9/2017
3 March 2017

wts TAX LEGAL CONSULTING

wts klient newsletter

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Dear Readers,

Almost a month ago we launched our weekly newsletter, the **WTS Klient Newsletter**, in which we strive to provide you with useful taxation, legal and accounting information every week.
We have held a lot of in-house discussions on topics and articles as well as what our readers and clients would need.
Yet is there anyone who knows better what they would like to read and which topics they would like more detailed information on than you, our partner, who reads these articles?

We are only doing our job properly if our clients receive the best service and the best solutions. Your feedback and opinions are therefore very important to us.

We have put together a short survey that can be completed in 10 minutes and can be found at the following link.
We would be grateful if you could let us know your needs, opinions and ideas.
wtsklient.hu/en/2017/03/03/survey

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Guidelines for HR professionals – taxation of foreigners' income in Hungary

Taxation of foreigners' income in Hungary

When assessing a potential tax liability, the first thing that comes to the mind of most employees who have worked abroad is the

183-day rule.

But the situation is not quite as simple.

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The deadline for submitting personal income tax returns is drawing near and because an increasing number of enterprises have foreign employees, it can often be difficult to judge whether these individuals have to pay taxes or submit personal income tax returns in Hungary. It is frequently not even clear what administrative tasks the HR department has in respect of income tax on foreigners' income in Hungary. In our series of articles we would like to give you some pointers here.

Tax residency in Hungary

When assessing a potential tax liability, the first thing that comes to the mind of most employees who have worked abroad is the 183-day rule: if I worked at least 183 days in a given country, I have to pay taxes there. Unfortunately, the situation is not quite as simple.

When the taxation of foreigners' income crops up in Hungary, the first step should be to check the employee's **tax residency**. Tax residents under Hungarian legislation are considered to be, among others, Hungarian citizens, foreign private individuals who using their right to stay here freely for more than three months have spent at least 183 days in Hungary, or those individuals who only have a residence in Hungary. Resident individuals are subject to an unlimited tax liability.

However, it can easily happen that a foreign employee of a corporation has an unlimited tax liability abroad as well, in Germany for example, if the individual has a permanent home there.

Tax residency in treaties

What should HR do if it turns out that several countries intend to tax a given employee's income under an unlimited tax liability? You can find guidance on the taxation of individual types of income in the double taxation treaties. Hungary currently has valid **double taxation treaties** with 80 countries.

The treaties help to decide in which country the private individual qualifies as a tax resident. To this end, you have to carry out the test specified by the given treaty in each case. Most treaties link tax residency to the person's permanent home, centre of vital interests or habitual abode.

Taxation of individual types of income

The treaties clearly specify the country that may levy tax on individual types of income, such as interest income, dividends, income from employment, etc. The treaties provide guidance on how the given countries should avoid the double taxation of the income in question.

Let's continue with the German example. If a German employee joins the company and his family comes with him, but they keep their home in Germany, then based on domestic regulations both Hungary and Germany will consider the employee as a resident, but based on the treaty we find that he should be considered resident in Hungary. If the private individual receives interest from Germany, this will be taxable in Hungary, and the private individual has to inform his German bank about it and also has to request the suspension of tax deductions. However, in the case of any tax payment in Germany, this income may have to be taken into account when determining the tax rate.

Income from employment

Special rules apply to the taxation of income derived from non-independent activities. In addition to the country of residence, the country of employment, the person paying the salary, the period spent in the country of employment and the notion of the economic employer have to be taken into account as well.

It is evident from the above that the taxation of foreigners' income can pose many problems, and we have to answer several questions in order to draw the right conclusions.

Newly established company obligations: registrations, returns, payments

Newly established company obligations

- Registration obligations
- Opening bank account
- Tax return and payment deadlines
- Annual Report
- Tax top-up obligation
- Capital adequacy rules

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It is very important for every company in Hungary, but particularly newly-established enterprises, to know which tax return obligations they have to comply with. What is perhaps even more important is to know what tax payments and reclaims to calculate with from a cash-flow planning perspective.

Below we have summarised some of the main newly established company obligations of an average company in relation to registrations, tax returns and tax payments.

Registration

After being established, the first duties that fall under newly established company obligations in Hungary are **registering** with the National Tax and Customs Administration (NAV), the relevant local authority(ies), the relevant chambers (paying a chamber membership fee of HUF 5,000 annually – approx. EUR 16), and the Central Statistics Office. Given that almost every tax return and item of data must be filed and submitted electronically to the NAV, one of the first things is to request access to the government portal, generally for accountants and/or tax advisors.

Every calendar year, the National Tax and Customs Authority selects at least 10% of the companies established without a legal predecessor in the given year for inspection, based on a risk analysis. At the selected taxpayers, the tax authority carries out an on-site inspection within 90 days of the issuance of the tax number, to examine in detail the authenticity and credibility of the information reported by the taxpayer (in particular, the registered office, place of central administration, representatives), as well as the fulfilment of tax liabilities.

Value added tax

Newly established enterprises in Hungary are subject to monthly **value added tax** returns in the year they were established and in the following year. Return for the given month must be submitted to the tax authority by the **20th of the following month**, and if any tax is payable, it must also be paid by the 20th day of the month following the month in question. If a claim is submitted for a refund of value added tax, the tax authority makes the payment within 75 days. This deadline is reduced to 30 days, or, in the case of value added tax refunds exceeding HUF 1 million (approx. EUR 3,250), to 45 days, if the company has settled its liabilities giving rise to the deduction of value added tax by the day the tax return is filed, and it notifies the tax authority in writing upon submitting the return.

Personal income tax and other contributions

As an employer, the enterprise has to declare and pay the **personal income tax** advances, health insurance and pension contributions it has deducted, along with the social contributions and vocational training contributions imposed on employers, by the **12th of the following month**.

Annual Report and annual tax returns

If the company did not perform any activity during the pre-company period in Hungary, which is the time between the establishment and the registration of the company, and the company was registered before the chosen reporting date, then there is no need to prepare an individual annual report and returns for the pre-company period. The filing deadline for the annual report and the annual tax returns, and thus the payment deadline for corporate tax and local business tax is the last day of the fifth month following the reporting date, which generally means **31 May** (for companies choosing a financial year that coincides with the calendar year).

If an enterprise has a corporate tax payable, then from this point onwards it will also be subject to advance payments, which are due (depending on the amount) by the **20th of the month following the given month or quarter**. For companies adopting the calendar year as their financial year, local business tax advances must be paid by **15 March** and **15 September** every year.

Tax top-up obligation

The 20th of the last month of the financial year is another important date for companies in Hungary, which generally means **20 December**; this is when the difference between the corporate and local business tax advances paid during the year and the expected total amount of corporate and local business tax for the reporting year must be declared and paid (**top-up obligation**), if sales revenue in the financial year prior to the reporting year exceeded HUF 100 million (approx. EUR 325,000). For newly established companies, the sales revenue generated in the reporting year must be annualised and used as the basis for the calculation.

Other newly established company obligations to focus on when setting up a company

What is particularly important is that the company manager must **open at least one bank account** within 8 days of the company registration. Section 3 (1) of Government Decree 227/2006 (XI. 20) on payment services and electronic payment instruments defines those obliged to open a bank account. Accordingly, resident legal persons and business organisations without legal personality must keep all their monetary assets on a bank account, with the exception of funds kept on hand for cash transactions, execute their financial transactions through such account, and enter into a bank account contract for this purpose.

If the parent company wants to consolidate the newly established company from the very beginning, then attention should be paid here at the outset because this automatically means that the newly published company **has to be audited**.

Another cash-flow planning issue is where the newly established company in Hungary obtains the funds needed for its operations during the first few years. It often happens that the parent company only provides the statutory minimum capital for the newly established company when establishing it, which does not always cover the costs that arise in the initial years of the start-up. Owing to potential losses sustained in the first few years, the company can quickly find that it no longer complies with the **capital adequacy rules** as prescribed in the Hungarian Civil Code, which later on can mean more registered capital is needed or other capital has to be injected.

Of course, over and above the tax types and the tax payment liabilities mentioned above, newly established company obligations can also comprise other tax payment obligations depending on the company's size and activity, such as the innovation contribution, the environmental product fee and the rehabilitation contribution. It is advisable to consult with your accountant or tax advisor on these items.

Key changes to environmental product fee rules from 1 January 2017

Key areas affected by the changes to environmental product fee rules in 2017

- → export chain transactions
- → flat-rate product fee for vehicles
- → statements for advertisement papers
- → product fee codes

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It would have been unusual not to start the year seeing a few changes when studying the legislation on environmental product fee rules. Amongst other things there have been changes to **export chain transactions**, and the group of vehicles where a **flat-rate product fee** may be chosen has been expanded. We also find some amendments regarding the statements related to advertisement paper, while the product fee codes have changed from 2017 (packaging and environmental protection codes). Below we go into some detail on these and other important legislative changes regarding environmental product fees.

Clarification of chain transaction rules

Under the environmental product fee rules in effect from 1 January 2017 **there is no product fee liability** when the ownership of a domestic product subject to a product fee is transferred for the first time to a business organisation established in Hungary for business purposes, or registered in Hungary, if it is verified that the product subject to the product fee was transported abroad to a foreign place of destination or was sent abroad as a postal consignment.

The legislator adding the expression "for the first time" to the wording of the law from 1 January 2017 clearly shows that the **exemption condition above only relates to chain transactions with three parties**.

The law defines the **first of the three parties** as the holder of the ownership right to the domestic product subject to the product fee, who is generally subject to paying the product fee if the ownership right is "transferred to a business organisation established in Hungary for business purposes or registered in Hungary".

The **second party** is the Hungarian business organisation that acquires the ownership right. The **third party** is a delivery address abroad. The wording of the law does not name the third party, and instead requires a verified delivery to a foreign address. The verified delivery of the product to a foreign address starts from the first party, but the second party or even the final foreign customer can initiate the delivery abroad, and in this special case there is no product fee liability.

In light of the above, with export chain transactions involving more than three parties in which products subject to the product fee are sold several consecutive times in Hungary, we definitely recommend reviewing these transactions from a product fee perspective owing to the change in the environmental product fee rules.

Extending flat-rate product fee to more vehicles

The environmental product fee rules valid from 2017 expand the definition of "vehicle", and therefore the scope of vehicles which can opt for a flat-rate product fee. According to this change, the **flat-rate product fee can be chosen from 2017 for buses and vehicles transporting goods as well**.

Statements for advertisement paper

In the case of advertisement paper, customers still have to provide a statement to the manufacturer (printer) in 2017 on whether the ordered product qualifies as advertisement paper or not. However, **from 2017 the lack of such statement means the printer will be subject to payment of the product fee**, while previously, if the customer did not provide the statement, then the printer could decide at its discretion whether the given product qualified as advertisement paper or not, and therefore was it subject to a product fee or not.

Changes in product fee codes

The structure of packaging (CSK) and environmental protection (KT) codes has changed from 2017 as well. Since products subject to the product fee are recorded and declared based on CSK and KT codes, we recommend studying Schedule 1 to the Implementation Decree (Government Decree 343/2011), and where changes have been made then the records should be modified accordingly, in order to ensure that the new and updated codes are used in the product fee returns to be submitted for the first quarter by 20 April.

Other changes to environmental product fee rules

From 2017, plastic freezer bags will no longer qualify as plastic advertisement shopping bags, but as plastic packaging. This reclassification means the **product fee rate so far of HUF 1,900/kg (EUR 6) drops to HUF 57/kg (EUR 0.18)**.

Furthermore, no product fee has to be paid from 2017 for plastic bags used to collect separated waste, and for packaging made entirely from raw material derived from renewable sources and biodegradable plastic. Please note, however, that a return still has to be filed for these products.

Services of the WTS Klient Hungary:

» Tax consulting
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» Legal consulting
» Accounting
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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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