfers of residential properties and of cars, and for the acquisition of real estate by leasing companies.

In case of shareholdings in a real estate company and of immovable properties, a transfer tax rate of 4% applies up to a value of HUF 1 billion (approx. EUR 278 million) and 2% above that threshold. The duty is capped, however, at HUF 200 million (approx. EUR 555,600) per property.

2.2 GIFT TAX

According to the Act on Duties, solely the donee is liable to gift tax. The transfer of real estate, movable property (which also includes liquid assets) without consideration and the gratuitous creation of a right of pecuniary value is subject to gift tax. Gift taxation is triggered if the gift is duly documented and the transfer takes place in Hungary.

The donation of movable property with a market value exceeding HUF 150,000 (approx. EUR 420) is subject to gift tax regardless whether the donation was documented or not. Furthermore, if the donation of movable property is duly documented the gift tax obligation arises regardless of the market value.

Donations between relatives in direct line (including adoption) and between married spouses and registered couples are fully tax exempt.

The general rate is 18%, where special rules are applicable for transfers of residential properties (9%) and of cars.

2.3 INHERITANCE TAX

Currently, a tax exemption of up to HUF 20 million (approx. EUR 55,600) applies to the transfer of property, provided that the beneficiary is the stepchild or foster child or the stepparent or foster parent of the decedent. Inheritances between relatives in direct line (including adoption) and the inheritance of a surviving spouse are fully exempt from tax obligations.

The general rate is 18%, where special rules are applicable to transfers of residential properties (9%) and of cars.

2.4 STAMP DUTIES

Stamp duties are levied as procedural fees on both administrative and court proceedings.

Administrative fees are levied at the time the proceedings are initiated on the party requesting such proceedings (e.g. proceedings related to obtaining Hungarian citizenship). Stamp duties may vary between HUF 100 (approx. EUR 0.30) up to HUF 8,000,000 (approx. EUR 22,200).

Procedural fees on court proceedings are levied on the filing of civil and administrative law suits with a court (in proportion to the value of the claim). In general, the fees amount to 6% of the value under dispute, but at least HUF 15,000 (approx. EUR 40) up to a maximum of HUF 1,500,000 (approx. EUR 4,100). In addition, procedural fees are levied by the Court of Registration on incorporation or any other change regarding the registration of companies. The fees vary from HUF 15,000 (approx. EUR 40) to HUF 600,000 (approx. EUR 1,660).

3 Customs duties

In general, all goods crossing the Hungarian border from non-EU countries (third countries) are subject to customs duties. The customs tariffs towards third countries are determined by EU legislation, and therefore the majority of the revenue is retained by the Community. In addition, various international agreements providing for customs exemptions or preferential customs tariffs apply.

As of May 2016 the regulations of the new Customs Code of the European Union were implemented and are applicable concerning Hungary as well.

4 Excise taxes

In accordance with EU Directive 2003/96, electricity, natural gas, and carbon are deemed energy products (in addition to tobacco, alcoholic drinks, and mineral oils) and excise duties are levied on them. (The separate energy tax on these products was abolished.)

The Hungarian compliance rules were amended as of 1 April 2017 (see Act LXVIII of 2016 on Excise Taxes). In line with the EU Directive, excise duties are levied on the production of excisable goods in the domestic territory, importation from non-EU countries, as well as the transportation of excisable goods released for free circulation to another Member State for commercial purposes or during transport within the framework of mail-order selling.

Commercial activities related to excisable goods need to be authorized by the Hungarian tax authority. Excisable goods may be produced and stored – in the framework of tax suspension arrangement – in tax warehouses until tax liability arises or untaxed excisable goods may be used in tax warehouses for tax-exempt activities, as determined in the Act on Excise Taxes.

In order to cover tax risks associated with the transportation under the tax suspension arrangement, excise tax security has to be provided. Excise tax security can be provided in the form of cash/bank transfer to the bank account of the Hungarian tax authority, financial guarantee or joint and several guarantee.

5 Environmental taxes

Environmental taxes are levied on certain activities that cause pollution of the soil, air or water. However, the tax is partly refunded if investments are made for purposes of protecting the environment, see Act No. LXXXIX of 2003 on Environmental Tax.

Moreover, for the first domestic supply or intra-company use of certain products (e.g. packaging material, tires, refrigerants, batteries, advertising paper, electric equipment, artificial plastic flowers, some chemical products and office papers as well) an environmental protection product fee is levied.

6 Surtaxes for financial institutions

Financial institutions are obliged to pay surtax. The tax base and the tax rate differ depending on the type of the financial institution. For example, the tax payable by credit institutions amounts to 0.15% of the modified balance sheet total (»banking tax«) up to HUF 50 billion (approx. EUR 139 million) and 0.2% above HUF 50 billion.

7 Company car tax

The company car tax is defined under the Act No. LXXXII of 1991 on Motor Vehicle Tax. Generally, automobiles (passenger cars) owned by other than private persons and with regard of which direct costs were deducted are subject to company car tax. However, electric cars and environmentally friendly cars are exempted. Company cars used for health care services by certain entities/organizations defined by law are tax exempted as well. The owner of the car according to the official registration or the lessee of the car in case of financial lease is liable for the tax payment. In case of cars owned by the Hungarian state, the person who exercises the right of utilization (or lacking that: the property management rights) of the car is liable to pay company car tax.

Automobiles not registered in Hungary may also be subject to company car tax.

The company car tax obligation falls into 12 categories, depending on the vehicle's engine power and environmental classification, and ranges from HUF 7,700 to HUF 44,000/month (approx. between EUR 21 and EUR 120 per month). Tax has to be calculated and declared by self-assessment on a quarterly basis.

8 Insurance tax

Insurance tax on certain types of insurances, if the place of occurrence of the risk is in Hungary, is payable. Besides Hungarian insurance service providers, cross-border insurance service providers are also subject to the tax. The tax base should be the service fee for the insurance services rendered, whereby the following tax rates are applicable:

- CASCO insurance: 15%
- property and accident insurance: 10%.

In case the tax base of the taxable person does not reach HUF 8 billion (approx. EUR 22.2 million) in the preceding year, the following tax rates apply:

- up to the tax base of HUF 100 million (approx. EUR 278,000): 25% of the abovementioned tax rates (i.e. effective tax rate is 3.75%/2.50%);
- between HUF 100 million (approx. EUR 278,000) and HUF 700 million (approx. EUR 1.94 million): 50% of the abovementioned tax rates (i.e. effective tax rate is 7.50%/5.00%);
- exceeding HUF 700 million (approx. EUR 1.94 million) the abovementioned tax rates.

In case of compulsory insurance of motor vehicles, the tax base is the insurance fee, which is taxed at a rate of 23%.

9 Public health tax

A public health product tax (Act No. CIII of 2011) is levied upon the sale of soft drinks, energy drinks, pre-packed sweets, salted snacks, culinary flavorings, flavored beer, alcoholic beverages, fruit jam and juices.

The person or organization first selling the product in Hungary (i.e. the manufacturer, importer, distributor) is subject to tax. In addition the import and intra-Community acquisition of products that are ingredients to the manufacturing of new products for sale in Hungary also trigger the tax liability.

The tax rates depend on the categories. Under specific circumstances, export within the European Union or to countries outside the EU is tax exempt. No tax obligation will arise either if the merchant sells less than 50 liters or 50 kilograms of the taxable products in a calendar year.

The taxpayer may offer the amount of tax payable for funding a health program by means of a statement of instruction through its tax return (offer is capped at 10% of the tax payable).

The tax is levied by self-assessment; the selling person or organization (taxpayer) is obliged to compute the tax, to prepare and file the tax return and to pay the tax according to the rules for VAT periods.

10 Telephone tax (telecommunication tax)

For service providers, a special tax liability (Act No. LVI of 2012) is applicable to phone calls and messages. The tax rate differentiates between individuals and corporations.

The tax rate is differentiated between individuals and corporations.

In case of individuals, a tax in the amount of HUF 2 (approx. EUR 0.005) per minute on phone calls and per message (SMS, MMS) is levied, while the monthly payable maximum of the telephone tax per phone number amounts to HUF 700 (approx. EUR 1.9) for individuals.

In case of corporations, a tax rate in the amount of HUF 3 (approx. EUR 0.01) per minute on phone calls and per message is levied and the monthly payable maximum of HUF 5,000 (approx. EUR 14) per phone number applies.

Although the service providers are liable to pay the tax to the tax authority, in practice the telephone tax is charged to the customers.

11 Financial transaction tax

Financial transactions are to be taxed as follows:

- 0.3% for transfers capped at HUF 6,000 (approx. EUR 16) per transaction;
- 0.6% for getting cash either directly from the account or through an ATM, and for paying with a credit card.

The above applies for Hungarian bank accounts and does not have an impact on transactions effected through a foreign bank account.

In addition, further tax rates are defined in case of specific transactions (e.g. payment transactions executed by the beneficiary with the same cash-substitute payment instrument).

Similar to the telephone tax, according to the Act, financial service providers are liable to bear and pay the transaction tax; in practice, however, the fees are re-charged to the customers.

In the case of a declaration of the account holder, the first two cash withdrawals either directly from the account or through an ATM are not subject to financial transaction tax levied by the bank if the conditions prescribed by law are met. This benefit is available solely to private persons and is capped at HUF 150,000 (approx. EUR 416) per month.

Furthermore, money transfers up to HUF 20,000 (approx. EUR 55) are exempt from financial transaction tax.

12 Advertising tax

According to the currently applicable rules, the advertising tax provisions have been suspended beginning from 1 July 2019 until 31 December 2022.

13 Digital services

N/A

14 Tourism contribution

The tourism contribution amounting to 4% has been introduced by a tax amendment act (Act No. LXVI of 2016). The tourism contribution is levied on the supply of meals, food and non-alcoholic beverages prepared on site in restaurants, which is taxable at a reduced VAT rate of 5%. In order to support the most vulnerable sectors affected by the COVID-19 pandemic, the payment of the tourism contribution is suspended for the sale of food and beverages at restaurants and commercial accommodation services acting as an agent.

II SPECIAL AREAS OF TAXATION OF BUSINESS-RELATED ACTIVITIES

A HOLDING STRUCTURES

1 Participation exemption

The Hungarian CIT Act provides for an exemption of dividends derived by resident companies on their shareholdings in domestic and foreign companies. As of 27 November 2020, the CIT Act provides this exemption even if the distributor is a CFC; however, only if it comes from a real legal transaction. The part of the income from a non-genuine transaction reduces the tax base only if the taxpayer has previously increased his pre-tax profit. The Act does not provide an exact method for determining what share of the revenue comes from a real legal transaction. It can be assumed that within the total revenue, the share of the profit from the real legal transaction is decisive for the dividends. The exemption applies regardless of the amount and the holding period of the participation. The exemption is also granted to Hungarian permanent establishments of non-resident companies (regarding the restriction on CFCs, see I.C.3).

In this regard we recommend reviewing the details of corporate taxation (I.B.3) and reorganizations (I.B.4). The special rules concerning the exemption of foreign-source income are summarized below.

2 Withholding taxation

Hungary does not levy any withholding taxes on cross-border payments to corporations (i.e. interest, royalty payments and service fees are exempt from withholding tax in Hungary). Dividends distributed to corporations are also exempt from Hungarian withholding taxes, irrespective of the residence of the recipient.

3 Interest deduction

Interest on loans and other debts is generally deductible for tax purposes, provided that the business purpose test is met and the interest income does not fall under the interest deduction limitation rules that are determined and depending in most cases on the level of the EBITDA (see I.B.3.3).

4 Taxation of capital gains

4.1 REPORTED PARTICIPATION SCHEME

In general, capital gains are taxable in Hungary under the general rules (9% CIT). Nevertheless, by using the »reported participation scheme«, capital gains realized upon the alienation of domestic and foreign shareholdings (including contributions in kind) are tax exempt, provided that the following conditions are met:

- participation held in CFCs is not subject to the scheme;
- the participation is held for at least one year;
- reorganization does not interrupt the required holding period;
- the acquisition of the shareholding is reported to the tax authorities within 75 days after the acquisition is registered by the Court of Registration (or after the contract on the acquisition takes effect, if no registration is required by the Court). Taxable persons established abroad are also entitled to report the shareholdings acquired prior to shifting their effective place of management to Hungary.

This »reported participation scheme« applies only to Hungarian residents. Although capital gains under the scheme are tax exempt, capital losses are not deductible. Therefore, the tax base must be increased if capital losses occur upon the alienation of shareholdings. Please also note that the value of goodwill needs to be adjusted to the tax base amendment items.

Tax schemes are available to get a CIT exemption for intangible assets (see III.A.4.2 and III.A.4.3).

4.2 REPORTED INTANGIBLE ASSETS

The »reported scheme« is extended to intangibles as well, including intellectual property and pecuniary rights generating royalties. The conditions of applying the tax exemption for the »reported intangible assets« are partly similar to the above mentioned, i.e. exemption may be available after the one-year holding period. However, the reporting must be done within 60 days of acquisition or creation and the tax base shall be increased if capital losses occur. The intangible asset to be reported shall qualify as a »royalty-generating intangible asset«, otherwise the preferential tax treatment is not available. Specific transitional rules apply until 30 June 2021.

4.3 ALIENATION OF ROYALTY-GENERATING INTANGIBLE ASSETS

Capital gains realized on the alienation of royalty-generating intellectual property and pecuniary rights may also be exempt from corporate income tax provided that a special reserve is created in the tied-up reserves in the amount of the capital gain (if not reported as an intangible asset). The special reserve must be used within five tax years for the acquisition of similar royalty-generating intangibles; otherwise the unpaid tax at the tax rate of the year of generating the special reserve along with respective late payment interest is due. Specific transitional rules apply until 30 June 2021.

5 Tax group

The Hungarian income tax legislation provides for the possibility of group corporate taxation of two or more entities as a single fiscal unity. For more details on the rules of group taxation in Hungary, please see regarding Income Tax aspects B.

B REAL ESTATE INVESTMENTS

The general principles of taxation of Hungarian resident or non-resident individual and corporate investors apply also for real estate investors.

1 Resident investors

Based on domestic rules, a natural person's tax residence is determined by (Hungarian or EEA) citizenship, or the individual's permanent home. If this test is not met, the decisive criterion should be the center of vital interest and subsequently the place of habitual abode. Residents are subject to Hungarian personal income tax levied on the worldwide income, including income from real estate.

A corporate investor (Kft., Rt., Bt., Kkt. or Ec.) is tax resident in Hungary under domestic law if the legal seat or place of management is situated in Hungary. Such a corporate investor is subject to Hungarian CIT on its worldwide income, including income from real estate.

1.1 REAL ESTATE INVESTMENT INCOME

Individual investors
Under the PIT Act, income from real estate may be the following:

- business income;
- income from rentals and leasing characterized as consolidated income;
- capital gains resulting from the sale of real estate. (Please note that the serial sale of building plots or real estates no older than two years may qualify the individual as a taxable person for VAT purposes if four sales are carried out within two calendar years.)

BUSINESS INCOME
If the real estate activity qualifies as business income (see I.B.1.1), the principles of taxation for private entrepreneurs apply (see I.B.1.2). Expenses (e.g. ongoing expenses and maintenance) directly related to the income are, in general, tax deductible. Capital gains from the sale of the real estate are fully taxable.

For real estate, the depreciation is calculated based on the amount of acquisition costs. The same is applicable for investments (costs incurred by the land owner for the construction of a building or major extensions and value-increasing improvements of existing buildings) in connection with real estate. According to Hungarian personal income tax law, the maximum depreciation rates for real estate are:

- 2% per year for long-life structures;
- 3% per year for medium-life structures;
- 6% per year for short-life structures; and
- 1-25% per year for special buildings.

Land (except for land used for mining, storing waste and soil amelioration) may not be depreciated. A tax-effective write down to the lower market value is required if the market value is permanently below book value.

INCOME FROM RENTALS AND LEASING

If the activity of the individual does not qualify as a business activity, the rental payment is taxed as income from independent activity and taxable as part of the consolidated tax base. The depreciation and the cost incurred in connection with the reconstruction of the building are deductible. The rental income is subject to 15% personal income tax.

A tax exemption is provided by the law for the leasing of arable land if the term of lease exceeds five years.

CAPITAL GAINS RESULTING FROM THE SALE OF REAL ESTATE

If the sale or transfer of rights in real estate leads to business income, the income from the transfer of real estate is subject to the following taxation scheme. The capital gain resulting from the sale of immovable property (including certain rights) is determined as the difference between the income realized from the sale of the real estate and the following certified expenses:

- amounts paid for the purchase of the property and other related expenses;
- costs of investments that increase the value of property; and
- any expenses in connection with the transfer of property.

Gains from the alienation of immovable property or certain property rights are taxed as follows:

- 100% of the amount in the year of purchase and the subsequent year;
- 90% in the second year after the year of purchase;
- 60% in the third year after the year of purchase;
- 30% in the fourth year after the year of purchase; and
- 0% in the fifth or subsequent years after the year of purchase.

Corporate investors

Income of a company is to be regarded as »business income« in any event, regardless of the nature of the income (e.g. income from real estate investment). The rules for business income are applicable. Rental and leasing payments as well as capital gains are subject to CIT according to the tax rate of 9%.

The principles of international taxation are basically laid down in the applicable tax treaty concluded between Hungary and the other state.

REAL ESTATE INVESTMENT FUNDS

Hungarian tax law does not provide for any special provisions regarding the income taxation of real estate investment funds. Therefore, entrepreneurs engaged in real estate investment are taxed according to the general rules. If real estate is acquired by an investment fund operating with permission of the Hungarian Financial Supervisory Authority, a moderate real estate transfer tax rate of 2% applies.

REAL ESTATE INVESTMENT TRUSTS (REIT)

Under strict conditions, REITs might be exempted from Hungarian CIT (effective tax rate is 0%) as well as local business tax; however, real estate transfer tax on the acquisition of real estate or shares in a real estate company is capped at 2%. In the case of non-compliance with the special rules and conditions the REIT is liable to pay double of the tax benefits (applicable for CIT, local business tax and real estate transfer tax as well).

1.2 TAX RATES AND TAX PAYMENTS

As regards the personal and corporate income tax rate, see I.B.1.6 (generally 15%; for private entrepreneurs 9% personal income tax rate) and I.B.3.5 (9% CIT rate).

2 Non-resident investors

Individual non-resident investors

Individual real estate investors are considered to be non-resident in Hungary in the absence of the Hungarian citizenship, permanent home, center of vital interest or place of habitual abode, and are only taxed with regard to their Hungarian-source income (see II.B.1.1):

- business income if the real estate business activity is carried on in Hungary or the Hungarian real estate belongs to a non-Hungarian business;
- income from rentals if the immovable property is located in Hungary; and
- income from the sale of real estate located in Hungary within the five-year holding period.

Non-resident individuals liable to personal income tax in Hungary due to realizing real estate income from Hungarian sources have to file an annual personal income tax return. The same domestic tax rates as mentioned under II.B.1.1 apply. A tax rate of 15% applies to income resulting from the transfer of immovable property, which, however, may be overridden by treaty provisions, if applicable.

Corporate non-resident investors
Non-resident investors are subject to limited CIT liability based on the economic activities carried out by the Hungarian permanent establishment. The use (transfer of rights), the sale and the contribution in kind of the immovable property located in Hungary by the non-resident investor creates a permanent establishment under the current interpretation of the relevant rules.

Therefore, the non-resident will qualify as a taxable person in Hungary from a CIT point of view. Income from the use of the immovable property attributed to a Hungarian permanent establishment is subject to corporate income taxation under the general rules. The CIT rate of 9% applies.

Non-resident organizations being a shareholder in a company owning real estate located in Hungary (»real estate company«) qualify as taxable persons for CIT purposes if they derive income from the withdrawal (i.e. reduction of the registered capital) or alienation (sale, free transfer or in-kind contribution) of shares in the real estate company.

An organization qualifies as a real estate company for CIT purposes if the value of the real estate located in Hungary exceeds 75% of the book value of the total assets as per consolidated financial statement (including related Hungarian companies and related foreign companies with a permanent establishment in Hungary).

Taxation may be modified by the treaty provisions.

3 Real estate taxes

3.1 REAL ESTATE TRANSFER TAX

Transfer of real estate and comparable rights
Real estate transfer tax is levied on the transfer of immovable property (land and buildings) located in Hungary, on the transfer of certain rights related to immovable property and on the transfer of shares held in a real estate company. Taxable transactions include – inter alia – the sale, contribution in kind and exchange of immovable property, as well as transfers without a legal title and transfers of beneficial ownership, and also the acquisition of real estate within the framework of a closed-end finance lease (rent to own). The tax base is the market value of the transferred real estate.

The tax rate is 4% (on the market value of the acquired property) up to a value of HUF 1 billion (approx. EUR 2.78 million), and 2% above this threshold. The tax will be capped, however, at HUF 200 million (approx. EUR 555,555) per property.

As of 2020, the transfer of real estate that has been reclassified as built-up (inland) areas, and the transfer of shares of a company with holdings in the above-mentioned real estate located in Hungary, are subject to real estate transfer tax. It should be emphasized that, contrary to common practice, it is not the acquirer of the real estate or share who is liable to pay the duty, but the competent transferor. The tax rate is especially high, at a rate of 90% of the difference between the acquisition value and the transfer value of the real estate at the time of transfer. The date of the reclassification is relevant; it should be within the 10 years prior to the transfer of the real estate, excluding any real estate which has been reclassified as an inland estate within or after the sixth year following the acquisition by the transferor, or acquired by inheritance. Tax exemption may be applicable to preferential transformations and exchanges of shares, preferential asset deals, or between related parties, as detailed below II.B.3.1. in the chapter titled Transformation.

The transfer of real estate between related parties is not subject to the transfer tax, if the main activity of the acquiring company is the rental or management of own or rented real property, or the sale and purchase of own real property.

Transfer of shares
A share deal is subject to real estate transfer tax, provided that the shares transferred are held in a real estate company.

The definition of the real estate company for transfer tax purposes is not identical with the definition stated in the CIT Act. For transfer tax purposes a company qualifies as a real estate company if the balance sheet value of the real estate located in Hungary exceeds 75% of the balance sheet value of the total assets or this company holds at least (directly or indirectly) a participation amounting to 75% in a company where 75% of the balance sheet value of the total assets are domestic real estate.

The acquisition of shares in a real estate company would trigger transfer tax payment liability, irrespective of the main business activity of the acquiring company.

The transfer tax base is the market value of the real estate owned by the company. The applicable tax rates are the same detailed above in II.B.3.1. The transfer of the shares held in a real estate company between related parties is, however, free from the transfer tax.

Transformation
Legal transformations are generally subject to transfer tax; how-ever, the regulation, especially for the exemptions are complex and diverse. The subject matter of a duty can also be different depending on whether the transfer was affected free of charge (donation) or against payment (quid pro quo acquisition). Preferential transformations and exchanges of shares, preferential asset deals are usually tax exempt, but with further restriction if the tax rate equivalent to CIT is not less than 9% (low-tax jurisdictions excluded). Moreover, the transaction shall be supported by sound business and commercial reasons, where the burden of proof lies with the taxpayer. Other special exemptions may be applicable for related parties that are considered related parties within the meaning of CIT.

Agencies and financial leasing activity

Financial leasing companies carrying out their activities under the control of the Hungarian Financial Supervisory Authority and real estate agencies are entitled to apply a reduced tax rate of 3%, provided that the real estate concerned is resold or leased within two years. The tax rate may be decreased to 2% if the reseller undertakes that the buyer/lessee acquires title of ownership to the real estate without terminating the agreement. In the case of the real estate agencies another condition for the application of the reduced transfer tax rate is that at least 50% of their net sales revenue of the last year must be derived from this activity. The reduced tax rate is not applicable in case the real estate is sold to a related party of the real estate agency or financial lease company.

3.2 PLOT TAX AND BUILDING TAX

Municipalities may levy taxes on property (plots and buildings) located in their territory. Undeveloped land plots (including forests, etc.) within the territory of the municipality are subject to the tax on land plots. The tax base can be determined either by the size or the adjusted market value of the land, depending on the decision of the respective municipality. The tax rate may be fixed by the municipality, but may not exceed HUF 366.9 per m² (approx. EUR 1.1) or 3% of the market value of the land.

Buildings situated within the territory of the municipality are generally subject to a tax on buildings, but there are some exemptions applicable. The tax base may be determined either by the size or the adjusted market value of the building, while the tax rate may not exceed HUF 2,018 per m² (approx. EUR 5.6) or 3.6% of the market value of the building.

4 VAT on real estate

Generally, the alienation of real estate is subject to VAT at a rate of 27%. However, a reduced VAT rate of 5% was introduced in 2016 for the supply of new and unused residential property. The reduced tax rate is applicable until the end of 2026 ultimately for those residential properties for which the construction license was granted until 31 December 2022.

The 5% VAT rate is applicable for new flats in the rust belt as of 22 July 2020 without any time limit. »Rust belt« (brownfield land) means any abandoned, underused, or degraded parcel of land, other than agricultural land and woodland, that has previously been used for industrial, commercial, transportation, or military purposes, and has typically been affected by environmental damage, which may be converted into increased value development land by means of environmental and technical intervention. The rust belt area is defined in a government decree.

The sale of real estate occupied for more than two years, the sale of undeveloped land (except building plots) as well as the rental and leasing of property is tax exempt. Notwithstanding this general rule, the taxpayer may opt for taxation, but will be bound to his decision until the end of the fifth calendar year.

With respect to real estate transactions, taxpayers may opt to be taxable on the sale or the lease or both. It is also possible to differentiate between residential and non-residential real estate, but either all real estate or only non-residential real estate may be treated as taxable.

5 Real estate investment funds

The real estate investor can acquire Hungarian real estate in the course of an asset deal (i.e. the direct acquisition of real estate) or share deal (i.e. the acquisition of a corporation owning real estate). In case of a share deal, further reorganization steps may be required to achieve a debt push-down.

Please note that foreigners (non-EU/non-EEA investors) may acquire real estate and land in Hungary. As of 1 May 2014, citizens of the EU Member States are entitled to acquire arable lands under strict conditions.

5.1 ASSET DEAL

Direct acquisition of real estate

A Hungarian corporation may acquire Hungarian real estate directly. As a general principle, costs and expenditures are deductible as far as they are incurred for business purposes. Interest on loans are generally deductible for tax purposes, but the interest limitation rules as described in detail in Chapter B 3.3 have to be taken into account as a threshold. The acquisition costs incurred before capitalizing the real estate are treated as being part of the purchase value. These costs are not immediately deductible, but are depreciated together with the real estate. Other costs borne by the acquiring company after the capitalization of the asset are immediately tax deductible if incurred in the interest of the business. The acquisition of real estate is subject to a real estate transfer tax as mentioned above whereby the tax base is the market value, see II.B.3.1. Moreover, the acquisition also triggers VAT and CIT consequences.

Acquisition of business units

The acquisition of business units including real estate (with the option to impose VAT) is not subject to VAT if the business unit is acquired for the purpose of further operation and if the acquirer, inter alia, opts to be taxable on the sale or the lease of the real estate which was acquired together with the business unit. As a further requirement the acquirer must be entitled to deduct VAT.

5.2 SHARE DEAL

As Hungarian tax law does not differentiate between partnerships and other types of corporations, the acquisition of a partnership interest would have identical tax consequences.

If real estate is held by a Hungarian corporation (target) and the purchaser acquires the target (e.g. via a special purpose vehicle), Hungarian law allows the merger of the Hungarian target (corporation holding the real estate) with the purchasing special purpose vehicle company, which may allow a debt push-down. Costs or expenditures connected with the acquisition of the shares in the target are immediately tax deductible, provided that the business purpose test is met.

5.3 MERGER

For the regulation and tax consequences of a merger, see I.B.4.

5.4 REIT

As mentioned under II.B.1.1, REITs may be exempt from CIT and local business tax; tax advantages are also available with respect to the real estate transfer tax upon the fulfillment of the special conditions.

6 Trusts and private foundations

The concept of trusts introduced to the Hungarian legislation was expanded in 2019 to include private foundations.

Certain favourable tax regimes are to be applied in the field of gift tax, corporate income tax, local business tax, personal income tax and social contribution in case the trust or private foundation fulfills certain criteria (see IV.4.).

Some of the beneficial regimes are listed below (the list is not exhaustive):

- there is no CIT payable in case of both the principal and the beneficiary is a natural person and the income earned by invested financial assets, receivables, securities or cash and cash equivalents;
- the assets acquired due to a trust foundation contract by a person or organization reported to the Hungarian Tax Authority as a trustee with certain exceptions shall not be subject to gift tax.

III EMPLOYEES AND BOARD MEMBERS

A EMPLOYEES

1 Resident employees

An individual is tax resident in Hungary if he has the Hungarian nationality or if he has a permanent residence in Hungary. The individual will also become a Hungarian tax resident if he is a citizen in the European Union or the European Economic Area and spends more than 183 days per calendar year in Hungary. Any home is permanent if it is permanently available for the individual's use.

If the tax residence cannot be determined based on the above criteria, the decisive criterion is the center of »vital interests« i.e. where the individual's personal and economic relations are closest. If this test is not met either, then residence is determined by the place of habitual abode i.e. where the individual spends more than 183 days.

Hungarian tax residents are subject to Hungarian personal income tax on their worldwide income (unlimited tax liability).

1.1 EMPLOYMENT RELATIONSHIPS

Based on Hungarian legislation, income earned from an employment relationship (Hungarian or foreign) qualifies as employment income. Employment income includes all wages, remuneration or honoraria received for such activities but also bonuses or cash payments (redundancy payments) in connection with the employment relationship.

1.2 PRINCIPLES FOR THE DETERMINATION OF THE TAX BASE

Employment income is deemed to be income from dependent activities. It constitutes part of the individual's consolidated tax base and is taxed at a flat tax rate of 15% (see III.A.1.3).

Ordinary and necessary employee's business expenses borne by the employer (e.g. business travel and accommodation expenses, etc) are not considered income for Hungarian personal income tax purposes.

Housing provided to a seconded employee is generally tax free if the foreign employment relation is maintained (no Hungarian employment contract is concluded) and appropriate contractual arrangements and invoices are in place.

1.3 TAX RATE, ASSESSMENT AND SOCIAL SECURITY CONTRIBUTIONS

Personal income tax
The applicable tax rate to the consolidated tax base is 15%.

In Hungary the annual salary is paid in 12 equal installments. The personal income tax has to be withheld by the employer from the gross salary of his employees and paid to the tax authorities on a monthly basis until the 12th of the month following the calendar month.

For lack of a Hungarian disburser to withhold the prepayments of personal income tax, the individual has to settle the personal income tax due on the employment income on a quarterly basis. The personal income tax advances should be transferred to the Hungarian tax authorities by the 12th of the month following the calendar quarter (i.e. 12 April, 12 July, 12 October and 12 January of the following year in which the income was received).

Personal income tax withheld by the employer/disburser is considered to be a prepayment on the employee's final income tax and is credited against his assessed income tax liability. Individuals liable to Hungarian personal income tax should file an annual income tax return whereby the deadline is 20 May of the year following the calendar year concerned. The tax authority prepares a draft personal income tax return, which can either be accepted or modified by the person in question. Any difference between the annual tax liability and the prepayments must be paid by the employee by the filing deadline. Any excess tax payments must be refunded by the tax authorities within 30 days from the date the tax return was submitted.

Employees may not request that their employers assess their annual taxable income and the personal income tax obligation.

Employees may, under certain conditions defined by the Hungarian personal income tax rules, deduct certain tax credits and allowances (i.e. family allowance, allowance for first-time married couples, allowance for certain diseases and disabilities, etc.) from their personal income tax base. Mothers raising four or more children are eligible for a full tax exemption.

Social security contributions
The employer is obliged to withhold the employee-side social security contribution from the gross salaries paid to the employees and is also liable to pay social tax and vocational training contribution in its own name on the employer side over the gross salaries.

Pensioners are not obliged to pay social security contributions on their income. Therefore, their income is subject only to PIT at the rate of 15%. As a further advantage, the employer of a pensioner does not have to pay social tax and vocational training contribution on the remuneration of the employed pensioner.

The social tax rate is 15.5%.

Currently, the level of the employee's contribution is 18.5%.

In order to ensure a higher level of utilization in connection with the family allowance, 15% of the unutilized family allowance balance exceeding the personal income tax base is enforceable in the form of families' contribution allowance by reducing the social security contribution at the rate of 18.5%. For 2021, the social tax and social security contribution rates for employed persons and the vocational training contribution rate are:

BY THE EMPLOYER	RATE	BY THE EMPLOYEE	RATE
social contribution tax (expected to be reduced to 15.50% as of 1 July 2020)	15.5%	social security contribution	18.5%
vocational training contribution	1.5%	–	–

1.4 REHABILITATION CONTRIBUTION

In 2021 the amount of the rehabilitation contribution is HUF 1,449,000 (approx. EUR 4,025) per person (below the mandatory employment ratio). Companies employing more than 25 persons are obliged to pay the rehabilitation contribution if the number of employees with disabilities does not exceed 5% of the total labor force (mandatory employment ratio). The annual amount of the rehabilitation contribution must be calculated by multiplying the number of employees under the mandatory employment ratio by HUF 1,449,000. The contribution advances must be paid in the first three quarters by the 20th of the month following the quarter. The difference between the advances paid and the annual contribution obligation must be paid for the tax year by 25 February of the following year.

1.5. NON-CASH BENEFITS

From January 2019, the cafeteria system in Hungary was simplified, since the scope of in-kind benefits was narrowed down significantly.

The non-cash benefits are taxed as follows:

- **Fringe benefits with advantageous employer-side taxation**
  Only the payments to the so-called SZÉP card may be provided as fringe benefits subject to preferential taxation of 15% PIT plus 15.5% social tax and 1.50% vocational training contribution, resulting in the overall tax rate of 32%.

  The aggregate annual amount of cafeteria subject to the preferential employer's tax rate of 32% is HUF 200,000 (approx. EUR 555) for public employees and HUF 450,000 (approx. EUR 1,250) for people employed in the private sector.

  The three sub-accounts for SZÉP card benefits remain unchanged: annual HUF 225,000 (approx. EUR 625) for accommodation, HUF 150,000 (approx. EUR 417) for hospitality (catering) and HUF 75,000 (approx. EUR 208) for leisure activities.

  To mitigate the economic effects of the COVID-19 pandemic, preferential rules have been introduced on a temporary basis until 30 June 2021, where the yearly recreational amounts have been increased to HUF 800,000 for private sector workers and to HUF 400,000 for public employees.

  A further change is that only 15% PIT is payable after the benefit granted by the employer. The benefit granted in excess of the abovementioned recreational amount will continue to be taxable as »certain specified benefits«. In this latter case, the tax base is 1.18 times the fair market value of the provided benefit on which 15% PIT, 15.50% social tax and 1.50% vocational training contribution are payable.

  Fringe benefits exceeding the abovementioned caps will qualify as »certain specified benefits« and will still be taxable by the employer at a higher rate (see below).

- **»Certain specified benefits« payable by the employer**
  Further non-cash benefits are subject to 15% PIT, 15.5% social tax and 1.50% vocational training contribution over a super-grossed amount (multiplier: 1.18; effective tax rate altogether: 37.76%) next to the benefits provided in the preferential category (see above), for instance the following are applicable: representation expenses and business gifts, entitlement to private use of company mobile phones, gifts of negligible value (up to 10% of the minimum wage, once a year), certain taxable insurance premiums paid by the employer. Benefits granted to all employees under the same circumstances or on the basis of a company policy are taxable as wages. The payment of the vocational training contribution is suspended until the end of the state of emergency.

- **Generally taxable non-cash benefits**
  Those non-cash items which are not subject to the above two categories will be taxable as part of the consolidated tax base (15% PIT, 18.5% social security contribution, 17.5% employer's social tax plus 1.50% vocational training contribution).

- **Tax-exempt benefits**
  The scope of tax-exempt benefits has been narrowed radically from the beginning of 2019. Benefits that were tax exempt until 2018 (e.g. risk insurance paid by the employer, housing assistance for labor mobility purposes, employment support for the repayment of student loans) are now taxable as wages. The reimbursement of nursery and kindergarten costs remains tax exempt in 2021. Tickets for cultural and sport events are tax exempt up to the amount of the minimum wage.

1.6 DAILY ALLOWANCES

A daily allowance paid by the employer in the case of domestic business trips is fully taxable in the hands of the employee (i.e. part of the consolidated tax base). There is an exemption applicable for truck and bus drivers.

Daily allowances paid for foreign business trips are exempted from taxation up to 30%, but maximum EUR 15/day.

Daily allowances provided to truck drivers are tax exempt up to the amount of EUR 60/day.

2 Non-resident employees

Non-resident individuals (the criteria for tax residence are provided in detail under III.A.1) are subject to Hungarian personal income tax on their Hungarian source income, i.e. income received from activities performed in Hungary (limited tax liability).

The rules regarding the determination of the tax base, tax rate, assessment, social security contributions and social tax are similar to the treatment of resident employees (see III.A.1).

B BOARD MEMBERS

1 Executives

The income of company executives (managing directors, board members, etc) is taxed as employment income, income from dependent activity (for details, see III.A.1).

If the executive also performs other services (e.g. advisory services) based on an agency agreement, the income derived from this activity will qualify as income from independent activity and is taxable as part of the consolidated tax base (see III.A.1.3 and III.A.1.4). However, either a lump sum of 10% of the income or the actual expenses incurred may be deducted from the tax base.

A minimum contribution liability is applicable for domestic and foreign individuals registered as owners of a company and simultaneously carrying out managing director's activity without direct remuneration under an agency agreement (thus, not in the frame of an employment). These rules do not cover individuals whose social security liability is based on another legal relationship (e.g. any other work-related legal relationship of the participating member) with the company.

2 Non-executives

The income of elected representatives of a company who do not qualify as executives, for example the Members of the Supervisory Board, is considered to be income from dependent activities and is taxable as part of the consolidated tax base (see III.A.1.3 and III.A.1.4).

3 Non-resident board members

Non-resident executives are taxed only on income derived in Hungary (limited tax liability – source income taxation), irrespective of the type of the relationship (employment relationship or service contract). This income is taxed in the same way as the income of resident executives, i.e. as income from dependent activity (see III.B.1).

The minimum contribution liability is due for non-resident executives as well. Exemption from the minimum contribution might be reached by foreign managing director owners under the EU Regulation on the coordination of social security systems (EC Regulation No. 883/2004).

C MUNICIPAL TAX

N/A

D SPECIFIC PROVISIONS FOR CROSS-BORDER EMPLOYMENTS

1 General provisions

1.1 TAX TREATY LAW

If an individual is tax resident in Hungary and is also deemed to be resident in another country based on its domestic law, tax residence should be determined in line with the provisions of the relevant treaty. The taxation of the income earned will further depend on the relevant provision of the respective treaty.

As most of the Hungarian treaties are concluded in accordance with the OECD Model Convention (OECD MC), Art. 15 OECD MC is the applicable provision in the case of cross-border employment. Under Art. 15 OECD MC, the taxation right for employment income is attributed to the country where the employment is performed (state of exercise). The individual's income – with respect to the Hungarian employment – is only exempt from Hungarian taxation, if:

- the individual is a resident of a country other than Hungary with which Hungary has concluded a treaty; and
- the individual is present in Hungary for a period not exceeding 183 days in the calendar year/tax year/12-month period concerned; and
- the remuneration is neither paid by, or on behalf of a Hungarian employer, nor by a permanent establishment in Hungary.

Otherwise, the individual's income paid for the Hungarian activities is taxable in Hungary.

If a Hungarian tax resident performs dependent activities abroad and the income is taxed in the country of exercise in accordance with Art. 15 OECD MC, this income is exempt from taxation in Hungary.

With respect to cross-border employment of members of supervisory boards or boards of directors, the provisions of Art. 16 OECD MC may be applicable. According to Art. 16 OECD MC, the fees of the supervisory board members and the directors are taxable in the state of residence of the company.

1.2 SOCIAL SECURITY LAW

Exemptions from the Hungarian social security obligation depend on the individual's citizenship (EU citizens, third-country citizens) and on the conditions of the employment/assignment.

Foreign nationals coming to Hungary to perform their dependent activities are basically subject to the same social security system applicable for domestic employees. In general, if the foreign individual is employed by the Hungarian company (also in the case of a dual employment), all social charges are due, as in the case of employees with the Hungarian nationality.

Moreover, foreign individuals are in most cases also insured in their home country for social security purposes. With the aim of preventing double payment or double non-payment of social security contributions, EU coordination rules and bilateral social security agreements (Hungary has concluded 15 social security agreements with non-EU countries) are applicable.

In the case of EU citizens, EU coordination rules (EC Regulation No. 883/2004) determine which country is entitled to charge social security contributions. Based on the general rule of the EU Regulation, the individual should pay social security contributions in the country where the work is carried out. However, if an individual wishes to remain in the home country's social security system, certain conditions must be met and a certificate of coverage (»A1 certificate«) must be obtained, based on which Hungarian social security charges may be avoided.

2 Specific provisions

Besides the general rules described under III.A, there are no special provisions or tax exemptions applicable to non-residents working in the territory of Hungary or to Hungarian residents working abroad. Non-resident art performers (e.g. musicians, actors, film crew) are obliged to pay 15.5% social tax. The social tax liability is capped; the tax base shall be calculated based on the minimum wage multiplied by 24 (HUF 3,864,000, approx. EUR 10,773). Accordingly, applying the tax rate of 15.5%, the social tax liability is capped at HUF 598,920 (approx. EUR 1,664) in 2021 per annum.

If the conditions set out in the PIT Act are met (presence in Hungary does not exceed 183 days in any 12-month period, no social security residence in Hungary), non-resident art performers can determine their personal income tax base according to the simplified taxation method.

Regarding movies shot in Hungary, the temporary status is not harmed either, when the complete production (including the preproduction) of this kind of piece of art exceeds 183 days.

Further registered non-resident persons who are not art performers (generally not only the cast but crew members also) may choose the simplified method for determining the personal income tax base.

By determining the PIT base, it is not obligatory to take into account as income the reimbursement of travelling and accommodation costs, or the in-kind refund/compensation of these costs. There is no way to decrease the PIT base with a lump-sum cost deduction.

The calculated personal income tax shall be declared and paid before the foreign art performer leaves Hungary. If the revenue derived from Hungary does not exceed the amount of HUF 200,000 (approx. EUR 555) in any 12-month period, no income shall be determined, i.e. no tax obligation shall arise.

IV TAX ASPECTS FOR PRIVATE INVESTORS

A CAPITAL INVESTMENTS

1 Resident capital investors

Residents are subject to Hungarian personal income tax on their worldwide income regardless of whether or not the funds are transferred to Hungary (for the residence test, see III.A.1).

1.1 INVESTMENT INCOME

Investment income includes interest income, income from securities lending, income from swap transactions, dividend income, capital gains, capital gains from controlled capital market transactions, income derived from long-term investments and royalty income.

Interest income
Based on domestic rules, for example, the following qualifies as interest income: interest on savings deposits, savings notes and foreign exchange deposits, the yield from debt securities publicly offered and traded but only if designated as interest by law, the yield from publicly offered investment certificates, the part of the insurance payment that exceeds the insurance fees paid by the private individual (except risk insurance), etc.

Any income with the nature of interest that is not included in the exhaustive list of the Hungarian PIT Act (especially income arising from privately issued and traded bonds) is classified as other taxable income.

Dividend income
The following income of private individuals is considered to be dividends: a private individual member's (shareholder, founder) or owner's share from the taxed profit of a business association, including interest on interest-bearing shares from the taxed profit; income defined as dividends by the laws of other countries; yield from venture capital funds and prepayment of dividend with respect to the expected dividend of the tax year.

Capital gains from shares
Under the Hungarian legal system, shares are generally deemed to be »securities« according to the Hungarian Civil Code. For tax purposes the Hungarian PIT Act differentiates between capital gains derived from listed and non-listed shares.

Capital gains derived from non-listed shares means the proceeds received upon the transfer of securities (not including lending arrangements) in the over-the-counter market or on the stock exchange of a third country less the purchase price of the securities and any incidental associated costs.

In the case of shares in a foreign non-listed entity, it has to be examined whether the shares are characterized as securities according to the provisions of the respective country. If according to these rules the shares cannot be considered securities, any capital gains derived therefrom are regarded as other taxable income.

As regards capital gains from stock exchange transactions of listed shares, the provisions of capital gains from controlled capital market transactions are applicable, see below.

The PIT Act does not provide for special regulations concerning »speculative transactions« at the level of an individual. Consequently, there are no preferential rules for the non-speculative holding of shares in Hungary.

Capital gains from controlled capital market transactions
Controlled capital market transactions include not only stock exchange transactions but also various financial investment services. Controlled capital market transactions refer to the sale or purchase of certain financial instruments (except securities issued in private placement), goods and foreign currencies.

The transactions are supervised by the Hungarian Financial Supervisory Authority. The provisions on such transactions may also be applied if an agreement on such transactions is concluded with, or with the collaboration of, an investment service provider or a financial institution operating in a market of another EEA/EU Member State or in a state with which Hungary has concluded a treaty.

Capital gains from the transfer of financial instruments, goods or currencies in capital markets other than the EU and a treaty state – i.e. in third countries – are taxed as other income.

Income from controlled capital market transactions is also characterized as income derived from long-term investments (see below).

Income derived from long-term investments
A tax advantage has been introduced for long-term investment contracts over HUF 25,000 (approx. EUR 69.44) concluded with credit institutions or investment service providers. The investments can be held in HUF or in foreign currency. Only one long-term investment contract can be concluded with the same credit institution or investment service provider in the course of one year; in other aspects, however, the number of the investment contracts is unlimited.

According to the legislation, full tax exemption is given to investments held over five years and favorable taxation (10%) for investments held for three years. If the investment contract is interrupted before the end of the commitment period (i.e. at least three years), 15% of PIT would be applicable on the investment.

Income upon termination of the company or reduction of the registered capital
The PIT Act provides for special rules with regard to investment income if the membership or the business association (Kft., Rt., Bt. or Kkt.) is terminated without a legal successor, or if the registered capital is reduced by way of a withdrawal of the registered capital. For personal income tax purposes these provisions are also applicable if a foreign company – subject to a similar corporate income tax – is involved.

During the course of the termination of the business association without a legal successor the assets (valued at their market value) received by the individual shareholder are deemed to be income. For calculating the tax base, the acquisition costs of the shares and the amount of the business association's liabilities (as a percentage of the individual's shareholdings) must be deducted from the assets of the company distributed among its members. In the case of a reduction of the registered capital by withdrawal, the same tax provisions apply.

Taxation of investment income from low tax-rate states
Capital gains, dividends and interest from shares distributed by a legal person or other organization registered in a low tax rate country (the CIT rate is 9% maximum, and there is no tax treaty) are regarded as other taxable income according to the Act on PIT. Other taxable income is included in the consolidated tax base (together with income derived from dependent and independent activities).

Dividend income from controlled foreign corporations (»CFC«)
Income of an individual taxable in Hungary (including dividend income and deemed income relating to non-distributed profit) derived from CFCs must be regarded as other income and will be subject to the general flat tax rate of 15% as part of the consolidated tax base.

As of 1 January 2017, the definition of CFC in the PIT Act was abolished and replaced by »a foreign company with a seat in a low tax rate state«.

1.2 PRINCIPLES OF DETERMINATION OF THE TAX BASE

In general, investment income is calculated as the excess of taxable earnings over deductible expenses. However, the tax base of each type of investment income is determined differently in the PIT Act.

Tax rates and tax payments
»Investment income« – both from domestic and from foreign sources – is generally subject to withholding tax. The rate of withholding tax on investment income (e.g. interest income, dividends, capital gains, etc.) equals with the general PIT rate of 15%.

Certain investment income such as dividends, capital gains from shares, income from lending securities and income from the termination of a company or the reduction of registered capital is subject to 15.5% social tax with a yearly cap of HUF 598,920 in 2021 (approx. EUR 1,660). Dividends and prepayments of dividends derived from securities listed on recognized stock markets of any EEA/EU Member State are not subject to the social tax of 15.5%.

However, other taxable income as part of the consolidated tax base is subject to a higher contribution of 15.5% (e.g. investment income from low tax rate countries, dividend income derived from CFCs).

Credit of foreign tax
If the investment income derived by resident individuals from foreign companies has already been taxed abroad, the foreign taxes may be credited in Hungary. However, in the absence of an international treaty, the payable Hungarian tax on the investment income would under no circumstances be less than the 5% of the investment income. Foreign taxes that are paid by the individuals but are later reimbursed cannot be credited.

2 Non-resident capital investors

An individual capital investor is non-resident in Hungary if he cannot be characterized as resident based on the residence test (see III.A.1).

2.1 LIMITED TAX LIABILITY

An individual non-resident capital investor is taxed in Hungary only on investment income resulting from domestic assets such as

- income from dividends on domestic shares, equity participations of any kind or participation in a commercial business as silent partner and distributions made by private foundations;
- interest on loans if the loan was secured by real estate situated in Hungary; and
- income from the alienation of substantial participations in a resident corporation.

2.2 WITHHOLDING TAX OBLIGATIONS

Non-resident individuals with Hungarian-source investment income have to file tax returns, unless their income is subject to Hungarian withholding tax by the Hungarian disburser at the same flat tax rates as applied to the investment income of resident individuals (described under IV.A.1 – if tax treaty is not applicable).

The non-resident individual may opt for a regular assessment procedure by filing a tax return if the assessed tax would be lower than the tax withheld.

2.3 TAX TREATY PROTECTION FROM HUNGARIAN WITHHOLDING TAX

Tax treaties usually provide for reduced withholding tax rates for investment income of individuals. Thus, if the relevant Hungarian withholding tax rate exceeds the source tax rate provided by a tax treaty, the latter is normally applicable.

However, the reduced treaty tax rate may only be applied (directly) at source if the non-resident recipient of the income submits a certificate of residence to the paying company on the respective Hungarian tax form. Otherwise, tax has to be withheld as provided for by the Hungarian domestic tax law and the part of the withholding tax exceeding the treaty tax rate may be reclaimed in the course of a refund procedure.

3 Investment funds

The investment management industry in Hungary is regulated by the Act on the Investment Management and Collective Investment Forms and supervised by the Hungarian National Bank (HNB) Section of Supervision of the Financial System. An investment fund is a form of collective investment that pools money from many investors investing their money in stocks, bonds, short-term money market instruments, real estate and/or other securities.

The Act on the Investment Management and Collective Investment Forms concerns Directive 2009/65/EC. It contains a definition of the term »investment fund« and general procedural provisions. Under these rules, an investment fund in Hungary may be established only in the form of a Hungarian joint stock company (private: Zrt., open: Nyrt.) or a Hungarian branch of a foreign entity. Therefore, investors own shares in such a company. The establishment of an investment fund is subject to registration and the trading activity regarding investment fund certificates must be authorized by the HNB.

3.1 TAX RATES AND TAX PAYMENTS ON INCOME FROM DOMESTIC INVESTMENT FUNDS

The PIT Act does not differentiate between the income arising from a bond or from an investment fund. From a personal income tax point of view, income derived from an investment fund is treated as interest income. This interest income will be taxed at the rate of 15% if the investment fund certificate was issued publicly. If the investment fund certificate was issued privately, the income derived will be treated as other income (and taxed also at the rate of 15%).

Income from stock exchange transactions of domestic investment fund certificates is subject to personal income tax at the flat rate of 15%. Dividend income resulting from domestic investment fund certificates is also subject to the 15% withholding tax.

3.2 TAX RATES AND TAX PAYMENTS ON INCOME FROM FOREIGN INVESTMENT FUNDS

If the foreign investment fund intends to offer and trade its investment fund certificates publicly in Hungary, authorization by the HNB is required. In this case the foreign investment fund certificate will be treated as a domestic investment fund certificate from a personal income tax point of view. Consequently, the income derived from such a security will be treated as interest income.

Income from an investment fund certificate of foreign investment funds that are not registered (hence not actively distributed) in Hungary is classified as other income and taxed at the flat rate 15%.

B INHERITANCE AND DONATION TAX PLANNING

1 General

According to the Act on Duties, inheritances and gifts are subject to »property acquisition duty«. The inheritance and gift tax is levied on transfers of property in the course of an inheritance or inter vivos if either the testator/donor and/or the beneficiary are resident in Hungary at the time of the transfer. If neither the testator/donor nor the beneficiary is resident in Hungary, inheritance or gift tax is levied only on the transfer of particular types of Hungarian property (e.g. Hungarian real estate).

The inheritance and gift tax is levied at 18% flat rate (in the case of housing estates at 9%) depending on the type of the property transferred. However, there are some special rules regarding tax exemptions.

2 Inheritance tax

The Act on Duties provides for the following inheritance tax exemptions:

¬ bequests for scientific, artistic, educational, cultural; and public welfare purposes;
¬ wealth acquired under home savings contracts according to the Act on Home Savings and Loan Associations;
¬ the part of the inheritance having a value up to HUF 20 million (approx. EUR 555,555) per step and foster child and step and foster parent;
¬ movable property with a market value of less than HUF 300,000 (approx. EUR 833) per heir;
¬ inheritances between parents and their children (including adoption) and the inheritance of surviving spouse, siblings (as of 8 July 2020);
¬ inheritance of debt securities issued by any EEA Member State;
¬ inheritance of ownership or share ownership of a piece of land suitable for constructing a residential property if the beneficiary builds a residential property within four years from the date of the inheritance;
¬ inheritance of property that was previously part of a public collection maintained by the state or local government.

As regards inheritance double taxation, Hungary has concluded three tax treaties (with Austria, Romania and Sweden) that cover inheritance tax (but not gift tax).

3 Gift tax

According to the Act on Duties, the taxpayer of the gift tax is the donee only. The transfer of real estate, movable property (which also includes liquid assets) without consideration and the gratuitous creation of a right of pecuniary value is subject to gift tax. A gift will be subject to gift taxation if it is duly documented and the transfer takes place in Hungary.

The donation of movable property with a market value exceeding HUF 150,000 (approx. EUR 416) is subject to gift tax regardless whether the donation was documented or not. Furthermore, if the donation of movable property is duly documented the gift tax obligation arises regardless of the market value.

Donations between parents and their children and between spouses and also siblings (as of 8 July 2020), wealth acquired from the termination of marital community of property, release of claims for dividends and release of claims in bankruptcy and liquidation proceedings (if the claim holder is not a member of the business organization under bankruptcy or liquidation proceedings) are also exempt from gift tax obligations. Further, the acquisition of arable land as a gift and the acquisition of land use rights and any financial gain obtained through the termination of such rights are exempted as well if further conditions are met.

The acquisition and assignment of claims without consideration, and the assumption of debts without consideration are only subject to gift tax if the donee is a domestic private person as defined by the PIT Act, or if the donee is a business entity and the subject of the donation falls under the scope of the duty on the acquisition of property for consideration.

As from March 2019, a new legal form (so-called »trust fund«) was introduced in the Hungarian legislation, which is the special combination of foundations and trusts. The amendment of the Act on Duties effective from 1 January 2020 ensures that these institutions share the treatment of trusts, i.e. the same exemptions from duties apply to them.

4 Foundations

According to Hungarian law, a foundation is a legal entity having its own property and assets, which have been provided to it by the founder. The founder may not dispose of the property or assets of the foundation. A foundation may only be established for continuous charitable/non-profit objectives and not primarily for business purposes. A Hungarian foundation may be established both by Hungarian or foreign individuals and legal entities.

Under the Hungarian provisions, a non-profit organization may not distribute any profits to its founders. It may conduct its business activities solely in the interest of, and without jeopardizing, its public welfare objectives. Any business profits it may make must be used for its social objectives.

4.1 TAXATION OF INCOME DERIVED FROM FOUNDATIONS

Beneficiaries are taxable on distributions made by a foundation. If the profits and assets are retained at the level of the foundation, no tax liability arises. Due to this fact, assets or income should only be distributed if the funds are actually required by the beneficiaries.

In 2019, the Hungarian Personal Income Tax Act introduced the concept of private foundations. A trust fund, as opposed to a public-benefit organization, qualifies as a private foundation as well, provided that it is funded exclusively by a private individual founder and whose funds consist solely of the donation provided by a private individual and the income earned on such funds.

As from 2020, the distribution that is paid from the earnings on the assets of the private foundation other than a public-benefit organization is taxable as dividend income at the rate of 15% personal income tax. If the distribution is paid as a compensation for, or in connection with, some activity, transfer of an asset or a service, the income shall be qualified and taxed according to the given activity. If the activity cannot be qualified, the income shall be considered other income.

If the distribution is paid from the assets of the foundation (not from the earnings on such assets), the income realized by the private individual is tax exempt.

If a foreign foundation makes distributions, the income would be treated either as income derived from dependent personal activities or from independent personal activities. Consequently, it would be taxed in Hungary as part of the consolidated tax base (the tax rate is 15% plus 18.5% social security contribution and 15.5% social tax).

5 Tax exemptions

Certain types of allowances granted by a foundation to individuals are exempt from personal income tax liability if certain conditions are met. These exemptions include:

- amounts paid by a Hungarian public benefit foundation for studies pursued in educational institutions, research, foreign study trips (as scholarships), as well as amounts paid as social aid to indigent persons, and amounts less than HUF 500 (approx. EUR 1.38) paid occasionally to the participants in students' or other leisure sports; and
- revenues acquired in kind (except fringe benefits) or revenues acquired in cash in a maximum amount of 50% of the minimum wages by an individual from a non-profit company, foundation or public foundation under certain conditions.

However, regarding the above allowances each given case must be examined as to whether a gift tax payment obligation arises.

LeitnerLeitner Consulting d.o.o.
SRB 11000 BEOGRAD, Knez Mihailova Street 1-3
t +381 11 655 51 05 f +381 11 655 51 06
e beograd.office@leitnerleitner.com

LeitnerLeitner Tax s.r.o.
SK 811 03 BRATISLAVA, UNIQ. Staromestská 3
t +421 2 591 018-00 f +421 2 591 018-50
e bratislava.office@leitnerleitner.sk

Leitner + Leitner Tax Kft
H 1027 BUDAPEST, Kapás utca 6-12
t +36 1 279 29-30 f +36 1 209 48-74
e budapest.office@leitnerleitner.com

LeitnerLeitner GmbH
Wirtschaftsprüfer und Steuerberater
A 8041 GRAZ, Liebenauer Tangente 6
t +43 316 426 100 f +43 316 426100-763
e graz.office@leitnerleitner.com

LeitnerLeitner Tirol GmbH
Wirtschaftsprüfer und Steuerberater
A 6020 INNSBRUCK, Sillgasse 12/2.Stock
t +43 512 55 77 55 f +43 512 55 77 55-806
e innsbruck.office@leitnerleitner.com

Leitner + Leitner Tax Kft
H 6000 KECSKEMÉT, Munkácsy Mihály u. 19
t +36 76 884 021
e kecskemet.office@leitnerleitner.com

LeitnerLeitner GmbH
Wirtschaftsprüfer und Steuerberater
A 4040 LINZ, Ottensheimer Straße 32
t +43 732 70 93-0 f +43 732 70 93-156
e linz.office@leitnerleitner.com

LeitnerLeitner d.o.o.
SI 1000 LJUBLJANA, Dunajska cesta 159
t +386 1 563 67-50 f +386 1 563 67-89
e ljubljana.office@leitnerleitner.com

LeitnerLeitner Tax s.r.o.
CZ 180 00 PRAHA 8, Voctářova 2449/5
t +420 228 883 921
e praha.office@leitnerleitner.com

LeitnerLeitner GmbH
Wirtschaftsprüfer und Steuerberater
A 4910 RIED/INNKREIS, Bahnhofstraße 14
t +43 7752 858 88 f +43 7752 858 88-807
e ried.office@leitnerleitner.com

LeitnerLeitner Salzburg GmbH
Wirtschaftsprüfer und Steuerberater
A 5020 SALZBURG, Hellbrunner Straße 7
t +43 662 847 093-0 f +43 662 847 093-825
e salzburg.office@leitnerleitner.com

Leitner + Leitner Revizija d.o.o.
BIH 71 000 SARAJEVO, ul. Hiseta 15
t +387 33 201-628 f +387 33 465-793
e sarajevo.office@leitnerleitner.com

LeitnerLeitner GmbH
Wirtschaftsprüfer und Steuerberater
A 1030 WIEN, Am Heumarkt 7
t +43 1 718 98 90 f +43 1 718 98 90-804
e wien.office@leitnerleitner.com

LeitnerLeitner Consulting d.o.o.
HR 10 000 ZAGREB, Heinzelova ulica 70
t +385 1 60 64-400 f +385 1 60 64-411
e zagreb.office@leitnerleitner.com

LeitnerLeitner Zürich AG
CH 8032 ZÜRICH, Zeltweg 7
t +41 44 226 36 10 f +41 44 226 36 19
e zuerich.office@leitnerleitner.com

cooperations and memberships

Tascheva & Partner
BG 1303 SOFIA, 4, Marko Balabanov Str.
t +359 2 939 89 60 f +359 2 981 75 93
e office@taschevapartner.com

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www.leitnerleitner.com

leitnerleitner
tax audit advisory