# TAXATION IN HUNGARY

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# HIGHLIGHTS

Flat 9% corporate income tax rate

Shareholdings enjoy participation exemption on dividends and capital gains

Royalty regime leads to a 4.5% effective tax rate

No withholding tax is levied on dividends, royalties and interest paid to companies

Over 90 double tax treaties, some of them with particularly favourable terms

# CORPORATE INCOME TAX

## General overview

CIT rate is flat 9%.

Taxable persons are resident companies (unlimited tax liability) and permanent establishments (limited tax liability); resident companies include companies incorporated in Hungary and those having their place of effective management in Hungary.

Group taxation is available.

Taxable basis is derived from the accounted profit, modified by various additions and deductions, as required by the CIT Act.

Tax losses may be carried forward for 5 years and used up to 50% of the positive taxable basis of the given tax year.

Rules concerning controlled foreign companies, intellectual property tax benefits, exit tax and interest limitation transpose the Anti-Tax Avoidance Directives of the EU (ATAD).

Being an EU and an OECD member state, Hungary's tax system is harmonized with EU law and OECD recommendations

## Participation exemption

Dividend and liquidation proceeds are tax exempt – no holding period or minimum shareholding is required.

Capital gain on disposition of shares is exempt (except if realized on CFCs), subject to a 1-year holding period – no minimum shareholding is required.

## Controlled foreign companies (CFC)

Hungary follows the "non-genuine" approach of the EU Anti-Tax Avoidance Directive (ATAD).

Definition of CFC: (i) over 50% direct or indirect control; and (ii) the effective tax paid by the foreign company does not reach 50% of the hypothetical Hungarian CIT calculated on the foreign company's profits.

Numerous safe harbours allow exceptions from CFC-status.

Consequences of CFC qualification: (i) attribution of certain passive income of the CFC to the Hungarian company's taxable basis and (ii) participation exemption is not available for shareholdings in CFCs.

# CORPORATE INCOME TAX

## Royalty regime

Qualifying intellectual properties (IP): software, patent, utility model, plant variety right and topographies of semiconductor products.

Qualifying IP income: (i) royalty from licensing the IP; (ii) income from the sale of the IP; and (iii) income from the supply of products and services directly related to an IP asset (embedded IP).

Tax benefits: 50% of the profit from qualifying IP income is deductible from the CIT base and no local business tax is payable (resulting in an effective tax rate of 4.5%).

Sale of a qualifying IP is fully exempt from CIT and local business tax, subject to a 1-year holding period and the registration of the IP with the tax authority.

The OECD “nexus rules” apply (IP tax benefits may be enjoyed to the extent the IP is developed in Hungary).

# CORPORATE INCOME TAX

## Exit tax

Taxable events include outbound transfer of a taxpayer’s (i) place of effective management to another country; (ii) assets held by a Hungarian head office/PE to its foreign head PE or head office; (iii) business carried on through its Hungarian PE to another country.

Consequence: value step-up obligation and inclusion of unrealized gains in the taxable basis.

Possibility to defer the exit tax for five years (in case the transfer is to an EU/EEA member state or to a state with mutual assistance).

## Interest deduction limitation (thin capitalization)

Unused interest deduction capacity of previous tax years may also be used in the given tax year in addition to the deduction allowed for that year by the general rules.

Interest expenses may be deducted up to the higher of (i) 30% of the EBITDA and (ii) EUR 3 million / year.

# CORPORATE INCOME TAX

## Transfer pricing

OECD Transfer Pricing Guidelines are accepted and followed.

Definition of related companies: (i) more than 50% direct or indirect control between the companies; (ii) companies under common control; or (iii) companies having identical management.

Documentation requirement exists, except for small enterprises and for transactions below HUF 50 M [EUR 150.000].

Master/local file concept is adopted.

Advance pricing arrangements may be obtained.

## Development tax incentive

The CIT can be decreased (in the form of tax credits) by the eligible cost of new investment projects meeting certain conditions.

Amount of tax credit depends on the value and the location of the investment, industry sector, SME status, increase in headcount.

Tax credit is available for 12 years following the commencement of the operation of the investment.

Annual use of the tax credit is limited to 80% of the calculated CIT for the year of the use.

## Tax incentive for film production / sport activity support

Supporting film production financing and sport associations leads to various tax benefits.

Benefit is granted through a complex system of tax allowances and tax credits.

A net saving from 2.25% to 6% can be achieved as a result.

# CORPORATE INCOME TAX

## Group taxation

Eligibility for inclusion in the tax group: (i) more than 75% direct or indirect control between the companies; (ii) companies under common 75% control.

Grouping is possible for Hungarian companies only.

Tax benefits: group consolidation of current losses and losses carried forward (after the group is formed); transfer pricing rules are not applicable.

## Accounting

Companies can choose between Hungarian GAAP and IFRS for accounting.

Election of accounting currency (HUF, EUR, USD, etc.) is possible subject to certain conditions.

Financial year matches calendar year, but diversion is allowed.

# WITHHOLDING TAXES

No withholding tax is levied on outbound dividends, interests, royalties and service fees paid to foreign entities (based on domestic tax law).

Exception: capital gain realized on real property asset and share deals may be taxable – subject to the applicable double tax treaty.

# LOCAL BUSINESS TAX

Levied subject to the decision of local municipalities.

Taxable basis: gross income from sale of goods and services, reduced by certain deductible expenses (R&D expenses, material cost, COGS, expenses of services “resold” in an unchanged form).

Income from financial assets (dividends, interest, capital gains) and qualifying IP is not taxable.

Tax rate: up to 2%, depending on the municipality’s decision. Most municipalities (including Budapest) levies LBT at the rate of 2%.

# SPECIAL SURTAXES

Financial institutions, advertising activity, telecommunication services and energy companies are subject to special surtaxes.

Surtaxes may represent significant tax burden as the tax liability can exceed the CIT liability.

## Taxable basis

Energy companies: adjusted pre-tax profits.

Financial enterprises: balance sheet total (for credit institutions), income from interest and other fees (for other financial enterprises).

Telecommunication services: number of the service provider’s customer subscriptions.

Advertising activity: net sales revenue resulting from advertising.

# WAGE TAXES

Employer's liabilities (payable over the salary): 17.5% social security tax and 1.5% training fund contribution.

Employee's liabilities (deducted from the salary): 15% personal income tax and total 18.5% social security contribution (including 7% health care contribution, 10% pension fund contribution and 1.5% employment contribution).

Tax basis of all wage taxes the gross salary.

Net salary of employee compared to the total wage costs: 56%.

Various tax allowances may reduce effective tax burden (e.g., family allowance, allowances for voluntary mutual health and pension fund contributions).

Dividends and capital gains paid on shares granted through employee participation schemes may enjoy a flat 15% personal income taxation.

No family taxation is available.

# VALUE ADDED TAX

Part of the EU VAT system.

General VAT rate is 27%.

Reduced VAT rates are: 5% (e.g., books, certain food products, medicines, internet service, catering, green energy heating service) and 18% (e.g., dairy products, cereals).

VAT grouping is possible.

Domestic reverse charge mechanism applies to supplies of certain goods and services in industries more vulnerable to VAT frauds (e.g., construction, cereal and sugar industry).

Transfer of businesses as going concerns is possible in a VAT neutral way.

# TRANSFER TAX

Person liable to pay the tax: the acquiror.

Taxable base: the fair market value of the real property assets acquired.

Tax rate: 4% up to HUF 1 Billion [EUR 3 Million] and 2% on the excess value; the total tax being capped at HUF 200 million [EUR 600.000] per property.

## Taxable transactions

Direct acquisition of legal title or other rights over a real property.

Acquisition of a more than 75% direct or indirect shareholding in a “real property holding company” (company holding properties more than 75% of its total assets).

## Special features of TAX
# ADMINISTRATION

Binding rulings can be requested from the Ministry of Finance (subject to the payment of a HUF 5 Million [EUR 15,000] procedural fee).

Non-binding guidance can also be requested from the Ministry of Finance or the Tax Authority – no formal rules apply to the issuance and effect of such guidance.

Advance Pricing Agreements are available in transfer pricing matters.

Individual invoice containing VAT over HUF 100,000 (EUR 300] need to be reported immediately to the tax authority without human intervention.

Online real-time road transportation control system (EKAER) is in place to monitor the traffic of goods.v

Cash registers need to be connected to the tax authority so that all sales data is automatically reported in real time.

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