

Guideline

A short summary on the taxation of business associations

Corporate and dividend tax

The profit of companies is subject to corporate tax.

1. Taxable person of corporate tax

Pursuant to Act LXXXI of 1996 on Corporate Tax and Dividend Tax [hereinafter referred to as the 'CT Act'], resident taxable persons include:

- business associations established under Act V of 2013 on the Civil Code, and, before 15 March 2014, Act IV of 2006 on Business Associations (such as joint-stock company, limited liability company (kft.), general partnerships (kkt.), limited partnerships (bt.) and other organisations (e.g. foundations, associations);
- non-resident taxable persons with a place of business management in Hungary.

From 2019, the CT Act allows at least two taxpayers to create a corporate taxpayer group if certain conditions are met. Members of a corporate taxpayer group may be the following entities:

- business/economic company (except not-for-profit economic company),
- association,
- European public limited-liability company,
- cooperative society (except certain types of cooperatives),
- European cooperative society,
- sole proprietorship,
- foreign person considered a resident taxpayer due to the location of the head office,
- any non-resident/foreign entrepreneur via its Hungarian branch.

Generally the tax year corresponds to the calendar year. However, pursuant to the Accounting Act, taxable persons may exercise discretion in deciding on the operation of a financial year differing from the calendar year, especially if it is made reasonable by the characteristics of operation (with special regard to the cyclicity of the course of business or the information claim of the parent company).

2. Taxable income

The incomes deriving both from Hungary and abroad of resident taxable persons shall be subject to tax. Pre-tax profit, determined by applying the tax base increasing and decreasing items set forth in the Corporate Tax Act, represents the corporate tax base.

Pursuant to the general anti-avoidance rule, the Tax Authority shall qualify contracts, transactions and other similar acts in accordance with their true contents. A further general anti-avoidance provision is that the costs and expenses accounted for on the basis of a legal transaction (series of legal transactions) cannot be effected if their main

purpose or one of their main purposes is only to achieve a tax advantage (tax exemption, tax allowance, tax relief) that is contrary to the purpose of the tax law.

Items adjusting the tax base include:

2.1 The tax base must be increased with the costs and expenses incurred in relation to items specified in legislation, including e.g. fines, penalties, late payment penalty interest due to delay in the payment of taxes.

2.2 Depreciation

Regarding taxation, the entire purchase value or cost of production – in the course of several years – may be written off the tax base.

2.3 Development reserve

The portion of the retained earnings committed to future capital investments (development reserve) shall be regarded as accelerated depreciation and can be deducted as a lump sum from the pre-tax profit. The taxpayer may release the non-distributable reserve exclusively in accordance with the costs of the implemented capital investment over 4 tax years following the generation of such reserve. The full amount of the development reserve set up under this title cannot exceed the amount of the pre-tax profit per tax year.

2.4 Provisions

The tax base must be increased with the amount of the provisions for probable liabilities and future costs accounted for as expenses; however, the amount recognised as income due to the utilisation of such provisions qualifies as a tax-base decreasing item.

2.5 Losses

In principle, deferred losses of previous tax years (negative tax bases), can be deducted from the tax base in an amount of the taxpayer's choice, in the forthcoming five tax years after the occurrence of the losses (up to 50% of the tax base calculated without losses), and the deferred but not yet deducted loss may be rolled on, with regard to the time limit of five tax years.

2.6 Dividend

Income from dividends is deducted from the tax base when the corporate tax liability of Hungarian companies is determined. The amount of dividends received from a controlled foreign company cannot be deducted from the tax base insofar as it relates to genuine legal transactions.

From 1 January 2006, income from dividends is not subject to dividend tax. No withholding tax is imposed on dividends paid by a resident company to another (either resident or non-resident) company. (This is not the case – according to a separate law – if dividends are allocated to private individual members of a resident company).

2.7 The tax base of taxable persons in contact with a controlled foreign company

Increases the profit before tax in the tax year of the controlled foreign company in which the last day of the tax year (fiscal year) of the controlled foreign company is, the part of the positive taxed profit recognised on the last day of the tax year (fiscal year) of

the controlled foreign company, less an approved (distributed) dividend, to the extent that it is linked to assets and risks related to the significant personal functions performed by the taxpayer, provided that the amount thus obtained is positive.

Payments made to the controlled foreign company do not usually qualify as eligible cost incurred in favour of the undertaking except if the taxable person can prove that the payment has incurred in connection with its business activity.

2.8 Transfer price

Transfer price regulations are based on OECD guidelines. Under transfer price regulations, if prices applied in related-party transactions differ from arm's length prices applied by unrelated parties, the company

- may decrease its pre-tax profit by the difference, provided that:
 - the consideration applied renders the pre-tax profit greater than it would have been in case the arm's length prices had been applied and
 - the related party is also a resident taxpayer or such non-resident company which is subject to corporate tax in their country of residence (with the exceptions of controlled foreign companies) and
 - it holds a document signed by both parties establishing the amount of the difference, or
 - it has a declaration by the other party that the other party takes into account (taken) the amount of the difference (determined by the normal market price under the other party law) when determining the basis for corporation tax or equivalent tax; Or
- shall increase its pre-tax profit by the difference, provided that the consideration applied renders the pre-tax profit smaller than it would have been in case arm's length prices had been applied.

The above rules of transfer pricing shall not be applied to long-term agreements concluded by small and medium-sized enterprises if the associated enterprise was established in the interest of purchases and sales and the voting rights of the small and medium-sized enterprises held in the affiliated company exceeds 50 per cent on the aggregate.

3. Rules of income (profit) minimum

Pursuant to regulation on income (profit) minimum, if pre-tax profit or the tax base, whichever is higher, does not reach 2% of the adjusted total income, the taxpayer shall

- pay tax on 2 % of the adjusted total income, otherwise
- make a statement in the form complementing the tax return, which shall qualify as a return.

4. Tax rate

As of tax year 2017 the corporate tax rate is 9 % of the positive tax base.

5. Tax allowances / tax benefits

5.1 Development tax allowances

Among others, development tax allowances can be obtained regarding the following investments:

- (1) investments worth at least HUF 3 billion at present value;
- (2) investments worth at least HUF 1 billion started and operated within the administrative jurisdiction of a preferential municipal self-government;
- (3) investments of at least HUF 100 million aimed at establishing food hygiene conditions, stand-alone environmental protection investments, investments in basic research, applied research or experimental development;
- (4) investments of at least HUF 100 million related to the production of films and videos;
- (5) investments promoting the creation of jobs.

5.2 Tax allowance of sponsoring spectator team sports

By applying the tax allowance granted by legislation, taxpayers may achieve a tax saving if they support organisations with an approved sport development programme conducting activities in any of the following six sports.

Spectator team sports include:

- (1) football;
- (2) handball;
- (3) basketball;
- (4) water polo;
- (5) ice-hockey;
- (6) volleyball

5.3 Additional tax allowances

In addition to the above, the assessed tax may be reduced with the following tax allowances:

- (1) Tax allowance for supporting film making,
- (2) Tax allowance for supporting cooperatives to create community funds,
- (3) Tax allowance for the SMEs investment credit interest,
- (4) Tax allowance for supporting energy efficiency investment, renovation,
- (5) Tax allowance for supporting live music service,
- (6) Tax allowance for research and development activities,
- (7) Tax allowance for investment in the construction of an electricity storage facility,
- (8) Tax allowance for investments and renovations aimed at restoring environmental damage and other specific environmental protection objectives

6. Avoidance of double taxation

Double taxation may be avoided unilaterally or on the basis of a treaty. A unilateral tax withholding shall be applied to income taxes paid or payable abroad, limited to 90% of

the foreign tax and may not exceed the amount determined according to the Hungarian rules.

If a **treaty** is to be observed, allowances serving the purpose of avoiding double taxation may be obtained under the treaty.

7. Non-resident individuals

7.1 Foreign companies conducting entrepreneurial activities in premises in Hungary (known as 'non-resident entrepreneurs' in Hungary) shall pay tax on their income deriving from their entrepreneurial activities conducted in premises in Hungary. The cases in which foreign companies shall apply a form of business establishment in Hungary (for example establishing a branch office) are specified by specific other legislation. A branch office is an organizational unit of a foreign company, without legal personality, vested with financial autonomy but registered in Hungarian company registration records. For taxation purposes, a branch office is considered a place of business in Hungary if it complies with the definition of place of business provided under tax legislation. The definition of 'place of business' in the Corporate Tax Act fundamentally corresponds to the one in the OECD Model Convention. However, sites of construction or assembly operations – in case of lacking a convention – may be regarded as a place of business only after at least three months elapse.

Taxable incomes related to the place of business shall be determined under the rules applicable to resident companies. Furthermore, the tax base of a foreign entrepreneur in respect of their place of business in Hungary shall be adjusted by reducing it by a portion of its operating costs and expenses and overhead charged to the place of business establishment as commensurate with total revenues and be increasing it by operating costs and expenses and overhead of the place of business charged to the pre-tax profit or loss; furthermore, it shall be increased by 5 per cent of the revenues earned through but not accounted for at the place of business.

The profit of the place of business is subject to tax at the general tax rate and also tax allowances may be obtained, if relevant conditions are fulfilled.

No corporate tax liability is incurred by foreign organisations with no place of business in Hungary with respect to their revenues deriving from Hungary.

7.2 Non-resident individuals who obtain any income through the transfer or withdrawal of their share in a company with real estate holdings ('member of a company with real estate holdings' in Hungary), incur corporate tax liability with respect to this income. Corporate tax is calculated at the general corporate tax rate and payable to the Hungarian Tax Authority. The tax base of members of companies with real estate holdings shall comprise the consideration received upon the transfer of their share in the company, or the sum received when decreasing the subscribed capital of the company through disinvestment, less the costs of acquisition or maintenance as verified, if the resulting amount is positive.

8. Administration (tax refund and tax return, payment of taxes)

The annual corporate tax return shall be filed by taxpayers operating according to the calendar year by 31 May of the year following the tax year. In case of taxpayers opting

for a business year other than the calendar year, a return shall be filed until the last day of the fifth month following the last day of the tax year.

Corporate tax shall be established by the taxpayer through self-assessment.

OTHER INCOME TAXES

Local governments impose a local business tax on business activities carried out on a permanent basis at a maximum rate of 2%, which shall be collected by the tax authorities of local governments of Hungary.

TAXES IMPOSED ON PROPERTY

In Hungary, local taxes, i.e. building tax and land tax, are payable to the local government. Owners are liable to pay the above taxes. The annual maximum rate of building tax is HUF 1,100 per square metre or a maximum 3.6% of the market value of the real property. The annual maximum rate of the land tax is HUF 200 per square metre or 3% of the market value. The above taxes can be accounted for as costs when determining the corporate tax base.

National Tax and Customs Administration