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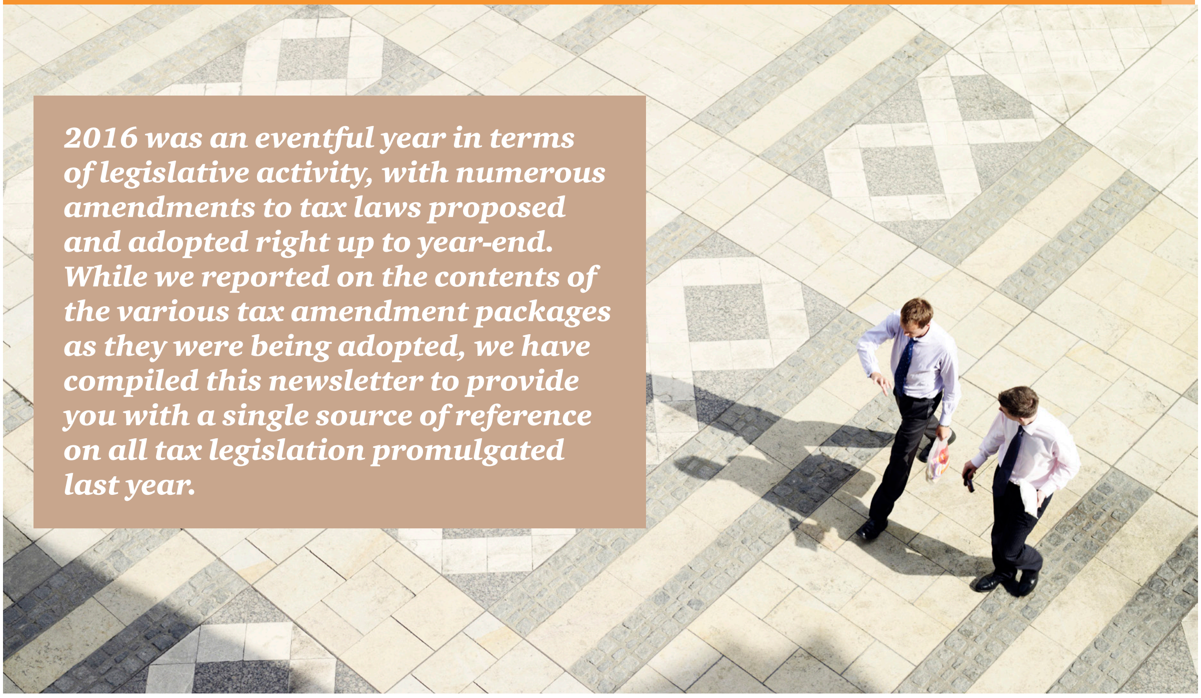

2016 was an eventful year in terms of legislative activity, with numerous amendments to tax laws proposed and adopted right up to year-end. While we reported on the contents of the various tax amendment packages as they were being adopted, we have compiled this newsletter to provide you with a single source of reference on all tax legislation promulgated last year.

Content

Changes to tax proceedings

Taxpayer classification

From 1 July 2016, the total tax difference charged to taxpayers classified as "reliable" has to be reduced by the total tax difference credited to these taxpayers during the current year and the preceding five years.

As of 1 January 2017, the tax authority will be transferring VAT refunds to public limited liability companies within 30 days.

The criteria for classifying taxpayers as reliable or high-risk has changed, along with the related legal consequences.

A new requirement for reliable taxpayer status is that the sum of taxes paid by the taxpayer in the year concerned must be positive, meaning that dormant companies will no longer qualify for reliable status.

In addition, reliable taxpayers are automatically provided payment facilities. This means that reliable taxpayers may request a payment facility for a period of 12 months, without incurring a surcharge. This option may be exercised once a year, provided that the taxpayer's net outstanding tax liabilities do not exceed HUF 1.5 million at the time its request is evaluated. Reliable taxpayers may thus pay their taxes in instalments or even request a payment deferral. This is expected to benefit more taxpayers, since the HUF 500,000 limit has been raised to HUF 1.5 million. Under the amended legislation, public limited liability companies no longer need to have been in operation for at least three years in order to be classified as reliable.
The scope of high-risk taxpayer status has also been extended. The amended legislation provides that companies undergoing involuntary deregistration and taxpayers who have amassed unpaid default fines exceeding 70% of their tax payments also be slotted into the "high-risk" category. High-risk status is also attributed to companies whose registered office is registered at an office service provider and that were subject to a default fine imposed in a binding decision in the year concerned or in the three preceding years. Companies headquartered at registered office service providers have become subject to a more in-depth data supply obligation.

Tax audit of binding rulings

On 1 July 2016, a new type of tax audit was introduced: binding rulings are now fact-checked to find out whether the events underlying a binding ruling actually occurred, and if so, whether the ruling in question is binding on the tax authority. During the audit, the tax authority may only request documents specifically mentioned in the binding ruling as records that, if issued, kept or retained, prove that the underlying events have actually occurred. Regarding binding rulings becoming final and binding before 31 December 2015, the proceedings may also be initiated by the taxpayer.

Another change is that the expert opinion of the Hungarian Chamber of Auditors must be attached to requests for a binding ruling pertaining to IFRS accounting.

Publication obligation under the block exemption regulation

From 1 July 2016, in accordance with Article 9 of Commission Regulation (EU) No 651/2014 ("block exemption regulation"), the Member States concerned must ensure the publication of relevant information on each individual aid award exceeding the HUF equivalent of EUR 500,000. According to the amended legislation, for aid in the form of tax advantage, the required information on individual aid amounts in the specified ranges must be published within one year of the date the tax declaration was due, and must be available for at least 10 years after the date on which the aid was granted.

Self-revisions after the limitation period

According to the amended legislation, from 1 July 2016, taxpayers may, subject to a final court decision, submit self-revisions even after the right of tax assessment has lapsed, in order to meet their tax obligations. Based on the self-revision, the tax authority may conduct an audit within one year. For periods already closed by an audit, the related tax obligation may be corrected by means of a re-audit at the taxpayer's request.

Assistance procedure

From 1 January 2017, the tax authority is offering a new service: the assistance procedure. In essence, where errors or deficiencies are identified by risk assessment, the tax authority may, rather than commencing an audit, offer to assist the taxpayer in remedying those errors and deficiencies and invite it to conduct a self-revision. Participation in the procedure is voluntary. Infringements remedied under an assistance procedure are not subject to sanctions, but if the procedure is unsuccessful, the tax authority may commence a tax audit.

Food and beverage vending machines

The sale of food and beverages through vending machines will be subject to a data supply obligation from 30 June 2017. By that date, a monitoring device must be installed in every vending machine, except where, according to a unanimous declaration by monitoring service providers, it is technically impossible to install such equipment in the machine concerned. In addition, the relevant regulation sets out detailed rules concerning the licensing, operation, and liability of monitoring service providers.

Changes related to personal income tax, social security contributions, and the social tax

Clarifications and changes to statutory definitions

The definition of secondment changed on 1 August 2016: official and business trips (other than commuting to work or travelling to the employer's registered office or place of business) will also qualify as secondment.

Other smaller changes and clarifications have also been made in connection with allowances related to pension insurance, and reporting on controlled capital market transactions. The definition of "primary agricultural producer" has been amended, and the rules on the taxation of income from long-term investments have also been clarified.

In connection with employer-assisted housing benefits, from 1 January 2017, the amended laws include definitions for "modernisation", "accessibility", "reasonable housing need" and "family member sharing the same household".

The amended regulation aims to align the definition of seconded employee, as found in the Act on Personal Income Tax, with the provisions of the new Labour Code. In connection with employer-assisted housing benefits, the definitions entering into force from 1 January 2017, including for terms such as "reasonable housing need" and "family member sharing the same household", have been made clearer.

Personal income tax

The amended legislation extends the scope of the five-year phased tax base reduction to include all types of real estate (currently this only applies to intangible asset rights related to residential property). This means that, from 1 January 2017, income from the sale of all types of real estate will be tax exempt from the fifth year following the year of acquisition.

Along with the reduction of the corporate tax rate, the rate of income tax payable by individual entrepreneurs has been reduced to 9%.

In accordance with the amended definition, the rules concerning controlled foreign companies are no longer included in the Personal Income Tax Act. Consequently, dividend paid in 2017 by companies that no longer qualify as controlled foreign companies as of 2017, will be treated as dividend income (rather than as other income), which will result in a significantly reduced tax liability.

Draft tax returns for more taxpayers

Effective from 1 January 2017, the tax authority will prepare draft personal income tax returns for taxpayers registered for electronic tax filing who have either not requested their employers to prepare their tax return for them or whose request was not granted. Under the amended legislation, taxpayers not registered for electronic tax filing may also request the tax authority to prepare their draft tax returns, at the latest by 15 March of the year following the tax year.

We note that the draft tax returns may not necessarily include all income that the persons concerned are required to declare. This is because the draft tax returns are based on data (e.g. on wages paid by a Hungarian-based employer) that is reported to the tax authority during the year. However, not all items of income are subject to interim reporting. Therefore, the draft tax returns should be carefully reviewed and corrected or supplemented if necessary.

Reduced charges on interest income

The 6% healthcare tax on interest income was eliminated on 1 January 2017. Thus, interest credited after 31 December 2016 is only subject to personal income tax.

Promoting labour mobility

The amended legislation has implemented several changes aimed at promoting labour mobility. On 1 January 2017, the tax-exempt reimbursement that can be provided to employees using their own cars to commute to work increased to HUF 15/km from the previous HUF 9/km. It is now also possible to provide tax-exempt housing assistance for labour mobility purposes under the conditions and to the extent specified by law.
Under the amended regulations, providing accommodation in any real property owned or rented by the payer (workers' hostel or other employer-assisted housing) qualifies as a tax-exempt benefit even if only one person is housed in a given residential space.

Sporting events

There is a new statutory definition for "sporting event" from 1 August 2016. Accordingly, tax exemption will only apply to sporting events organised by a sports association or other sports organisation. Other economic operators no longer have this opportunity as of the above date.

Tax-exempt benefits

From 1 January 2017, in addition to child day-care services and benefits, kindergarten services and benefits will also qualify as tax-exempt benefits.

Fringe benefits

On 1 January 2017, the current fringe benefit system changed significantly. Fringe benefits now essentially comprise cash benefits and amounts credited to SZÉP cards. Only cash amounts provided within the annual threshold and amounts credited to SZÉP card sub-accounts within the statutory limits qualify as fringe benefits (the annual threshold is HUF 200,000 thousand per year for public sector workers, and HUF 450,000 per year for workers employed by non-public sector employers). Any part of the combined amount of benefits qualifying as fringe benefits (i.e. cash benefits and amounts credited to SZÉP cards) exceeding the annual threshold are regarded as other specific benefits. In the case of full-year employment, cash benefits of up to HUF 100,000 per year are taxed at a preferential rate, while cash benefits provided in excess of this amount are taxed as salary (i.e. this portion is not taxable as other specific benefits).

From 1 January 2017, previous fringe benefits are taxed as other specific benefits, i.e. at a higher tax rate.

Reduction in taxes and other dues on Cafeteria benefits

Under the previous rules for calculating taxes and other dues payable on fringe benefits (e.g. local travel passes) and certain specific benefits (e.g. private use of company phones) the tax base was the value of the benefits multiplied by a tax base increasing factor. As a result of the amendments, this tax base increasing factor has been reduced from 1.19 to 1.18. Consequently, from this year taxes and other dues have been reduced by about 0.3 percent on fringe benefits and by about 0.4 percent on certain specific benefits. Taking the reduced healthcare tax into account as well, the reduction amounts to 6.6%.

Social tax allowances

The amending act reintroduced the "Karrier Híd" Programme from 1 August 2016: employers of persons whose previous job was in the public sector will once again be eligible for social tax allowance. The tax allowance for employing career starters under 25 and job seekers who have been out of work for a long period will be available even in the event of a change of employer. A new social tax allowance was introduced for in-house R&D activities, with effect from 16 June 2016.

Social tax

Under the amended legislation, the social tax rate was reduced to 22% on 1 January 2017, and will be reduced to 20% a year later. In line with the above amendment, there are also several changes that affect the rate of social tax allowances. Instead of the allowances of 27%, 13.5% or 14.5% available previously, the rate of the social tax allowance will be equal to the tax rate or 50% thereof. This will reduce employers' payroll expenses by 3.9%.

From 1 January 2017, no social tax liability will arise on remuneration paid to workers who are exempt from contribution liabilities in Hungary (whether under certain internal rules or international treaties) in respect of the exemption period, even if such remuneration is paid after the expiry of the exemption period.

Healthcare tax

The rate of healthcare tax (27%) was reduced to 22% on 1 January 2017, and will be reduced to 20% on 1 January 2018, in line with the reduction of the social tax rate. As a result, public dues payable for business meals, corporate events and certain cafeteria benefits have been reduced from 49.98% to 43.66% in total.

Secondments of third-country nationals

Third-country nationals employed by a foreign employer and working in Hungary under a secondment arrangement will be exempt from the social security and social tax payment obligations if the duration of their secondment is less than two years.

The above rule will also apply to third-country nationals seconded to Hungary who are insured in their home country and whose country of nationality has a bilateral social security agreement with Hungary, as well as to EU nationals who are not covered by the relevant EU social security regulations and are insured in and seconded to Hungary from a third-country. These rules may be applied to secondments that commenced on or after 1 January 2016.

If the secondment is extended to more than two years, special rules will apply. In contrast with the previous rules, if the extension is due to unforeseen circumstances, and the employee concerned duly informs the tax authority of this, the social security and social tax payment obligations will arise from the end of the second year. This rule may be applied to secondments that commenced on or after 1 January 2016.

Less administration for Airbnb hosts

On 1 January 2017 the itemised flat-rate tax for private persons providing accommodation services was raised to HUF 38,400, while their health care tax liability was eliminated. Hosts opting for flat rate taxation will not see a change in their actual tax burden, but will certainly benefit from a reduction in their administration obligations through declaring and paying the amount corresponding to the former health care tax as part of their itemised flat-rate tax.

Less administration for claiming the tax incentive for first-time married couples

Under the previous rules, entitlement to the special tax incentive for first-time married couples ends upon conception of a child. According to the amended legislation, conception will no longer affect entitlement to this tax incentive. Under a transitional provision, the amended rules will apply to all marriages entered into after 31 December 2014. This is intended to ensure that the incentive can be claimed retroactively – e.g. by self-revising tax returns for 2015 – by those who were unable to do so previously due to conception of a child.

Amendments to the act on the economic stability of Hungary

Effective 18 January 2017, the amended legislation will repeal the provisions pertaining to the Stability Savings Account. However, private individuals will be able to choose to pay the 10% personal income tax on certain types of income earned before 30 June 2016 from sources other than payers of taxable income. In addition to personal income tax, a self-revision fee will also have to be paid on such income. The tax can only be paid through a bank designated for this purpose by the national tax authority; additional rules on the fulfilment of this tax liability are laid down in an implementing regulation. Private individuals will be able to choose this new option in respect of tax liabilities incurred in any prior year. The procedure is anonymous, as the designated bank will not disclose information on the private individual or the income. During a tax audit, the individuals concerned will be able to prove that they have fulfilled their tax obligations using a certificate issued by the bank.

The acquisition of shares or other members' equity issued by a legal person or other organisation will not give rise to any tax, contribution or duty liability if the shares or members' equity are acquired between 1 January and 30 June 2017 under transparent conditions. The exemptions can only be used if the party acquiring the shares free of charge reports the acquisition to the national tax authority, or if the purchase price of the shares is paid through a bank based in an EEA Member State (the detailed rules will be laid down in an implementing regulation). The rules on reported shareholding will not apply to shares acquired as described above.

Changes related to value added tax

Extending the scope of the reduced VAT rate

According to the amended regulations, the scope of goods and services subject to the reduced VAT rate has been extended. On 1 January 2017, the VAT rate on poultry, eggs and fresh milk (except for breast milk, UHT and ESL milk) was reduced to 5%, and the 27% VAT rate on internet services was reduced to 18%.

The catering sector will also benefit from VAT rate cuts: on 1 January 2017, the 27% tax rate was reduced to 18%, and will be reduced once again from 1 January 2018 to 5%, on meals provided and certain non-alcoholic beverages prepared locally in bars and restaurants.

Tourism development contribution

In parallel to the introduction of the 5% VAT rate, the providers of catering services subject to the preferential VAT rate will have to pay a tourism development contribution from 1 January 2018. The contribution base will be the price (excluding VAT) charged for the service, and the rate will be 4%.

The contribution will be determined by self-assessment, and the frequency of reporting will depend on the taxpayer's VAT filing frequency. The contribution will have to be reported and paid for the VAT filing period during which the services shown in the invoice or other accounting document were supplied, or if no date of supply is indicated, the period in which the invoice or other accounting document was issued. For periods in respect of which the service provider is not required to file VAT returns, the deadline for reporting and paying the contribution will be 25 February of the year following the date of supply within the meaning of the VAT Act. Revenues from the contribution must be spent on tasks related to tourism development.

Domestic recapitulative statement

According to the amended legislation, domestic recapitulative statements must be filed for all invoices with a VAT content of HUF 100,000 instead of the previous threshold of HUF 1 million. Therefore, as of 1 January 2017, the customer's tax number must be indicated on all invoices that reach this threshold. It is not mandatory to show the customer's tax number in invoices that were issued in 2016 with a settlement date in 2017.

Online data supply

From 1 January 2017, VAT taxpayers are required to supply data online to the tax authority on invoices that are issued using invoicing software and have a VAT content of at least HUF 100,000. In the first half of 2017, taxpayers may supply such data voluntarily, but will be obliged to meet this obligation from 1 July 2017. The tax authority is entitled under separate legislation to monitor and perform direct data queries from the invoicing software through telecommunications equipment.

Domestic reverse charge mechanism

The amended legislation provides that, from 1 January 2017, the reverse charge mechanism applies not only to construction services subject to a construction authority's permit or acknowledgement procedure but also to all construction services subject to a simple reporting obligation. In addition, the scope of the reverse charge mechanism has also been extended to cover the sale of chromium and vanadium waste and debris.

EKÁER reporting

Under the amended legislation, from 1 August 2016, a reporting obligation under the Electronic Road Freight Control System ("EKÁER") applies not only to deliveries performed using a vehicle subject to toll payment but also to deliveries in which the vehicle itself is not subject to toll payment, but its actual gross weight, including the goods transported, exceeds 3.5 tons. A further change is that carriers are required to keep the official seal intact until removed by the tax authority. Carriers that fail to meet this obligation are subject to a default fine of up to HUF 1 million. The tax authority may retain the vehicle without a specific decision until the default fine is paid. A further default fine may be imposed if the amount of the goods reported is higher than the amount of goods transported. The default fine may amount up to 40% of the value of goods reported but actually not transported.

The rules governing the EKÁER have been amended to include an obligation to provide risk deposits. Accordingly, for EKÁER reports filed after 15 February 2017, taxpayers that have not filed an EKÁER report or a VAT return or have had their tax number suspended in the year concerned and in the preceding two years, must provide a risk deposit for their first 10 reports, but no less than for a period of 180 days, in respect of intra-Community acquisitions of goods and the first taxable supply of goods in Hungary to parties other than end users.

Online connection of vending machines to the National Tax and Customs Authority

From 1 January 2017, vending machines (e.g. beverage vending machines) must be equipped with a monitoring device that facilitates data reporting to the tax authority. The amended legislation allows the tax authority to monitor vending machines through telecommunications equipment and to perform direct data queries.

Changes to the value threshold for individual tax exemption

Effective from 1 January 2017, the previous HUF 6 million threshold for individual tax exemption was raised to HUF 8 million. Under the transitional provisions, individual tax exemption is also available to taxpayers whose sales revenue in 2014, 2015, or 2016 was over HUF 6 million, but did not exceed HUF 8 million. This amendment could result in a significant increase in the number of taxpayers opting for individual tax exemption.

Changes to the reporting obligation of VAT payers concerning passenger cars

Under the amended legislation, taxpayers subject to VAT also have to report the vehicle identification number (chassis number) of passenger cars in the following cases: (i) import, (ii) intra-Community acquisition, and (iii) intra-Community supply. The required data must be provided in the VAT returns.

Changes related to customs regulations

The amended provisions concerning Act XIII of 2016 on the Implementation of Union Customs Law were laid down based on experience and observations since the Act's entry into force on 1 May 2016. Accordingly, the new regulations contain mostly technical amendments and additions. However, they also incorporate a number of material changes, such as the following:

- Under the general rules, deadlines for customs authority proceedings launched ex officio will be the same as for proceedings initiated upon request.
- The detailed rules on repeated audits conducted by the customs authority have been set out.
- In the interest of uniform legal interpretation, the amended legislation also sets out detailed rules for amending customs authorisations issued under the Community Customs Code that are still in effect.

Changes concerning corporate tax

New corporate tax rate

On 1 January 2017, the corporate tax rate was reduced to 9%. As a result, progressive exemption will no longer be available. The introduction of a flat corporate tax rate will affect payable and deferred tax calculations.

Transitional provisions concerning the tax rate change

Due to the introduction of the new tax rate, transitional provisions will apply to calculating corporate tax advances payable in the first half of 2017, as well as from July 2017. Concerning the first half of the 2017 tax year, taxable persons that established their tax liabilities for 2015 using the 19% tax rate will have to pay a tax advance of 50% of the total of their tax established at a rate of 10/19% for 2015 and HUF 20 million, but not more than 50% of the tax paid for the 2015 tax year. Tax advances payable in the second half of 2017 and the first half of 2018 will have to be calculated at the 9% tax rate.

Changes concerning the development tax incentive

According to the amended rules, the period for applying the development tax incentive has been extended for requests and declarations submitted after 31 December 2016. The tax incentive may be applied in the tax year in which the investment project is put into operation (or, at the taxpayer's discretion, in the following tax year) and in the following twelve tax years (previously, nine tax years), but no later than during the sixteenth tax year (previously, the fourteenth tax year) following the tax year in which the report or the application was submitted.

The headcount- and wage increase-related requirements of eligibility for the development tax incentive were significantly lowered on 1 January 2017.

For investment projects of at least HUF 3 billion in present value, taxpayers must increase their staff number by at least 50 persons, or their wage costs by at least three hundred times the minimum wage; for investment projects of at least HUF 1 billion in present value, taxpayers must increase their staff number by at least 25 persons, or their wage costs by at least one hundred fifty times the minimum wage, in order to be eligible for the tax incentive. By way of comparison, for investments of at least HUF 3 billion, the required increase in staff numbers was previously 150 persons.

For investment projects of at least HUF 500 million in present value carried out by small and medium-sized enterprises, the required increase will be at least 5 persons or ten times the minimum wage for small enterprises, and at least 10 persons or twenty-five times the minimum wage for medium-sized enterprises.

Corporate tax incentive for investment projects aimed at energy efficiency

A corporate tax incentive was introduced on 1 January 2017 for the implementation and operation of investment projects aimed at improving energy efficiency by reducing final energy consumption, as laid down in separate legislation.

The tax incentive can be up to 30% of eligible costs (but not more than the HUF equivalent of EUR 15 million at present value), which can be increased by 20 percentage points for small enterprises, and 10 percentage points for medium-sized enterprises. The tax incentive can be used at the earliest in the tax year in which the investment became operational, and in the following five tax years.

The project must be operated for at least five years. The tax incentive may only be claimed in connection with projects aimed at energy efficiency and launched after the new regulations have entered into force, and only for eligible expenses incurred after the start of the project. The amendments also stipulate that the tax incentive for investment projects aimed at energy efficiency and the development tax incentive cannot be used at the same time.

Changes concerning the tax incentive for supporting sports and culture

Effective from 1 January 2017, the period for applying the tax incentive for providing financial support to performing arts organisations and sports organisations for popular team sports was extended to include the eighth calendar year (previously, the sixth tax year) following the year in which the support was provided. Under the amendments, taxpayers have to pay as supplementary support and additional supplementary sports development support an amount equal to at least 75% of the primary support amount as increased by corporate tax at a rate of 9%. At the same time, additional supplementary support and additional supplementary sports development support has been eliminated.

The amended legislation stipulates that following the promulgation of the relevant law (25 November 2016) taxpayers that provide supplementary support after the deadline but until the date on which the company's tax return is filed are eligible for 80% of the tax incentive stated in the support certificate.

If the 30-day deadline following the payment of supplementary and additional supplementary sports development support expires after the corporate tax return is filed for the tax year in which the support was provided, taxpayers will not be required to submit an extra report to the tax authority but may report payments in their corporate tax returns for the tax year in which the support was provided.

Corporate tax incentive for companies investing in business startups

From 1 January 2017, pre-tax profits may be decreased by three times the cost of shareholdings acquired in startup companies. The tax incentive can be used in four equal instalments, in the tax year of acquisition and in the three subsequent tax years, but only up to HUF 20 million per tax year.

"Business startup" is defined as a legal entity registered under separate legislation, with a headcount of at least two persons, one of whom must be employed in a research and development role (other requirements laid down in the relevant regulations may also apply). The detailed requirements will be specified in separate legislation.

Taxpayers may take advantage of the tax incentive if they acquire a shareholding in the equity of a business startup in which neither the taxpayer nor its legal predecessor or its related party was a member in the three tax years preceding the acquisition. The amount that taxpayers use based on the tax incentive, and the amount that business startups receive as investment qualifies as de minimis aid. The amended regulations stipulate an obligation to increase the tax base if the shareholding is derecognised, and imposes sanctions if this obligation is not met.

Tax incentive for providing housing assistance for labour mobility purposes and setting up accommodation facilities for workers

The amended legislation clarifies that starting from 1 January 2017 the corporate tax base may be reduced by the aggregate of the investment cost and the increment of cost of accommodation facilities for workers, as defined by the Act on Personal Income Tax, rather than the costs and expenditures recognised in the tax year in which the relevant construction or renovation project is completed. The corporate tax base may also be reduced by the rent of property rented for the purpose of providing accommodation facilities for workers.

Corporate tax incentive promoting the preservation of listed historic buildings

As of 1 January 2017, the amended legislation extends and formulates more precisely the scope of corporate tax incentives promoting the preservation of buildings included in Hungary's official list of historic buildings, structures, objects and sites deemed worthy of preservation. Accordingly, in addition to listed and locally protected properties, buildings and structures registered as having special historic or cultural significance will also be eligible for the tax incentive. The amended rules provide a non-exhaustive list of protected fixtures, protected areas, historic gardens, burial sites or their remnants, or any combination of the above.

According to the amendments, the tax incentive is derived from the total cost of the investment or renovation, rather than from the expenses incurred during a given tax year (the tax incentive will be twice the total cost). The part of the tax incentive not used by the taxpayer can be used by the taxpayer's related companies, regardless of whether it is related to maintenance, renovation or other investment.

Corporate tax incentive for support provided to the Disaster Relief Fund

From 1 January 2017, taxpayers supporting the Disaster Relief Fund may be eligible for a corporate tax incentive. The tax incentive is 50% of the (financial) support provided.

Corporate tax incentive for live music services

From 1 January 2017, taxpayers will be eligible for a tax incentive based on the consideration (fees) they have accounted as costs or expenses for live music services provided in the restaurants they operate. The tax incentive may be up to 50% of the consideration (fees) accounted in the given tax year (exclusive of VAT).

The amendments stipulate that the portion of expenses recognised as consideration (fees) paid for live music services by which taxpayers reduce the tax payable, will not be deductible from the tax base. The tax incentive claimed during the tax year will be treated as de minimis aid.

Changes in the principles concerning tax evasion

According to the stricter principles introduced as of 1 January 2017, taxpayers will not be eligible for a tax advantage if their transactions are aimed mainly (rather than exclusively, as was the case previously) at achieving a tax advantage.

Definition of controlled foreign company

As a first step of implementing the relevant EU regulation, the definition of "controlled foreign company" has changed. The new definition, effective from 18 January 2017, and the related items adjusting the pre-tax profit or loss rely significantly on the Council Directive laying down rules against tax avoidance practices that directly affect the functioning of the internal market (Anti-Tax Avoidance Directive, ATAD), but also show some differences.

According to the new rules, a foreign entity or permanent establishment will be treated as a controlled foreign company if a Hungarian taxpayer holds a direct or indirect participation of more than 50%, or owns directly or indirectly more than 50% of capital or is entitled to receive more than 50% of the profits of that entity, provided that the actual corporate tax paid by the entity or permanent establishment is less than half the corporate tax that would have been charged on the entity or permanent establishment under the Hungarian corporate tax system. The above provisions will not apply if the foreign entity or permanent establishment can demonstrate that it pursues actual economic activities, or that on the first day of the tax year it has at least one owner (or that owner has an associated enterprise) that has been listed on a recognised stock exchange for at least five years.

As a general rule, companies that have permanent establishments with a low effective tax rate, direct or indirect subsidiaries with a low effective tax rate can expect adverse tax consequences. Nevertheless, the wording of the legislation raises several interpretation issues. Therefore, companies that have direct or indirect subsidiaries, or permanent establishments with a low tax burden are recommended to consult their advisors until these issues are clarified.

Changes affecting tax allowance for royalty

As of 1 July 2016 the tax allowance for royalties received was reduced based on a redefinition of royalty, to include only income from patents, property rights and software copyright. Besides the narrowed definition, taxpayers are eligible for a tax allowance based on income from royalties to an extent to which the intangible assets are generated as a result of their own research and development activities. The direct expenses of R&D services ordered from related companies, and the historical cost of intangible assets purchased (received) from related companies may be recognised as direct expenses of own research and development activities up to 30% of the own R&D expenses. Based on a transitional provision, taxpayers may apply the previous rules to intangible assets recorded before 30 June 2016.

Changes affecting financial support provided free of charge

According to the amending act, taxpayers that provide grants and other forms of financial support free of charge will be required as of 1 January 2017 to increase their tax base by the amount of that support if the recipient is not liable to pay corporate tax on this income.

Preferential transformation and transfer of assets

Under the amending act, with effect from 1 January 2017, companies that perform a preferential transfer of assets and sell their acquired shares following the transfer, during the period for which they have a deferred tax liability, will be required to increase their tax base by the amount they previously used as a tax base decreasing item (not to exceed the amount not yet accounted as deferred tax by the receiving company), while the receiving company may establish its tax base irrespective of the tax deferral. A further change is that taxpayers that perform a preferential transfer of assets or a preferential transformation will be required to justify the transaction from the economic and commercial perspectives.

Changes affecting related companies

Under the amended legislation, beginning with any tax year starting in 2018, transfer prices between related companies may be used as decreasing items only if the related company declares that it takes into account the difference between the price applied and the arm's length price when calculating the corporate tax base.

Taxpayers whose receivables from their related companies turn into bad debts, will be required to supply data on their related companies and the economic reasons underlying the transaction in their corporate tax return.

According to the amendments, Hungarian permanent establishments are not obliged to prepare transfer pricing documentation if they are exempted from paying corporate tax in Hungary based on an international convention.

Loss carry-forwards for R&D activities

Effective from 16 June 2016, companies with a negative corporate tax base may claim 9.5% of the tax base deductions applied on account of R&D activities as a social tax incentive, subject to the following criteria: at least 40% of the total revenues must be derived from R&D activities; the company must maintain at least one trainee position; and the average statistical headcount of R&D personnel in the tax year may not decrease by more than 10%. If applied, 50% of the above tax base deduction will be regarded as a loss carry-forward already used.

Extent of the capital expenditure tax incentive and the tax incentive on interest paid

According to the amended legislation, from 1 January 2017 SMEs may deduct from their tax base the full amount of capital expenditures relating to new tangible assets and the renovation of real property, while the amount of the tax incentive on interest paid on capital expenditure loans has further increased.

Changes concerning local taxes

General changes

From 1 January 2017, when deducting the cost of goods sold and the value of intermediated services from their net sales revenue, companies that qualify as related parties under the Corporate Tax Act are only required to determine their local business tax bases from consolidated data if the related party relationship was formed after 1 October 2016 as a result of a demerger.

The amended rules also allow credit institutions and financial enterprises that have opted for gross settlement when determining their net revenue, to deduct from their local business tax base the amount of purchased receivables accounted against expenditure on other financial services. The selected option can be applied retroactively to the local business tax bases of tax years beginning in 2015 and 2016.

Changes concerning the local business tax base

The amendments have reduced the gap between the rules on adjustments to the local business tax base (royalty, R&D) and the corporate tax base. As a result, effective from 1 July 2016 the definition of royalty was made narrower. In addition, from 1 January 2017 only amounts deducted from the corporate tax base may also be deducted from the local business tax base as direct costs of basic research, applied research, and experimental development. As for the definition of royalty, a transitional provision permits application of the previous rules until the tax year ending on or before 30 June 2021.

Setting up a single point of contact for filing local tax returns

From 1 January 2017, entities subject to local business tax may file their tax returns with the competent local municipality through the national tax authority. The national tax authority will forward tax returns to the competent local tax authorities in an electronic format only.

Definition of cultivated land located within municipal boundaries; tax exemption

From 1 January 2017, plots of cultivated land located within municipal boundaries, of a size not exceeding one hectare and registered as withdrawn from agricultural use, are no longer exempt from land tax if connection to the drinking water, power, and sewage grids is possible in an adjacent area.

Changes related to building tax

According to the amended legislation, from 1 January 2017, to qualify for exemption from local taxes, non-profit organisations are required to make a written declaration on not having had a corporate tax liability in the tax year preceding the year concerned, by the last day of the fifth month of the tax year. In addition, non-profit organisations may only claim tax exemption in regard to buildings, parts of buildings, or plots of land if registered as owners of the same in the Land Register.

From 1 January 2018, outdoor advertising structures placed on real property in the area of jurisdiction of a local government will be subject to building tax. The tax liability will arise on the first day of the year following the date the permit authorising the placement of the advertising structure is issued, or in the absence of such permit, the date on which the structure is placed. The subject of the advertising tax will be the owner of the advertising structure, and the tax will be calculated according to the display area expressed in square meters to two decimal places. The maximum tax payable will be HUF 12,000 per square metre.

Changes regarding duties

The preferential 2% property transfer duty will only apply to real estate agents who agree to resell the real estate to a buyer or lessee within two years. Otherwise the duty is 3%.

The amended legislation also significantly reduces the number of cases in which the tax authority may issue an order for payment. Accordingly, for exempt transactions, an order for payment will only be issued if the application of the exemption is subject to fulfilment of a specified condition.

Changes related to advertising tax

The amended legislation makes it clear that for online advertisements, the person or organisation that has right of disposal over the advertising space qualifies as the publisher of the advertisement (i.e. the subject of the advertising tax). In addition, the obligation to determine the advertising tax base from the consolidated data of related companies no longer applies.

In addition, from 1 January 2017, if a publisher of advertisements fails to comply with its obligation to make a declaration to the advertiser in relation to advertising tax, it must, on request, fulfil that obligation to the national tax authority. Failure to comply with such a request will attract a default fine of HUF 500,000; repeated failure to comply in respect of the same advertiser will be subject to a further default fine of HUF 10 million, and any further instance of non-compliance to a fine equalling triple the amount of the previous fine. Failure to comply with the registration obligation will incur fines according to the same regime. Further, in the case of failure to file a return on advertising taxes, the tax authority will levy a deemed tax of HUF 3 billion, which the taxpayer concerned may challenge by submitting contrary evidence within a statutory deadline of 30 days.

Changes affecting the special tax on financial institutions

From 1 January 2017, the special tax on credit institutions and financial enterprises must be calculated from the tax base for the second tax year preceding the current tax year, rather than from the 2009 tax base. For credit institutions, the tax rate has been reduced to 0.15% on the part of the tax base not exceeding HUF 50 billion, and to 0.21% on the part exceeding HUF 50 billion.

Changes concerning the financial transaction tax

From 1 January 2017, the tax on financial transactions is also payable by financial institutions that engage in the granting and negotiation of credit and cash loans, but do not qualify as payment services providers. The tax base will be the amount paid in cash to the financial institution engaging in the granting and negotiation of credit and cash loans; the tax rate will be 0.3%.

Changes related to the public health product tax

According to the amendments, effective from 1 January 2017, Act CIII of 2011 on the Public Health Product Tax has been amended as follows:

Changes to definitions

The definitions for "additive" and "herb" have been clarified in order to make the tax classification of such products easier; exceptions include herbal extracts as specified by Community legislation. New definitions have also been added for "raw dairy materials", "sweetener" and "herbal beverage".

The amendments redefine "health promotion scheme" to include activities made available to private individuals for a fee of up to HUF 500 (the current definition only includes health promotion schemes available free of charge).

Changes related to taxable goods

The definition of "flavoured beer" has been extended to include beverages sweetened in whole or in part with sweeteners of a specified quantity. The sweetener content must be determined on the basis of how much sugar it replaces.

The definition for "alcopops" has also changed: like flavoured beers, alcopops sweetened in whole or in part with sweeteners of a specified quantity now also qualify as taxable. Alcopops containing additives are also taxable, irrespective of how much soft drink they contain. According to the amendments, alcopops may not contain more than 5% alcohol by volume.

Among alcoholic beverages, fruit spirits and herbal drinks will continue to be tax exempt. However, the requirements for herbal drinks are now more stringent: only those drinks are tax exempt that contain no additives, are made from at least seven different herbs (excluding flavoured vodka), and contain more than 3 g per 100 ml of herbs (or herbal extracts with an equivalent amount of active substances), and contain at least 0.2 g per 100 ml of each herb of the seven different herbs (or herbal extracts with an equivalent amount of active substances), with the proviso that the herb content must be taken into account converted to herb content with 15% moisture content, and that the dominant flavour and scent of the drink should be that of the herbs used.

Changes related to excise duty and the energy tax

The most important element related to excise duty is that the basic provisions of Act LXVIII of 2016 on Excise Duty ("new Excise Duty Act") will enter into force on 1 April instead of 1 January 2017. The current regulations on excise duty and the energy tax will also be repealed from that date.

However, Act CXXVII of 2003 on Excise Duties and Special Regulations on the Distribution of Excise Goods has been amended in such a manner that several provisions of the new Excise Duty Act on tobacco products will already be applicable from 1 January 2017. In line with the above, the following rules will apply to tobacco products from 1 January 2017:

The following will also qualify as tobacco products: products other than cigarettes, cigars, cigarillos, smoking tobacco or refill liquids, that are defined as tobacco products by the Act on the Protection of Non-Smokers and Certain Regulations on the Consumption and Distribution of Tobacco Products, i.e. all consumables that are, even partly, made of tobacco ("new tobacco product categories"), as well as refill liquids for electronic cigarettes.

The excise duty for tobacco products has increased. The duty rates for each new product category have also been specified:

- For cigarettes, the previous excise duty was HUF 15,700 per 1,000 cigarettes plus 25% of the retail selling price, but not less than HUF 28,400 per 1,000 cigarettes. This has increased to HUF 16,200 per 1,000 cigarettes plus 25% of the retail selling price, but not less than HUF 28,800 per 1,000 cigarettes.
- For cigars and cigarillos, the previous duty rate was 14% of the retail price, but not less than HUF 4,060 per 1,000 pieces. This has increased to 14% of the retail price, but not less than HUF 4,120 per 1,000 cigars or cigarillos.
- For fine-cut tobacco and other smoking tobaccos, the excise duty has increased to HUF 16,200 per kilogram from the previous HUF 15,100 per kilogram;
- For refill liquids, the excise duty will be HUF 55 per millilitre.
- For consumables belonging to the new tobacco product categories that contain tobacco or are consumed with tobacco, the excise duty has been set at
  - HUF 10 per unit for disposable products, and
  - HUF 70 per millilitre for liquids.

The excise duty and VAT on tobacco products will have to be paid in accordance with the general rules, and not at the time the tax stamps are received. Consequently, tax stamps do not correspond to the amount of excise duty and VAT, but rather they are valued at HUF 1,500 (this amount will have to be paid for each tax stamp the taxpayer cannot account for).

The regulations also set out the record keeping and reporting obligations for holders of excise authorisations in connection with the new Excise Duty Act. For example, warehouse operators wishing to continue their activities from 1 April 2017 will have to submit a statement to that effect to the tax authority by 28 February 2017.

From 1 January 2017, Act LXXXVIII of 2003 on Energy Taxes specifies the duty rate for natural gas in kWh (HUF 0.3038 per kWh) instead of gigajoule.

Changes to the duties applicable to excise goods

On 1 September 2016, the excise duty on fuel oil, petrol and kerosene was adjusted to reflect global oil prices. Depending on the price of crude oil on the world market, the duty on petrol and kerosene may increase or decrease by HUF 5 per litre, and the duty on fuel oil may increase or decrease by HUF 10 per litre.

Changes related to tax refunds

With the changing excise duty on fuel oil, the amount of excise duty that can be reclaimed on commercial fuel oil has also changed. Depending on the threshold set on the basis of global oil prices, the excise duty that can be reclaimed may be HUF 7 or HUF 17 per litre.

The amount of excise duty that can be reclaimed has also changed for fuel oil used in agriculture: depending on the threshold set on the basis of global oil prices, agricultural producers may reclaim 82% or 83.5% of the excise duty levied on the fuel oil they have used.

Changes related to accounting

Hedging and derivative transactions

The act includes several new definitions for hedging and derivative transactions, and hedge accounting, with some earlier definitions formulated more precisely.

According to the amended rules, derivative transactions may be linked to the prices of any financial instruments, and will no longer be restricted to the prices of securities or investments. In addition, the notion of fair value has been expanded to comprise intrinsic value, defined as the difference between the current market price (fair value) of the asset underlying the transaction and the value of the asset calculated at strike price.

The amendments provide a more precise definition for hedge effectiveness, and set the conditions under which a hedging transaction is likely to be effective.

As regards changes in hedging and derivative transactions, the amended act specifies in which cases it is required to account prepayments and accruals for derivative transactions.

Concerning fair valuation, the amended legislation stipulates more clearly that derivative transactions for trading purposes and for hedging purposes must be measured either at fair value or at intrinsic value. Accordingly, fair valuation may not be applied to forward delivery transactions and option transactions for goods that do not qualify as derivative transactions. In addition, the closing of forward and option transactions that do not qualify as derivative transactions will continue to be accounted according to the rules applicable to spot purchase and sale.

Depreciation of goodwill

The rule concerning the depreciation of goodwill changed again as of 16 June 2016. According to a previous provision of the Accounting Act, companies were allowed to decide whether they (i) write down goodwill in not less than five, and not more than ten years if the useful life could not be estimated, or (ii) continue to apply the depreciation rules that were in effect when goodwill was recorded. Under the amended regulations, depreciating goodwill will be obligatory from the financial year 2017.

The transitional rules stipulate that, for goodwill generated before the financial year 2016, companies have only an option to account depreciation for the financial year 2016, and are required to account depreciation from the financial year 2017 regardless of whether goodwill was recognised before or after the financial year 2016. Companies must determine the useful life of goodwill. Should this not be possible, they must apply a period of not less than five and not more than ten years (based on their decision), as stated above.

Subsidies and benefits received

Under the amendments, in addition to the repayable amount of subsidies for development purposes received in the previous financial year(s) and accounted as revenues, the repayable amount of subsidies and benefits received as compensation for costs (expenses) must also be accounted as “other expenses”.

Changes concerning corporate tax in connection with the transition to IFRS

Tax base adjustment due to the transition to IFRS and treatment of tangible and intangible assets

Taxpayers may have differing tax bases as a result of the transition to IFRS due to the difference of the accounting standards. To make the IFRS transition neutral, a transition-related tax base adjustment may be necessary. Previously, tax base adjusting items were based on differences in the amount of equity calculated under the different accounting standards, attributable to differences in balance sheet line items, i.e. the differences in accounting values served as a basis for determining whether and by which amount the tax base increased or decreased. As opposed to the previous practice, the new regulation focuses on the difference between the tax bases in the tax years following the transition, i.e. the differences between the values of assets and liabilities that can be taken into account for tax purposes. This amendment provides for, among other things, the tax treatment of tangible and intangible assets at the date of transition. From 2017, taxpayers will have to observe the IFRS requirements and take into account the cost carried on the first day of the tax year in which the transition takes place when calculating the depreciation allowable under the Corporate Tax Act. An exception to this rule may apply to tangible assets carried at deemed cost according to IFRS 1, for which taxpayers may choose either to

determine cost and tax value on the first day of the tax year in which the transition takes place to be identical with the book value or base the depreciation allowable under the Corporate Tax Act on a special extrapolation base.

Special option concerning the treatment of the transition to IFRS

Under the new legislation, taxpayers will have a choice in connection with the transition to IFRS. Taxpayers will be allowed to decide whether they will calculate their tax bases after the transition based on the entirety of their assets and liabilities, or only on their tangible and intangible assets as if they had not changed to IFRS. If taxpayers take advantage of any of these choices, the tax base will not need to be adjusted at the date of transition for the assets and liabilities concerned, and separate records will need to be kept on these assets and liabilities. Taxpayers that take this option will be required to take into account the cost and tax value calculated in accordance with previous accounting regulations when determining the amount of depreciation allowable under the Corporate Tax Act.

Tax base adjustment due to retrospective application of the accounting policy

Taxpayers are required to adjust their tax bases if changes in the accounting policy are applied retrospectively. Regulations concerning the obligation to adjust the tax base are in line with the tax base adjustment required due to the transition to IFRS, i.e. the tax base adjustment must be based on the difference between the tax bases, meaning that the tax base following the change must be compared to the tax base calculated if the accounting policy remains unchanged.

Jointly controlled operation

The previous regulations did not contain any provisions on the tax treatment of jointly controlled operation under IFRS 11, therefore, the tax base of jointly controlled operations would have been taken into consideration twice: 1) as the tax base of the entity performing the operation, and 2) in the tax bases of taxpayers exercising control, as calculated in the separate IFRS financial statements. Under the amended regulation, taxpayers exercising control will be required to recognise these operations in their tax bases as if they kept their records in accordance with the Accounting Act.

Equity-settled share-based payments

As of 2017, there are clear rules for considering share-based payments provided in equity instruments settled by means of repurchased treasury shares in the tax base. The amended act also contains supplementary provisions on tax base adjusting items related to share option schemes provided through ESOP trusts.

Regulations for termination without a legal successor

Similar to previous regulations, tax base adjusting items will become due as a single amount when a taxpayer that has adopted IFRS enters voluntary liquidation or liquidation. From 2017, exclusion from the scope of the Corporate Tax Act, with the exception of transfer of the registered office of a European Company and a European Cooperative Society to abroad, will have similar consequences.

Reduction of subscribed capital by means of divestiture

From 2017, taxpayers will be allowed to determine the tax impact of the reduction of subscribed capital by means of divestiture in accordance with the provisions of the Accounting Act also in cases in which the transaction is accounted other than as a derecognition of shareholdings (e.g. dividends) under IFRS.

Minimum tax and tax advance minimum

In regard to the reduction of the tax rate to 9%, taxpayers must determine their minimum tax and tax advance minimum liabilities by taking into account the tax payable for the tax year that precedes the tax year in which the transition takes place and that serves as the basis for comparison, using the tax rate as stipulated by the provisions in effect on the first day of the tax year in which the transition takes place. Accordingly, taxpayers that adopt IFRS as of 1 January 2017 are required to apply the 9% tax rate when determining the amount of minimum tax and tax advance minimum.

Transitional provisions

Under the newly introduced transitional provisions, taxpayers will be allowed to choose to apply the rules for jointly controlled operations and the cost and tax value of tangible and intangible assets already when calculating their tax bases for 2016.

Changes concerning local business tax in connection with the transition to IFRS

Changes regarding the transition to IFRS

From 2017, taxpayers adopting IFRS will be required to take into account their net sales revenues from continuing and discontinued operations, cost of goods sold, intermediary services, and raw material expenses when calculating their tax bases. However, taxpayers will have to calculate their tax bases for activities performed based on a joint arrangement under IFRS 11 as if they recognised them in accordance with the Accounting Act, i.e. net sales revenues from these activities, cost of goods sold, intermediary services and raw material expenses should not be regarded as part of the tax base.

Net sales revenue

The statutory amendment effective from 1 January 2017 has brought changes also in connection with adjustments to sales revenues as the wording for tax base adjusting items related to subsequently provided uninvoiced contractual discount (payable), and revenues from the supply of goods and services as part of extraordinary business activities has been formulated more precisely. Under the amended regulations, sales revenues from the extraction of mineral ores, and insurers' revenues from insurance contracts specified in IFRS 4 Insurance Contracts will also increase net sales revenues.

Cost of goods sold and raw material expenses

Similar to net sales revenues, the contractual amount of subsequently received (due) uninvoiced discount will change the value of cost of goods sold and raw material expenses. According to a further clarification, the cost of goods sold must be increased by the value of inventories received in exchange as determined in the exchange contract, rather than their book value. It has been introduced as a new element that the cost of goods sold and raw material expenses must be adjusted by the amount by which the hedge transaction modifies (increases or decreases) the acquisition cost of inventories.

Self-revision

From 2017, if, for a tax year prior to the transition, taxpayers correct accounting errors that must be treated differently under IFRS and the Accounting Act, the error limit must be taken into consideration in the tax base of the tax year in which the error is detected, without adjusting the difference attributable to the transition.

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