

TaxAlert

December 2009

Tax changes – 2010

In this tax newsletter, we would like to draw attention to the most important changes of the new tax laws for 2010.

Personal Income Tax

Determination of the Income Received in Foreign Currency

When converting income or expenditure from foreign currency into HUF, the applicable rate is the official exchange rate published by the Hungarian National Bank effective on the day when the income or expenditure arose.

An exception exists, if the private person opts to use the foreign exchange rate published by the Hungarian National Bank on the 15th day of the month prior to the income arising. This option can be determined in a declaration to the payer or in their tax return.

If there is a document proving that the exchange to HUF took place on the date the income arose, the foreign exchange rate indicated on the document can be applied.

Long-term Savings, Income Derived from Long-term Investments

A tax advantage is introduced for long term investments of more than HUF 25,000 entered into with credit institutions or investment service providers. Where an agreement persists for three years subsequent to the payment - or in case of continuous prolongation, in the following two calendar years-, the gain, interest or yield achieved is subject to 10% personal income tax.

If the term exceeds the fifth year subsequent to the conclusion of the agreement, there will be no tax liability arising and the private person should not indicate this income in their tax return.

If the contract is terminated before the three-year period expires, the tax rate will be 20%.

Controlled Capital Market Transaction

The treatment of income derived from a controlled capital market transaction - i.e. the sale or purchase of any financial instruments, goods, foreign currencies - is similar to that for stock exchange transactions. Accordingly, 20% tax is levied on the gain arising.

For such income, a private person is obliged to determine and pay the tax. However, it is possible to take into consideration losses arising earlier.

Application of the Rules on Controlled Capital Market Transactions to Other Investments

Income derived from transactions in publicly issued bonds and collective investment bonds (previously taxed similarly to interest) can, at the option of the taxpayer, be taxed according to the more advantageous rules relating to controlled capital market transactions.

Interest

Interest, royalty or service fees paid (in cash or in-kind) to a private person, resident (as defined) in a state, which does not have a double taxation treaty with Hungary, is subject to 30% tax. The tax is to be determined, declared and paid by the Hungarian payer of the income.

Controlled Foreign Company

Revenue derived from controlled foreign companies (CFCs) is classified as other income. This revenue constitutes the Hungarian resident person's share of the CFC's profit after taxation, less dividends distributed by the CFC. A private person qualifies as an owner, if they hold directly or indirectly (including through close relatives) 10% of the foreign company's shares and/or voting rights.

Vaccinations Provided by the Payer

Tax-free benefits in kind are extended to include vaccinations provided by the payer.

Subsidy Provided by the Employer for Housing Purposes

The 1 million HUF non-taxable limit prescribed for the subsidy provided to the employee by the employer for housing purposes through a credit institution is increasing to 5 million HUF.

Tax Base Completing Element

As mentioned in an earlier tax alert, the base for personal income tax will change. As of 1 January 2010, the so-called "super gross income" will be introduced, i.e. the base for personal income tax will contain all dependent, independent and other sources of income and a tax base increasing element (gross up).

The tax base is to be grossed up by the social security to be paid by the employer, or in the absence of Hungarian social security coverage, the mandatory health care charge. When calculating the tax gross up, non-taxable income should not be taken into account.

In addition, the new rules cover the case where the private person is liable to account for an employer's social contributions.

Health Care Charge

Percentage Based Health Care Charge

Based on the amendment previously accepted, it was not evident, whether the percentage based health care charge should be paid on the benefits in kind subject to a favorable tax rate or for other non-wage allowances. In the new amendment, it is now established clearly that in such cases no percentage based health care charge arises.

From 1 January 2010, foreign resident private persons, who are secured in a foreign country based on Paragraph 13 of the Act on Social Security Contributions, will not be subject to the percentage based health care charge.

Corporate Income Tax

Request for Loss Carry-forward

Loss carry-forwards will no longer be subject to permission from the Hungarian Tax Authority. This change applies to the carry-forward of negative tax bases realized in 2009 and subsequently.

Development Tax Allowance

From 2010, a potential relaxation is being introduced. Instead of considering the tax year before the start of the investment, taxpayers may opt to compare data on employees and wage costs to the average of the three tax years before the start date, when determining if the investment criteria are met. The investment thresholds remain 3 billion HUF, or for investments carried out in preferential areas at least 1 billion, and in case of investments executed by small- and medium sized enterprises at least 500 million HUF present value.

As a further relief, from 1 January 2010, the obligation to also increase the number of employees related to the development tax allowance, will be abolished.

The above changes will be effective for development tax allowance requests submitted after 31 December 2009.

Furthermore for the tax years 2009 and 2010 there is temporary mitigation of the requirements regarding the increase in the number of employees and wage cost.

The temporary reliefs will come into force on the 15th day following a resolution from the European Commission, but not before 1 January 2010.

Rules on Withholding Tax Related to Foreign Corporations

From 1 January 2010, exemption from the 30% withholding tax will be available for foreign companies resident for tax purposes in a state, with which Hungary has operative double tax treaty.

Interest paid by MNV Zrt., MFB Zrt., Eximbank Zrt. and MEHIB Zrt. will not be subject to withholding tax.

Furthermore, interest derived from bonds listed on a recognized stock exchange of any EU-, EEA or OECD countries will be exempted from withholding tax.

Controlled Foreign Companies (CFCs)

The concept of CFCs redefined by the tax law amendments accepted earlier in 2009 has been modified again.

A private person will qualify as an owner if they hold at least 10% (instead of the 25% enacted previously) of the voting rights or shares of the foreign company, not only directly but also indirectly.

In addition, a foreign company will qualify as a 'CFC' if a majority of the revenues obtained by the foreign company derive from a Hungarian source.

Investment activity has also been defined, such that it constitutes long-term investment in shares, the acquisition, holding and transfer of shares and bonds. Furthermore, the activities of investment funds and similar corporations seated in any EU or OECD member states, or states with which Hungary has an double taxation treaty, provided that the organizations are monitored by the national financial supervisory authority of the given state.

The CFC rules do not apply to foreign companies, where the owner, holding at least 25% of the shares of the company, is registered on a recognized stock exchange for at least 5 years.

Income Derived from CFCs

The obligation introduced last year, to purchase Hungarian state bonds as a condition for decreasing the corporate income tax and solidarity tax liabilities on income derived from controlled foreign companies, is abolished. This change was prompted by the Commencement of an EU Commission procedure which qualified this provision as discriminatory.

“Real Estate Company”

The definition of “real estate company” introduced in the summer tax law amendments has been refined in several aspects. The most important change is that whilst calculating the real estate value constituting 75% of the total assets, the market value of assets shown in the financial report of the taxpayer and its related parties effective on the balance sheet date should be taken into consideration.

The new provisions should not be taken into account where shares have not been transferred or withdrawn in the relevant calendar year.

Furthermore, it has been defined that if the foreign owner fails to declare its residence for tax purposes, it can be qualified as a taxable entity.

Foreign Interest Income

A tax base reduction is being introduced for interest income derived from other countries. The taxable interest income should be reduced by 75% of the interest arising, taking into account some amending factors prescribed by law.

Individual Owned Company

Further to the amendments listed above, the accepted amendment also extends the rules to companies owned by an individual.

Tax on Energy Suppliers and Traders

Interpretive clarifications are introduced on proportioning the tax base for energy suppliers and traders. The amendment prescribes comparison of the sales revenue derived from the energy supply activity shown in the financial report or accounting closing, to the total sales revenue.

The new provisions mentioned above can also be applied in the tax year 2009; however, due to lack of time, the affected taxpayers are not obliged to take the amended rules into consideration when fulfilling their top-up liability for 2009.

Local Business Tax

The tax-free part of the local business tax base derived from a foreign permanent establishment should be calculated based on the allocation rules in Appendix 3 of the Act on Local Taxes. In the future, the expression relating to a “conurbation” should also apply for foreign permanent establishments.

Property transfer tax and gift duties

The scope of gift duty and property transfer tax are being extended. The Act on Duties is being extended to apply to the acquisition of motor vehicles registered in Hungary, property rights, and the shares in companies owning domestic real estate. The changes also clarify that shares in business entities qualify as movable property.

The forgiving of claims up to HUF 10,000 of credit institutions, investment service providers and financial enterprises, derived from financial or investment services are exempt from gift duty.

From 2010, all entrepreneurs involved in trading in real estate are entitled to apply a favorable rate of 2% property transfer tax, provided that at least 50% of their net sales revenue achieved in the last tax year derived from trading of real estate. Furthermore, all entrepreneurs involved in financial leasing activity, which have a permission from the Hungarian Financial Supervisory Authority, are entitled to apply the favorable rate, provided that they issue a declaration on undertaking to sell the real estate in 2 years, or to lease it out under a financial lease, resulting in the transfer of ownership at the end of the lease term.

The new amendments maintain the changes on property transfer tax accepted earlier, with the addition of proportioning in case of shared ownership. Based on the changes, the general rate of property transfer tax will be 4% of the value of the property (not decreased by taxes and liabilities). For acquisition of real estate or shares in companies holding domestic real estate, the transfer tax rate is 4% up to HUF 1 billion per real estate, and 2% for the market value exceeding this threshold. The property transfer tax is capped at HUF 200 million per item of real estate.

The changes have refined the territorial and personal scope of the Act on Duties, with respect to companies owning real estate. The definition of a company owning domestic real estate has been extended to a company holding directly or indirectly, at least 75% of the shares in a company owning real estate in Hungary. This means that property transfer tax liability arises not only upon the direct sale of shares in companies owning real estate in Hungary, but also upon an indirect sale higher up the group ownership chain.

The stamp duty payable for the supervisory procedure initiated against a resolution of the Hungarian Tax Authority will be higher in most cases. The amount of stamp duty would change from HUF 15,000 to HUF 400 on each HUF 10,000 (or part thereof) of the disputed amount, with a minimum of HUF 5,000 and maximum of HUF 500,000.

Act on the Rules of Taxation

The applicability of a binding ruling can be extended (re-confirmed) for 50% of the related process fee, if changes in the findings of fact or in the relevant laws do not have a significant impact on the facts detailed in the ruling or the tax liability. An important amendment is that for certain cases, binding rulings can be requested not only for future transactions, but also for transactions already commenced and which are ongoing.

In future close relatives will also be included in the definition of related parties in the Act. Furthermore, the domestic taxpayer and its foreign permanent establishment will also be considered as related parties.

From the tax year 2011, "real estate companies" will be obliged to fulfill their registration liability not within 90 days subsequent to the due date of their corporate income tax return (as for 2010), but by 31 August.

In future, in cases related to payment relief and remission of penalties referring to local business tax, the requests should be submitted to the State Tax Authority. (In the first instance, the State Tax Authority will issue resolutions based on a declaration by the Local Tax Authority.)

Related to the taxpayers opting for a financial year differing from the calendar year, the new amendment refines the provisions included in the summer changes. The right to establish local business tax obligation will lapse within two years from the last day of the tax year starting in 2009.

Act on Accounting

The scope of the Act C of year 2000 on Accounting will also extend to companies operating with limited secondary responsibility, and those companies operating with unlimited responsibility, which do not fall under the scope of simplified enterprise tax.

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