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The be all and end all of taxation policy: predictability

Even the lowest tax rates are not enough for investors if past experience shows that tax laws are continuously amended. » page 1

Lubricating oil and excise tax: what is this about?

Those who trade in lubricating oil products subject to excise tax have to hold a NAV permit to start their activity. » page 3

Dear Readers,

To close our series we will explain the application of social security rules and regulations regarding foreign employees in Hungary.
We will discuss the fact that foreign employees may only have social security in one Member State, which can be verified with an A1 form within European Union countries. This document also shows how long posted employees are subject to the social security rules of the country they came from. With regard to non-EU countries, certificates issued pursuant to bilateral social security agreements are acceptable. You can find more details here.
This week, the first article of our newsletter examines the predictable nature of Hungarian taxation policy; our piece on excise tax provides additional information on the provisions of the new Act on Excise Tax effective from 1 July 2017.
I hope that our video series and the articles will help you in your work during the autumn months.

Marianna Fodor
payroll services – director

The be all and end all of taxation policy: predictability

> **"According to the main decision-makers of large companies, the reliability and predictability of the tax system and taxation policy is more important than the tax rate itself."**

Author: **Zoltán Lambert**
zoltan.lambert@wtsklient.hu

Hungary is a very popular destination in Europe for investments. Its geographical location in the middle of Central Europe is a valuable asset for the country. This benefit combined with advanced infrastructure creates optimal conditions for new investments. Proximity to customers, and low transportation costs and short deadlines as a result, provide an advantage for Hungary in becoming a popular destination for investments in the region. While transport is certainly becoming faster and faster in the region nowadays, we are also seeing fiercer competition. Our neighbouring countries of Slovakia, Romania and also the Czech Republic and Poland are Hungary's rivals in the race for new investments. Taxes play a key role in this competition. **The good taxation policy is the main reason for Hungary attracting a substantial part of investments in the region**.

If Hungary can play a key role in Central and Eastern Europe, investments implemented in the country can take a new direction. The government has also recognised that the activities of plants previously focused on serving central requirements can be complemented with key functions (e.g. research and development), which enable these units to pursue **independent and comprehensive economic activities** and have more freedom as market players in terms of business opportunities, and obviously risks of course. This entails an increasing need for highly qualified professionals (engineers, financial experts). The **expansion of work with higher added value** has become a key aspect of the current labour market conditions.

Role of taxation policy

To achieve a central role, however, we always need to **monitor the development of our neighbouring countries**. "Monitoring" the markets in the region can ensure that Hungary is able to secure the best position it can. Poland, for example, is a really successful competitor. With its special economic zones and highly qualified but not expensive labour force, Poland is a very attractive investment destination. Hungary must withstand the competition in all respects.

What we see is that investors consider a number of factors when making new investment decisions. Tax benefits are not enough for the Hungarian government to achieve its goal of attracting large investors. However, if an investment is implemented in this economic zone, taxation policy and taxes themselves play a key role in the selection of the target country.

The most important factor when making investment decisions is long-term predictability

During my 25 years as a consultant I have not had any meeting with any decision-makers of large companies where long-term predictability was not mentioned as a prime factor. Even financial managers and tax directors, whose main task nowadays is to reduce the so called "effective tax rate" of the corporation, unanimously confirmed that **a reliable tax system and predictable taxation policy are more important than the tax rate itself**.

Unfortunately, this opinion puts the advantages of Hungary's 9% corporate tax rate into context. Of course, Hungary cannot apply tax rates, that are higher than the regional average, but even the lowest tax rates are not enough for investors if past experience shows that tax laws are continuously amended. This can negatively affect the launch of large investments that only have long-term returns. In terms of the reliability of taxation policy in Hungary, the continuous changes in tax laws over recent years mean the disadvantage Hungary faces here is not negligible.

Past experience

Without aiming to give an exhaustive summary, the following list reveals examples of inconsistent changes:

- decreasing the value added tax rate, then increasing it twice;
- introducing special taxes, then abolishing them for energy service providers and telecommunication companies, introducing additional taxes in the same sectors (partly in parallel);
- introducing a fringe benefits system with the aim of optimising taxes, then increasing the taxes on these benefits;
- introducing a generous sponsorship system for sports clubs, then considerably reducing the available benefits;
- multiplying the food-chain supervisory fee and the advertising tax, then lowering it considerably following EU pressure.

These were only examples of **inconsistent tax law changes**. If a company made a decision based on these rules, it later had to reverse it, or was at a disadvantage because of the changes in the regulations. continued on page 3

"It is recommended considering and planning the legal framework of intra-group secondments before the posting starts."

Dr. Petra Eszter Deli,
WTS Klient Hungary

Source: inforadio.hu

Turn on your radio!

It is increasingly common for foreign parent companies to send their employees to work at their Hungarian subsidiaries. Dr. Petra Eszter Deli, expert at WTS Klient Hungary, discusses the legal aspects of the employment of foreigners in Hungary on InfoRadio on the evening of 28 September.

Listen to the conversation at this link!
Please note that the conversation is available only in Hungarian.

Price of changes

Besides these changes, **a number of new taxes have been introduced** over the past few years of taxation policy unfortunately: special tax on financial enterprises, transaction fee, telecom tax, tax imposed on utility infrastructure and energy service providers, insurance tax, accident tax, fat tax – it is hard even just to remember the names of the new taxes. Although these taxes barely affect parts of the companies, primarily their production units, the introduction of a new tax is always bad news in the head offices of these corporations. These measures create a negative atmosphere among investors. In addition, the taxes represent a significant cost factor: large organisations are very slow and it is costly for them to respond to changes. Due to the high number of small changes, **the system is no longer transparent**, which ultimately means that potential investors become unsettled, and decide to choose another location for their investment.

Key to the solution

Despite this, the solution is not necessarily abolishing the new taxes. Certain regulations incorporated into law a few years ago and clearly having a negative effect (for example deferring usage of loss carry-forwards) should definitely be removed. **It is much more important**, however, **to ensure that the current rules of taxation policy remain unchanged in the long run**. 16 years ago, the government currently leading the country accepted tax laws for two years. Investors would appreciate similar measures today.

Lubricating oil and excise tax: what is this about?

When trading with lubricating oil – NAV excise permit :

- Checking precise tariff classification of the product range
- A 50-square-metre warehouse
- Operating licence from the local authority
- Excise collateral
- Keeping records

Author: **Béla Kovács**
bela.kovacs@wtsklient.hu

When it comes to excise tax, most of us think of the so-called "ABC" products, namely alcohol (wine, beer), petrol ("benzin" in Hungarian, meaning petroleum products used as fuel) and cigarettes (tobacco and cigars). Fewer think of a restrictive measure in the case of a commercial company which acquires oil for example (even engine oil), in small packages with a certain customs tariff heading from an EU Member State, in order then to sell it to its customers in Hungary.

Below we explore this issue in greater detail from an excise tax angle, namely, based on the provisions of **the new law on excise taxes that entered into force on 1 July 2017**.

So which products are important from the perspective of excise tax?

Many of us were surprised to see the 2014 tax changes, when the amendments to legal regulations promulgated during the feverish legislative activity in late autumn included the requirement for an **excise permit covering lubricating oils**. And experts showing an interest in this issue only had the Christmas holidays to check out the transitional rules for the implementation. However, not even these specialists could provide any substantial relief for most of the companies affected: from January 2014, certain products can only be acquired and distributed in Hungary with an excise permit.

According to the new legislation, lubricating oil is an energy product including engine oil, turbine lubricating oil, hydraulic oil, driving gear oil and certain other lubricants, as classified by the Combined Nomenclature.

So what is needed for the activity?

It is important that those who intend to carry out **wholesale trading** with these products will need an excise permit, and they **need to be a trader with excise authorisation**. This essentially means that before starting the activity a request has to be submitted to the NAV, now electronically, and other legal conditions have to be fulfilled as well for someone to receive a permit. At each permanent establishment they have to have a warehouse of at least 50 square metres (it can of course be leased as well), and they need to apply for a (generally operating) licence from the competent local authority to start the activity. The NAV may impose a penalty if trade is conducted without a permit.

Expensive excise collateral

It may surprise many of you that one of the conditions for issuing a NAV permit is having **excise collateral**. The taxpayer can provide this either in cash or with a bank guarantee. If a company only distributes products that qualify as lubricating oil, the collateral is HUF 5 million (approx. EUR 16,100). However, identifying the range of products accurately and setting their correct tariff classification is key when assessing the amount of collateral: if the products include ones that qualify as other controlled mineral oils, the amount of collateral to be paid or provided may amount to HUF 120 million (approx. EUR 387,000).

Tax payments and keeping records

So conducting the indicated activity requires (a) permit(s) but generally speaking no excise tax payment liability arises, no tax return has to be filed.

However, **statutory records must be kept**, and failure to do so may result in a penalty levied by the NAV.

So what should you look out for?

It follows from the above that **defining the range of products to be distributed, naming the products and checking the classification** are the most important tasks: it has to be reviewed whether the products to be traded are even subject to the law on excise tax in the first place. As a first step, you should seek the assistance of an excise tax expert, who can provide effective assistance if required in what needs to be done, how to apply for a permit, and how to fulfil the required legal conditions in Hungary.

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