

## wts klient newsletter

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The Bridge.

Dear Readers,

In today's fast-moving world, more and more people are looking for stability in their lives to give them some kind of security. We are clearly not as likely nowadays to sit down in our favourite armchair to read a book, while the Hungarian Post Office also knows that it can no longer expect to base its business plan on delivering handwritten letters. Nevertheless, we also need some permanency in this digital world. If we don't want our smartphones taking complete control of our lives, it is worthwhile limiting the reading of emails and the use of social media to some extent, and adjusting our daily routines accordingly. With the now weekly publication of **our professional newsletter** we also want to try and give you back some stability in your life. So find a free half-hour every Friday afternoon or some other time during the weekend! From now on, we will send you the latest issue of our newsletter **on Fridays at noon**.

At work, in a café, or at home in your armchair; using your computer, your smartphone or a printed version – the choice is yours. We hope you will enjoy reading it!

Zoltán Lambert  
Managing Partner**VAT-registered taxpayer**

From 1 January 2016, the term VAT-registered taxpayer was finally included in the Act on the Rules of Taxation. We look at what it means in practice. » [page 1](#)

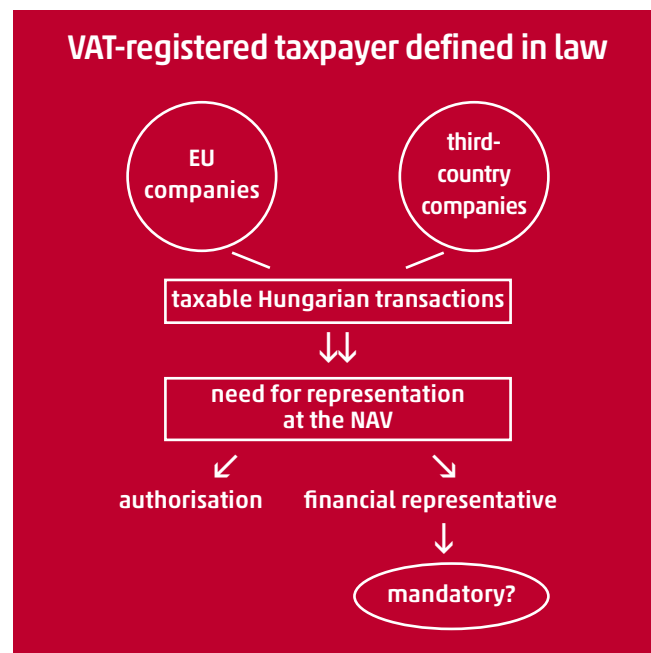
**Transfer pricing rules**

The issue of transfer pricing rules arises when two or more companies qualify as related parties and they conclude transactions with each other. » [page 2](#)

**Group reports**

While subsidiaries keep their books according to local laws, group reports are prepared according to the parent company's accounting policies. » [page 3](#)

## VAT-registered taxpayers now also defined in law: how can they interact with the NAV?

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Although VAT-registered companies have been a focal point for the NAV and the advisory profession for a long time, legal regulations have essentially neglected to define them, until recently; from 1 January 2016, the term "VAT-registered taxpayer" was finally included in the Act on the Rules of Taxation. In the first part of our series of articles on financial representation, we look at what this means in practice.

In professional circles we see more and more foreign and EU

companies as well as corporations outside the EU come into contact with Hungary in some way through **taxable product supplies or providing services** in the country.

**Legal definition**

Although the term did not used to be part of substantive law, the NAV did have guidelines on procedures for the tax inspections of all VAT-registered taxpayers, and it has updated these from 2017. The law defines the **status of VAT-registered taxpayers** as a company not liable to set up in the country for economic purposes, but is obliged to pay taxes in Hungary due to an activity that is taxable. It also means that these types of companies usually have neither the human resources nor the physical presence to perform economic activities (though this does not rule them out from keeping inventories at the warehouse of a logistic service provider).

## The issue of domestic tax liabilities

Foreign companies compelled to register in Hungary in this way will typically become VAT taxpayers. Although the EKAER and the environmental product fee are not discussed in this series of articles, these are the two other typical issues in respect of which a tax liability and tax payment obligation may arise – failing to fulfil them may result in the usual legal sanctions in the case of VAT-registered companies.

## Who can represent these companies at the NAV?

The question may be asked as to who helps these foreign companies in communicating with the tax authority; who can represent VAT-registered companies at the NAV in various official matters? According to the Act on the Rules of Taxation, during relevant procedures at the tax authority the taxpayer **may authorise** a tax advisor, tax expert, chartered tax expert or an employee of a company authorised to provide tax advisory and accounting services; and the taxpayer has to report any permanent authorisations to the tax authority.

## Financial representative

A foreign company that is not obliged to set up in Hungary for economic purposes in connection with its domestic business activity can engage a **financial representative** to fulfil any tax obligations. The rules on this will be described in detail in the following articles. What is important to note at the outset though is that a Hungarian business entity assumes a huge task with the status of financial representative; it has to comply with strict legal requirements (e.g. **joint and several liability** with the foreign company for its tax liability).

## Is it mandatory to engage a financial representative?

Although the Act on the Rules of Taxation generally lists for foreign companies only as a possibility to engage a financial representative, in certain cases this is unavoidable: if the company obliged to pay taxes is not in the EU, i.e. it has its registered office or economic establishment in a **third country**, there is no other legal way to represent the foreign company – with all of the complexity this involves. More details on this will be provided in a later article.

## The basics of Hungarian transfer pricing rules

### Transfer pricing rules

#### When can transfer pricing come into play?

- for transactions between related parties

#### What does a “related party” mean?

- direct or indirect majority interest
- permanent establishments
- overlap in management positions

#### What is a “majority interest”?

- votes > 50% of the total votes or a controlling influence

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Even at the beginning of the year we can almost take for granted that transfer pricing rules will be a key topic in the lives of Hungarian companies in 2017. Issues affecting transfer prices are continually changing, even globally: multinational companies are constantly searching for pricing solutions that are welcomed by the experts of the local tax authorities of the given member states.

Without a detailed review of the legislative environment it is difficult to understand and interpret what these rules apply to exactly, and what should be considered. By answering some basic questions, this article provides some assistance regarding transfer pricing rules.

#### When can transfer pricing rules come into play?

In many cases it is not clear whether we are dealing with a transaction where the issue of transfer pricing arises at all. When two

or more companies qualify as **related parties** and they conclude transactions, we need to review the development of transfer prices between them.

**Important!** Local transfer pricing rules exempt taxpayers from preparing transfer pricing documentation in many cases (e.g. based on the size of the enterprise or due to the low value of the transaction). However, this only means that the taxpayer does not have to prepare such documentation. Nevertheless, related party transactions have to be concluded at arm's length price in order to avoid any tax base corrections at the end of the year at the latest.

### What does a "related party" mean?

If we review a transaction for the purposes of corporate tax, the relevant definition will be found in the Act on Corporate Tax. Based on this, the following qualify as related parties:

- » enterprises which have a (direct or indirect) **majority interest** in each other, or a third party that has such an interest in them; or
- » a foreign company and its domestic permanent establishment(s) or the domestic establishment(s) and the persons where the issue of majority interests arises; or
- » a domestic company and its foreign permanent establishment(s) or the foreign establishment(s) and the persons where the issue of majority interests arises; or
- » the taxpayer and other persons if there is controlling influence over business and financial policy between the companies based on overlaps in the respective management teams.

**Tip!** Draw a simple chart of a company group in order to specify the companies that qualify related parties.

### What does a "majority interest" mean?

The term "majority interest" is defined in the Civil Code. In a nutshell, this is when an individual or a legal entity has more than half of the voting rights or a controlling interest in a legal entity. Consequently, they have decision-making authority or can appoint or remove the persons who make the decisions.

**Important!** The direct or indirect ownership shares or voting rights of close relatives have to be counted together.

Based on the above it is easy to identify related party transactions, and the ones where pricing has to be reviewed can be designated.

## Challenges when preparing group reports

### Preparation of group reports:

- Closing the books based on **own valuation principles**
- Identifying adjustments based on **parent company's accounting policies**
- Defining and substantiating **amounts of adjustments**
- Compiling **group report**
- **Auditor's opinion as required**

To achieve this, subsidiaries have to take the valuation rules prescribed by the accounting policies of their parent companies into consideration when preparing their reports.

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A good number of consolidated enterprises closed their previous financial years as of the end of January, and the annual group reports were prepared at the same time. The data of these reports and Hungarian statutory reports may differ, while their preparation deadline may not be the same either.

### The parent company is in control

Preparing reports containing data of group companies and carrying out the consolidation are the responsibility of the parent companies. This process is conducted according to predefined valuation principles and schedules so that the information is made available to the owners for decision-making at the right time. Group reports have to contain data established based on **uniform valuation procedures**.

Regardless of this, subsidiaries naturally keep their books and assess their taxes according to local laws. The difficulty here is that in order to **comply with group requirements**, they have to make changes that are usually implemented outside their bookkeeping system. Thus tracking these adjustments from previous years poses a serious challenge every year. One solution is to keep the differences in account class "zero", thus the data underlying both the local and the group reports is available in the bookkeeping system. Group reports are prepared for owners; their deadlines are set in advance and must be strictly complied with.

### Data content of group reports varies

Group reports always include a balance sheet and an income statement, while the number of detailed data items changes depending on **the data requirements of the owners**. The reports definitely contain information on equity and any changes thereto. Other important elements include the company's tangible assets as well as the volume of investments completed during the year. Experience shows that the extent of tangible asset depreciation required by the parent company deviates in many cases from the depreciation recorded based on local laws. So this is generally one of the differences that frequently crops up during group reporting.

The same is true for the impairment of receivables. The parent company's accounting policies generally include a rule for the lump-sum accounting of impairment, while according to Hungarian rules, only impairment calculated based on individual valuations is accepted. The profitability of the various business lines also constitutes important information, so this can form part of the group report too if it is relevant for the given company. Using the pre-tax profit established based on standard principles, **deferred (latent) tax** is calculated, and the calculation breakdown can be included in the report as well.

### Different forms

The **form** of group reports **may vary depending on the given group**. It can also happen that a parent company does not require a so-called reporting package, but simply aggregates the subsidiary's data as booked in its own accounting system and then performs the consolidation. That said, it is more common to consolidate the data of the reports prepared by the subsidiaries, and to this end, group reports have to be prepared.

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Services of the WTS Klient:

- » Tax consulting
- » Consulting
- » Legal consulting
- » Accounting
- » Payroll

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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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