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Common situations – when is VAT registration unavoidable?

If a foreign company takes part in a transaction that has a place of performance in Hungary from a tax perspective, this may create VAT registration liability in Hungary. » page 1

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A significant default penalty can be levied on companies failing to meet their country-by-country reporting obligation or to provide data. » page 3

Dear Readers,

Once the decision is made by owners on transitioning to accounting in a foreign currency, there are numerous factors to consider if we are to prepare thoroughly and in time for the change. First and foremost, we need to decide on the most ideal timing for the transition. We need to assess whether the accounting software in use at the company is suitable for the transition, and what IT developments are necessary for accounting in a foreign currency. There are plenty of tasks from an accounting perspective too. Accounting policies must be adjusted to meet the new requirements, and an opening balance sheet has to be prepared as of the day of the transition.

Our video highlighting the accounting aspects can be viewed by clicking on this link: www.wtsklient.hu/en/2017/06/14/transitioning-accounting-foreign-currency/
Please switch to English subtitles by clicking on "settings" in the right-hand corner of the video!

I hope you will find our summary useful.

Szabolcs Szeles
financial advisory director

Common situations – when is VAT registration unavoidable?

VAT registration: what should we look at?

- type of transaction: product supply or provision of service?
- place of performance: Hungary?
- customer's status (permanent establishment)
- reverse charge possibility

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In an earlier article I summarised what we need to know about financial representation, we looked at the benefits of company representation at the NAV, and I analysed how a financial representative can be of help when taking care of tax matters. In this article we look at some, but not all, of the common situations when VAT registration seems unavoidable for a foreign company.

Importance of place of performance

If the business activity of a foreign company involves Hungary to some extent, it can happen that this involvement is of a nature or an extent that means a **tax number must be requested** to carry out the activity.

First of all, we always have to examine whether any of our international transactions have their place of performance in Hungary: tax payment obligations can only arise where legislation "establishes" a place of performance in Hungary. What helps is that the **place of performance rules** are identical throughout the European Union, but you still need to be aware of related local regulations as well.

Product supply

Things are easier with product movements: in these cases the place of performance is generally where the product is located when the transportation starts, or if there is no transportation of the product, then where it is when the sale is completed. In practice, if the product is physically located in Hungary and it is used (for example sold) in Hungary, then we can be quite sure that this is a **transaction with a Hungarian place of performance**, meaning that we need to request a tax number from the tax authority at the very least. It is important to note that purchasing a product from another EU Member State or from outside the European Union, or moving your own product, can result in a place of performance and a tax obligation in Hungary.

Special product transactions: chain transactions

The situation is different if the product is sold several times and the product is physically transferred from the first seller to the last purchaser. Judging chain transactions such as these requires complex expertise: **actual transportation can only be linked to one sale in the chain, and only this sale can be tax free**. All other transactions will be taxable in the country of dispatch or the country of destination.

If we notice that the physical movement of the product differs from its invoicing path, then based on knowledge of the parties involved and the actual movement of the product we have a good chance of determining correctly which country the place of performance will be in, and where the tax and possibly reporting obligations will fall.

Provision of service and reverse charge

If we provide a service to taxpayers as a foreign company, then in certain cases (for example, if the foreign company typically performs this work in Hungary for a lengthy period, at a specific place, using equipment and personnel, and therefore the foreign company has a VAT fixed establishment in Hungary) it can be important that the work is performed in Hungary. In this case, the foreign company is generally required to request a tax number in Hungary, and the VAT fixed establishment created as a result has to be registered.

In most cases, the place of performance rules result in a Hungarian place of performance when services are provided for a Hungarian taxpayer. However, **generally speaking this does not mean the foreign company has to pay tax in Hungary and is subject to VAT registration in Hungary**. According to reverse charge rules, in the majority of cases the Hungarian tax on these transactions is included by the Hungarian tax-paying customer in its tax return (generally both as payable and deductible tax simultaneously). This means that the foreign company does not have to register in Hungary provided the permanent establishment affected by the service is not in Hungary; the Hungarian tax-paying customer "takes care" of everything instead.

Finally, a brief example of how interesting VAT registration is: if a foreign company provides passenger transportation services to private individuals (organising bus trips to European cities from Hungary), then although there is a place of performance based on the route completed in Hungary, the foreign company does not have to pay tax because such services are exempt from tax by law; the registration obligation applies, however.

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"One major advantage of accounting in a foreign currency is that it substantially decreases exchange rate risk for businesses."

Eszter Balogh, WTS Klient Hungary partner

Source: inforadio.hu

Turn on your radio!

"Companies are still a little bit reluctant to switch to accounting in a foreign currency, primarily because their tax liabilities in Hungary arise in forints" – reveales Eszter Balogh, WTS Klient Hungary partner, summarising her experiences on InfoRadio on 15 June. She discusses the benefits and drawbacks of accounting in a foreign currency, and highlights important information for making the transition.

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

Mandatory country-by-country reporting – Hungary joins the ranks

	Country-by-country reporting	Data reporting
Obligor	As a general rule, the ultimate parent company. In certain cases, the Hungarian group member.	Hungarian resident group member
Exemption	Group's consolidated revenue in the financial year < EUR 750 million	
Deadline	Within 12 months of the last day of the financial year for which data is provided	Last day of the financial year for which data is provided. Transitional rule: within 12 months of the last day of the financial year starting on or after 1 January 2016 for which data is provided.
Sanction	A default penalty of up to HUF 20 million (approx. EUR 64,000) upon failure to comply with obligations, or in the case of delayed, incomplete or defective execution	

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In our January 2017 newsletter we revealed that according to information from the Ministry for National Economy, Hungary would be joining the OECD convention on information exchange in accordance with the BEPS (base erosion and profit shifting) action plan, thus rendering country-by-country reporting mandatory. A couple of months have passed, and the legislation was adopted on 15 May: it incorporates the provisions in point 13 of the BEPS and the rules of Council Directive 2016/881/EU into Hungarian law.

What is the purpose of Action 13 of the BEPS Action Plan?

In the case of multinational companies, the action plan is designed **to mitigate aggressive tax planning and tax evasion**. To this end, in addition to the preparation of transfer pricing records (master file, local file), it also requires country-by-country (CbC) reporting.

What data is reported, and to whom?

It is essentially the group member qualifying as the ultimate parent company that is responsible for the country-by-country reporting (data provision). However, a multinational group is **exempted** from the country-by-country reporting obligation if its **consolidated revenues did not reach EUR 750 million** in the financial year preceding the financial year when the data was provided.

A country-by-country report should contain, among others, the amount and currency of revenues, pre-tax profit, income tax paid, income tax payable, registered capital, retained earnings, headcount, and many other pieces of information in respect of every state or region where the group performs economic activities; based on this information, the competent tax authorities can survey the risks related to assessing market prices, reducing the tax base and profit shifting.

In which cases and by when should Hungarian group members submit their country-by-country reports?

As a general rule, Hungarian companies have to submit a country-by-country report if they qualify as an ultimate parent company. The ultimate parent company of the multinational group (Hungarian resident) and the organisation designated as the resident parent company in Hungary first have to comply with their reporting obligation within 12 months of the last day of the financial year starting on or after 1 January 2016 for which data is provided.

In certain cases, although the Hungarian resident group member does not qualify as an ultimate parent company, it will still be the one subject to country-by-country reporting. These are:

- the ultimate parent company **is not subject to country-by-country reporting** in the state where it is resident, or

- the state of the ultimate parent company is a party to a valid international agreement **to which Hungary is also a party, but there is no valid agreement recognised by the competent authorities for country-by-country reporting**, or
- there is a **systemic error** in the state of the ultimate parent company and the national tax authority notified the Hungarian company of this.

What other obligations does a group member not qualifying as an ultimate parent company have, and by when should these be fulfilled?

Apart from the parent company meeting its country-by-country reporting obligation, **the Hungarian resident group members have a data reporting obligation** towards the relevant tax authority, ensuring that the latter becomes aware of the ultimate parent company, designated parent company or group member status of the Hungarian resident group member in the multinational group, or the lack thereof, and the identity of the organisation obliged to provide data in respect of the country-by-country report (besides reporting the affected companies' names, registered offices, tax numbers and financial years).

The data must first be reported to the tax authority within 12 months of the last day of the financial year starting on or after 1 January 2016 for which data is provided. This essentially means that the Hungarian group member of the parent company subject to country-by-country reporting has to comply with its data reporting obligation towards the NAV by 31 December 2017 at the earliest.

Sanctions

Please note that failure to comply with either the country-by-country reporting or the obligation to provide data, and in the case of delayed or defective execution, the tax authority may **levy a default penalty of up to HUF 20 million (approx. EUR 64,000) on the party with the reporting or data provision obligation**, so it is really important to comply with the above obligations on time and with the right data.

Services of the WTS Klient Hungary:

» Tax consulting
» Financial advisory
» Legal consulting
» Accounting
» Payroll

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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