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wts klient newsletter

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The Bridge.

Dear Readers,

Those of you who have been following recently what needs to be clarified at the outset in connection with an employee coming from abroad will be delighted to see this week's video on the legal aspects of this topic.
Should the original employment contract remain in force, or should we assign it a "dormant" status for the duration of the work abroad? It is important to know that even though we do not have to conclude an employment contract subject to Hungarian labour law for our foreign employee, we still have to comply with the minimum requirements of the Labour Code. You can find more details here.
This week's professional content covers the EKAER system, which has been a focal point in Hungarian economic life for many years now, and related experiences. This topic is relevant not only for Hungarian experts, but also for Austrian investors. My tax consultant colleague, Tamás Gyányi, will be holding a presentation on this topic on Wednesday, 27 September, at the Hungarian Embassy in Vienna. If you have time you are more than welcome to attend the event, and you can find more information here.

Dr. Petra Eszter Deli

EKAER number – the wound that never heals

Although the Hungarian authorities say that the EKAER is a huge success story, our experience shows that the system has its downsides as well.
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Penalties imposed in relation to an EKAER number should be differentiated and subsequent corrections should be allowed for reliable taxpayers.
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EKAER number – the wound that never heals

Possible reasons for EKAER default penalties:

- incomplete reports, or reports with mistakes or false data
- failure to request an EKAER number
- more than a 10% difference between the reported weight of the product and the actual weight
- incorrect licence plate number or other data

Author: **Tamás Gyányi**
tamas.gyanyi@wtsklient.hu

"The introduction of the EKAER has been a success story, and our neighbouring countries would like to "import" the system." According to the authorities, the system is good and has achieved its goal. Those who use the system and taxpayers making mistakes in the system might have a different opinion though. It must be said, the **EKAER has its downsides**. The greater administrative burden and therefore the increasing wage costs are only part of the negative effects. As tax consultants we meet more and more taxpayers on a daily basis who suffer from these consequences.

What are the implications of the EKAER system?

According to the Commission staff working document "Country Report Hungary 2017", the introduction of the EKAER (Electric Road Cargo Monitoring System) has created **administrative burdens as regards** "intra-EU trade". As stated in the Country Report "This highlights the trade-off between tax collection efficiency and compliance costs". And what about penalties in addition to compliance costs?

The **default penalty** related to the system can amount to 40% of the value of the goods transported without an EKAER number (in the case of such transport, the origin of the goods is considered unverified by the Hungarian Tax Authority (NAV), even if the waybill explicitly shows the sender and the origin of the goods). Taxpayers providing reports that are incomplete or include mistakes or false data can expect this type of fine. NAV can also impose a fine if you forget to request an EKAER number, or if there is more than a 10% difference between the reported weight of the product and the actual weight. You can expect a fine if your logistics colleague is tired and makes a mistake, and writes the letter Y instead of a V in the licence plate number.

Do not think you can relax at weekends either. A default penalty can rear its head if the closing of the EKAER number falls on a weekend, and your colleagues are unable to do so. There was one case when inspectors performing a tax inspection wanted to impose a fine because the name of a foreign city was incorrect. Only after our comments submitted to the report did they accept our explanation that the words Cologne and Köln, which is the Hungarian name of the city, mean the same place, and a city name given in another language should not constitute a valid legal reason to impose a default penalty. In addition to a penalty, **the goods can also be seized**, which in the case of a production process with tight deadlines may cause further problems, including production losses.

Penalties that are excessive or violate legal certainty

Although the sanctions are called default penalties by the legislator, we think that the sanctions imposed on the value of the goods are more than that. The aim of the very high penalty is to ward off tax fraudsters. However, **tax fraudsters are difficult to catch and the most difficult task is collecting any amount from them at all**. The maximum penalty imposed in the event of concealed revenues – at the moment totalling 200% – is planned to be amended soon in the new Act on Rules of Taxation and be reduced to 100%. Why? According to the law, the penalty amount should be reduced because it is very difficult to collect even the amount of the tax, not to mention the penalty. We would be happy to hear about a similar modification for the EKAER as well, although there would surely be taxpayers saying that when transporting goods amounting to hundreds of thousands euros, it makes no difference whether the maximum penalty rate is 40% or 20% of the value of the goods, because the company would probably close down anyway, no matter which amount is imposed.

We believe **the penalty of up to 40% of the value of goods of unverified origin, or of unreported goods, is excessive**, and **it is higher than the amount necessary to achieve the goal of the regulation** (i.e. being able to track the path of the goods). The discretion available to the tax authority in setting the penalty from 0% to 40% is also too wide, **which impairs legal certainty**. We should note here that it is important to clarify in the legislative text whether the net or the gross value of the unverified goods is the basis of the fine. For example, let us assume a net value of unverified goods of HUF 1,000,000 (approx. EUR 3,300). If the fine is imposed based on the net value, the amount of the fine can total up to HUF 400,000 (approx. EUR 1,300), while if 27% VAT is included in the amount used to calculate the fine, the basis rises to HUF 1,270,000 (approx. EUR 4,200) and the fine itself can exceed HUF 500,000 (approx. EUR 1,600).

What happens in practice?

We find it quite strange that **the maximum amount of the penalty is more than the VAT in the goods' value** (in case of carousel frauds, the high VAT rate (27%) is what motivates tax evasion). If the inspectors assume there has been no deliberate tax fraud based on the behaviour of the taxpayer and the documents examined, the maximum default penalty is unlikely to be imposed. In our experience, the 40% penalty has never been set, and in most cases the amount of the penalty is around HUF 100,000 (approx. EUR 330) per case/inspection.

This is enabled by the Act on Rules of Taxation because the **tax authority can weigh up all the circumstances in each case**, and when setting the default penalty it considers the severity and frequency of the unlawful conduct (activity or omission) of the taxpayer and whether the taxpayer or its representative acted with due care appropriate to the particular situation. Although we have not seen any significant EKAER fines so far, it can be really annoying if the tax authority imposes a fine equal to the salary of the logistics colleague over several months, or for a small company, a penalty that swallows the funds for salary increases planned for the following year.

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"If the tax residence of foreign workers cannot be determined unambiguously based on a permanent address, the next step is to examine which country the person's centre of vital interests is in."

Zoltán Cseri, WTS Klient Hungary manager

Source: inforadio.hu

Turn on your radio!

"When examining the income tax payment obligations of foreign workers in Hungary, the first step is to define their tax residence. To this end we have to examine the Hungarian regulations, but generally the provisions of the convention for the avoidance of double taxation concluded with the country concerned and overriding national law will be more helpful" – says Zoltán Cseri, manager of WTS Klient Hungary who will give an interview about the topic to InfoRadio on the evening of 21 September.

Listen to the conversation at this link!

Please note that the conversation is available only in Hungarian.

Who pays the penalty?

The tax authority identified some kind of problem in almost all of the EKAER audits we are aware of. At first it may seem obvious who has to pay the default penalty, but **there are cases where the party reporting the goods and the beneficial owner are not one and the same**.

The EKAER reporting obligation applies to Hungarian companies doing contract work – who are not the beneficial owners of the goods – on the grounds of "other intra-EU imports", and they also need to request an EKAER number as recipients of the goods. As a result, they risk receiving a fine which is often disproportionate to the value of the contract work performed (the value of the goods which these companies work on can be several times the value of the service completed).

Another legal consequence is that the NAV can seize the goods. This sanction affects the beneficial owner, who does not even have to report anything (so evidently there are several strands to follow in deciding which company is obliged to report the transportation and which company takes the penalty). It is difficult to imagine how the constitutionality and proportionality of a penalty can be justified if it is imposed on companies subject to the reporting obligation but which are not the owner of the goods, while the penalty is based on the assumption that these companies possess goods of unverified origin. Based on the above, we made a recommendation to the Ministry for National Economy that the default penalty rules be reconsidered, taking into account the cases where ownership of the product is not transferred to the taxpayers subject to reporting obligations for the transportation, contract work or import for other purposes. **The system should differentiate between penalties as to whether the owner of the unreported goods or another person (e.g. contract-work entity) is obliged to make the report**.

Lack of subsequent corrections and possibility to make subsequent amendments

For companies transporting large consignments and on a regular basis, it can easily happen that the EKAER number is not requested because of an administrative error, or that the data submitted is incorrect. It makes no difference if logistics companies are entrusted with this, both they or the programmes used for bulk data uploading can make mistakes. However, there is no option to subsequently file EKAER reports or correct them after 15 days. **Why is there no option to make subsequent modifications, almost as a self-revision, for issues related to an EKAER number**? We know the tax authority's answer to this: the system could subsequently be circumvented in this case.

However, it can also happen that the company itself identifies a shortcoming during an internal audit years later (while there was no real-time roadside check regarding the shipments in question). In these cases though, there is no option to subsequently request an EKAER number without receiving a fine, because the transportation could only have been completed with a valid EKAER number, so the only option for voluntary compliance is "to report ourselves" to the tax authority. Consequently we think the possibility to request an EKAER number subsequently and the method for doing so are missing from the regulation. Such modifications are justified because deciding whether a transportation needs an EKAER number or not requires great care in certain cases – or even a professional to help make the decision – and if so, then who should request the number. Chain transactions are a good example here. For instance, a foreign end-client takes over the goods at the site of the Hungarian seller, and the transportation is arranged by the foreign end-client (who does not have a Hungarian tax number). In this case, by law, the EKAER number must be requested by the foreign intermediary buyer (who has to ask for a Hungarian tax number too), even though this company is not involved in the transportation.

Furthermore, due to the closed system, if a company has already requested an EKAER number, but it turns out that the data provided (license plate number, weight of the product, etc.) was incorrect, there is no option to make subsequent corrections after 15 days.

For this reason we have mentioned several times that **reliable taxpayers should be allowed to subsequently modify data**. How nice it would be if legislators agreed with such recommendations, and next year we would be able to read the following regulation in the Act on Rules of Taxation.

"If a taxpayer subject to the reporting obligation is considered a reliable taxpayer according to Section 6/A of the Act on Rules of Taxation, the reporting can be completed or modified on the EKAER electronic platform within 5 years of the last day of the calendar year when the taxpayer should have requested an EKAER number."

Possible solutions

EKAER – suggested modifications:

- lowering and differentiating the sanction rate
- reduced, specific penalties instead of percentage penalties for "good" taxpayers
- if there is no immediate inspection or NAV inspection from an EKAER perspective, it should not be possible to impose penalties from one year after the transaction
- subsequent corrections should be possible for reliable taxpayers

To summarise the anomalies above, as tax consultants we would be happy to see the following changes:

- **Lowering and differentiating the sanction rate**. A penalty that can total up to 40% of the value of the goods transported is disproportionate to the set objective, and especially unfair in cases where the owner of the goods and the person obliged to report to the EKAER system are not one and the same.
- We should consider introducing a **reduced, specific penalty instead of a percentage penalty** for "good" taxpayers, even on a tax-performance basis. The 40% fine should not be imposed on mistakes that were made without the intention of avoiding tax.
- We would gladly accept a system that understands the fact that the EKAER is a tool for immediate checks. Accordingly, we suggest, for example, that if there is no immediate inspection and the NAV has not examined the reliable taxpayer from an EKAER perspective either, then **no sanctions should be able to be imposed from one year after the transaction** (especially because the "self-revision" option is not available).
- **Making subsequent corrections** should be permissible for **reliable taxpayers**.

We would like to highlight that as tax consultants we are aware the NAV weighs up all the circumstances based on the provisions of the Act on Rules of Taxation when imposing penalties. However, during repeated inspections, the tax authority can cause significant losses not just to small companies in the case of successive mistakes that cannot be corrected – the EKAER penalty system can cause unpleasant surprises even for large taxpayers too (losing their reliable taxpayer status for example).

This newsletter is special because we would like to call upon our readers to let us know what other modifications they would like to see in the EKAER system. Moving on from penalties and subsequent self-revisions, we welcome any suggestion to make the lives of system users and taxpayers easier. Although we cannot expect the system to become "more flexible" in the near future, we hope that based on the feedback the legislator receives about the problems, some steps will be taken to favour trustworthy taxpayers reporting and paying their taxes in a reliable manner, and to make a distinction regarding penalties between taxpayers intentionally submitting incorrect reports and those making administrative mistakes.

Do you have any opinion or suggestion? Please write to us: info@wtsklient.hu

This WTS information does not constitute advice and it serves only to provide general information about selected topics.

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Should you have any questions regarding the above or any other professional issues, please do not hesitate to get in touch with your WTS advisor or use any of the contact details below.

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WTS Klient Hungary
1143 Budapest • Stefánia út 101-103. • Hungary
Telephone: +36 1 887 3700 • Fax: +36 1 887 3799
info@wtsklient.hu • www.wtsklient.hu