Doing Business in Hungary

2009

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1. Introduction

UHY is an international organisation providing accountancy, business management and consultancy services through financial business centres in over 70 countries throughout the world. Business partners work together through the network to conduct transnational operations for clients as well as offering specialist knowledge and experience within their own national borders. Global specialists in various industry and market sectors are also available for consultation.

This detailed report providing key issues and information for investors considering business operations in Hungary has been provided by the office of UHY representatives:

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Information in the following pages has been updated so that they are effective at the date shown, but inevitably they are both general and subject to change and should be used for guidance only. For specific matters, investors are strongly advised to obtain further information and take professional advice before making any decisions. This publication is current at March 2009.

We look forward to helping you do business in Hungary.

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2. Business environment

The Hungarian economy

Hungary has a moderately developed agro-industrial economy that is very sensitive to international economic factors. Scarcity of fossil fuels and minerals means that Hungary relies heavily on the import of raw materials.

Two-thirds of Hungary's Gross Domestic Product (GDP) is generated in the services sector, where financial, real-estate, economic and public services are dominant areas. Industry, primarily manufacturing, generates approximately one-fourth of GDP. Agriculture and construction only amount to 4-5% of Hungary's Gross Domestic Product.

GDP growth in Hungary has somewhat slowed in previous years but in most developed European countries the economic climate was mainly unfavourable. Overall GDP growth was 3.9% in 2005, 4.1% in 2006, 1.1% in 2007 and 2.8% in 2008.

National currency, inflation and Central Bank interest rates

The period after Hungary's transformation to market economy in 1989 was characterised by high inflation. To the end of the decade inflation decreased to less than 10% and in 2001 the previous monetary system of gradual devaluation was changed to a floating exchange rate system where the Hungarian Forint (HUF) exchange rate could fluctuate in a relatively wide margin of plus-minus 15 percent around central parity. At the same time full foreign currency liberalization was achieved and the Hungarian Central Bank started using the monetary system of inflation targeting.

As a result of these arrangements and a favourable international economic environment, inflation has fallen to 4.7% by the end of 2003. Inflation was higher again at 6.8% in 2004 and slightly lower at 3.6% in 2005 and 3.9%in 2006 and 8% in 2007 and 6.1% in 2008.

The exchange rate on the 31st December 2008 was 264.76 HUF/EUR Following market processes the Central Bank interest rate gradually dropped to 10% at the end of 2008 from 9.5% in January.

In 2006 Prime Minister Ferenc Gyurcsány was re-elected on a platform promising economic "reform without austerity." However, after the elections in April 2006, the Socialist coalition under Prime Minister unveiled a package of austerity measures which were designed to reduce the budget deficit to 3% of GDP by 2008.

Hungary, as a member state of the European Union may seek to adopt the common European currency, the Euro. To achieve this, Hungary would need to fulfil the Maastricht criteria.

Because of the austerity program, the economy of Hungary slowed down in 2007. Despite some large investments, GDP grew only 0.6 percent in 2008. In foreign investments, Hungary has seen a shift from lower-value textile and food industry to investment in luxury vehicle production, renewable energy systems, high-end tourism, and information technology.

The Hungarian Central Hungary's low employment rate remains a key structural handicap to achieving higher living standards. The government introduced useful measures in the key areas, namely early retirement, disability and old pensions.

2008-2009 Financial Crisis

On 10 October 2008, the Forint dropped by 10% many loans are made in Euro or Swiss Francs in Hungary.

On 27 October 2008, Hungry reached an agreement with the IMF and EU for a rescue package worth about US$20 billion.

Official statistics

	2005	**2006**	**2007**	**2008**
Population average (1000)	10,098	10,077	10,045	10,031
Total area (in km2)	93,030	93,030	93,030	93,030
GDP at current prices (billion HUF)	22,055	23,757	25,374	No data
GDP index (Previous year=100.0)	104	104.1	101.1	100.6
Central Bank interest rate (at end of period) (%)	6	8	7.5	10
Consumer Price Index (Previous year=100.0)	103.6	103.9	108	106.1
Exchange rate (at the end of period HUF/EUR)	252.73	253.91	253.35	264.78
Exchange rate (annual average HUF/EUR)	248.05	264.27	253.15	264.15
Unemployment rate (%)	7.2	7.5	7.4	7.8

3. Foreign investment

Hungarian law offers a wide variety of tax and non-tax incentives in relation to capital investment. The tax incentives are largely restricted to manufacturing entities and are dependent on the size and/or location of the investment project. Non-tax incentives take the form of grants, interest-free loans or interest subsidies, and are given on a case-by- case basis following a specific and detailed application.

The fundamental incentive is in the tax system itself, under which a corporate tax rate of only 16% and a corporate income surtax rate of 4% applies to business profits. Profits that are retained or 'ploughed back' by the shareholder into the same or another business are subject to no further taxation, regardless of the type of activity, the size of activity or the size of the business. On the other hand, profits distributed as dividends are subject to further taxation, with the exception of dividends paid to domestic corporate shareholders. Dividends paid to individual shareholders are subject to dividend tax at 25%. Dividends paid to foreign companies are subject to dividend withholding tax at 25%, although most Hungarian tax treaties reduce this to 5, 10 or 15% on dividends paid to a foreign corporation having a 'substantial interest'. Dividends paid to EU companies are free of tax.

Regional development

Regional development is regulated under the Act on Regional Development and Land Use Planning of 1996, which also provides the general rules on funding. Funds are allocated to qualifying activities under the Act on the budget, which constitutes the major blueprint for central subsidisation, augmented by various allowances provided to businesses and funds for the development of the economy, employment and infrastructure.

Subsidies are available for resident legal entities (regardless of their domestic or foreign ownership), unincorporated organizations and natural persons with a domestic domicile. Subsidisation may take the form of grants, both repayable and non-repayable, and interest subsidies for development loans.

Each application must relate to a single subsidisation objective. Qualifying objectives are determined by Government Decree and include, for example, investment projects for creating new jobs and development projects for seeking new market opportunities or changing the product structure.

Regional funds include municipally regulated funds for developing local infrastructure, as well as funds and tax allowances granted by local government. Other funds include regional development aid and loans.

Environmental protection

The Environmental Protection Fund provides incentives for creating an environmentally-friendly economy, preventing or cleaning up environmental damage, preserving natural resources and areas, promoting the use of the best available technologies and pursuing environmental research. This Fund is a priority element within the state budget and qualifying activities are allocated subsidies under the Act on the budget. Applicable tender procedures, together with the relevant terms and conditions, are published by the Ministry of Environmental Protection.

Local governments have the power to establish local environmental protection funds. Allocations from these funds are determined on an annual basis, when the local government issues its decree on its budget and adopts the annual closing accounts.

Local support

Local authorities at the megye (county) and town or district level are also often able and willing to provide assistance, particularly for new projects or those likely to revitalise failing enterprises. Although cash grants are very rarely available at this level, valuable assistance can often be given in other ways. Such assistance includes the provision of cheap land (in some cases even free of charge), help and assistance with finding and training employees, and introductions to other reliable local businesses as future suppliers or customers.

Many local authorities have established formal programs to encourage investment. More than 30 towns have established ‘industrial parks’ as homes for new businesses.

Investors in these industrial parks typically received appropriate premises with full infrastructure backup services, thus enabling their management to concentrate (during the start-up stage) on marketing and other business-focussed matters. While the nature and extent of local authority support varies according to place and circumstances, early contact with the local authorities is recommended in all projects of potential significance to a local community.

4. Setting up a Business

Company legislation

The harmonisation of Hungarian commercial and company law with the EU legal system has been fully achieved. Act IV of 2006 regulates the formation of companies, whilst Act V of 2006 on publicly available company information, company court procedures and solvent liquidation governs the steps involved in founding companies.

Forms of Business entities

The following six types of business entities are available under the Companies Act:

- Company limited by shares (Részvénytársaság-Rt.)
- Limited liability company (Korlátolt felelősségű társaság-Kft.)
- General partnership (Közkereseti társaság-Kkt)
- Limited partnership (Betéti társaság-Bt.)
- Trade Association (Egyesülés).

Each of these entitles is permitted to be up to 100% foreign-owned or foreign-controlled.

Company limited by shares

A company limited by shares (Rt.) is a similar corporate form to the German AG and is the most strictly regulated of all the company forms. Depending on how they are established, Rts are either public or private companies, the difference being that a public company has at least some publicly issued shares. Initial public offerings and the publication and alteration of prospectuses are subject to the approval of the Hungarian Financial Supervisory Agency. The Companies Act allows Rts to have only one shareholder.

The Rt. form must be used by all companies that are engaged in banking, auxiliary financial, insurance or investment activities. Specific legislation pertaining to such companies contains further regulations.

Rts may issue shares in a printed or dematerialised form. However, from 1 January 2002, only dematerialised shares may be offered publicly. Except for certain statutory exceptions, Rts. may issue both registered and bearer shares. Additionally, an Rt’s statutes may allow for the issuance of several different categories of shares, including ordinary shares, preference shares, interest-bearing shares and employees' shares. There are detailed rules governing the issuance of these types of shares.

Rts must have a board of directors, composed of between three and eleven members, as well as a supervisory board of at least three but not more than fifteen members. If the annual average headcount of full-time employees exceeds 200, then one-third of the supervisory board must be made up of employees. The Rt. must also appoint a statutory auditor.

The minimum share capital for Rts is HUF 20 million, which may consist of both cash contributions and contributions in kind. To form a Rt., the greater of HUF 10 million or 30% of the share capital must be contributed in cash.

Limited liability company

A limited liability company (Kft.) is similar to the German GmbH and is the most popular form for foreign investors. The Kft. is most suitable for cases where the number of members is relatively small and where all the members intend to participate to some degree in the company's affairs. It is also possible to have a one-member Kft.

One or more elected managing directors will be responsible for the management and representation of the company vis-á-vis third parties. Additionally, a supervisory board of at least three but no more than fifteen members must be appointed if the Kft has an initial capital exceeding HUF 50 million or if the annual average headcount of full-time employees exceeds 200. For a one-member Kft, the establishment of a supervisory board is only required when the annual average number of full-time employees exceeds 200. In such cases, one-third of the supervisory board members must be employee representatives.

A Kft is required to appoint a statutory auditor if the total net revenue of the company exceeds 100 million HUF in two years average.

The registered capital of a Kft may not be less than HUF 500 thousand HUF and it may consist of both cash contributions and contributions in kind.

Partnerships (Kkt. and Bt.)

The partnerships listed in the Companies Act are general partnerships (Kkt.) and limited partnerships (Bt).

Partners in a general partnership are jointly and severally liable for their business activities. Each partner is entitled to manage the company in accordance with the company's statutes. If the partner is a legal entity, then the managing director or directors of the legal entity assumes management and representation responsibility over the partnership.

The Companies Act does not limit the number of partners in a partnership provided there are least two. There is also no requirement that partners should be natural persons. However, natural persons can only carry unlimited liability in one partnership at a time.

There are no maximum or minimum limits for capital contributions. Profits and losses are generally divided in proportion to the capital contributions, unless otherwise stated in the partnership statutes. However, a partner can not be totally excluded from either the profit or the losses of the partnership.

Limited partnerships are governed by the same rules as Kkt, unless the Companies Act provides otherwise. A limited partnership must have at least one unlimited and one limited partner. Only unlimited partners and, if applicable, limited partners whose name is included in the company name, may assume managerial responsibility and represent the partnership in its dealings with third parties.

Trade association

The rules applicable to trade associations are contained in the Companies Act and the Civil Code. This type of company currently plays a minor role in the Hungarian economy.

The trade association (Egyesülés) is a collaboration of two or more members for a specific purpose, such as industry advertising or maintenance of common training facilities. It is a non-profit organisation and is modelled on the EU European Economic Interest Grouping. The members of a trade association have joint and several liability for the company's debts that are in excess of its assets.

Branches and representative offices

Foreign companies wishing to conduct business in Hungary may now establish a branch, which is an economically independent organisational unit that has no independent legal entity. In order to do so, however, they must be based in a country that is party to a bilateral or international treaty (for instance, the OECD or EU) that allows the establishment of such an entity in Hungary. A branch may conduct the full range of business activities, such as trading, manufacturing or the rendering of services.

Foreign companies are also allowed to establish representative offices that do not carry out business activities and are engaged only in activities of an auxiliary or supplementary nature, such as the mediation and preparation of contracts.

Both branches and representative offices must be entered into a Hungarian company register. Unlike companies, which can operate as pre-companies, branches and representative office cannot commence operations until their registration has been finalised.

5. Labour

The supply of labour depends on the monetary compensation employers give for work. Higher wages make more people enter the labour market, although companies often consider promoting their best workers for upper-level jobs rather than hire new employees. It motivates workers to perform well and at the same time it reduces the costs of recruiting.

The activity (total labour force available) rate was around 54.6%, the unemployment rate was around 7.8% in 2008.

The Labour Code

The most important act that governs employment in Hungary is contained in the Labour Code, which was introduced in 1992. It contains that disadvantageous discrimination against employees is prohibited on a number of grounds which includes sex, religions and any factors unrelated to their employment. Discrimination in relation to promotion is specially prohibited and promotions must be based solely on the grounds of seniority, occupational ability, experience and performance.

With a few exceptions, the Labour Code covers all Hungarian and foreign employees who work in Hungary in the employment of a Hungarian or a foreign company. A work permit is required for foreign employees and they are subject to special security rules.

Collective agreements and employment agreements are null and void if they do not comply with the Act. The employer and the employee can agree to apply different rules from those contained in the Labour Code provided they are more beneficial for the employee.

Contracts of employment

An employer and an employee must enter into an employment contract, regardless of the anticipated duration of the employment. The contract must contain the employee's salary, job description and specific place of work. At least one day before the execution of the contract will be signed, the employer has to send a settlement to the tax administration which contains the new employee's personal details.

After the employment contract is signed, the employer must provide the employee with a written description of his or her most important rights and obligations.

Fringe benefits and paid vacations

Tax shelter means that you can reduce your tax, for instance with a determined percentage of the cost of your life insurance. Companies use another type of tax paying avoidance, which is increasing their employees' income by the means of invisible income such as luncheons vouchers, holiday vouchers, free health insurance and other allowances, instead of offering a higher salary. These are the so-called loopholes.

Employees are entitled a minimum annual vacation of 20 to 30, depending on their age. Single parents and employees who play the larger role in raising the children are entitled to receive supplementary holidays. Employers have a limited right to determine when employees can take their vacations.

Termination of employment

Employment may be terminated by mutual agreement and by ordinary or extraordinary termination. If the employee's contract is for a definite duration, then the employer may dismiss the employee before the contract expires and pay the wages for the remainder of the term (but not more than one year's wages). Another special feature of fixed-term employment arrangements is that they cannot be terminated with ordinary termination. Other than ordinary termination initiated by the employee, employees cannot be dismissed without sufficient justification. This justification must state clearly why the employment is terminated.

The option of extraordinary termination may be exercised if the other party wilfully or by gross negligence substantially violates an employment obligation, or acts in a way that renders the continuation of the employment impossible. The reasons for ordinary termination are related to the employee's work or to the employer's operations.

Special rules apply to layoffs where a number of employees are dismissed. The Labour Code lists the situation where employers may not terminate the employment (sick leave, military conscription or military reserve assignments).

For ordinary termination, extraordinary termination by the employee and the dissolution of the company without a legal successor, the employee is entitled to a paid notice period and severance pay. Where the employee does not make a claim for the restoration of the employment relationship, then he or she has the right to sue for damages equalling between 2 and 12 months' wages, in addition to the wages unpaid since the dismissal.

When the employer and the employee terminate the employment by mutual agreement, they are free to decide the relevant terms. Such agreements are practically impossible to challenge successfully in court.

Social security

The act which governs the social security system was introduced in 1997 and it is called Social Security Cover. It contains the regulations of health care, unemployment and retirement. Regarding the latest security rules employers have to make monthly and yearly various employment-related settlements which contain all of the contributions.

The 2009 contribution chart is shown below.

	Employer (%)	Employee (%)
Social security (health and pension)	29 (5+24)	15,5 (6+9.5)
Unemployment	3	1.5
Training contribution	1.5	-
Total	33.5	17.0

In addition, the following contributions are also payable:

- The employer is required to pay a standard health care contribution in sum of HUF 1,950 (which is 65 HUF per day) if the employee's income exceeded 30% of the minimum gross salary in the previous month.
- Foreign people employed in Hungary by a foreign employer are entitled to social security cover provided there is a social security agreement between the two countries. However, special agreements may be signed in order to ensure social security cover for foreign people and their family members.
- In Hungary there is a card called European Health Care Insurance Card which entitles you to resort to medical services in the area of EU countries and some other countries such as Croatia or Switzerland.

6. Taxation

Tax authorities

Most of the taxes, with tax rates of the same validity in the entire country, are assessed in accordance with law enacted by Parliament. Similarly, the determination of taxable income and the basis of assessment are also defined by tax law. The collection of taxes is the task of the tax authorities that operate under centrally organised common rules and procedures. One of the most significant exceptions is the act on local taxes. This act empowers the local municipalities to levy five different types of local taxes. The maximum tax rates are determined by the act. The municipalities levy and share income from the revenues of vehicle taxes, and to a certain extent they are also able to amend them. In practice, the local municipalities do not always levy the maximum tax rates set by the act; moreover, several municipalities do not levy local taxes of any kind at all. Local business tax plays a significant role upon the decision of finding a satisfactory location for a business venture in Hungary. Local taxes are deductible for Hungarian corporate income tax purposes.

The Hungarian tax authorities are the Hungarian customs office, the local city council levying local taxes as well as the tax office. The Hungarian customs office has rules of taxation different from the rules of taxation applying to the Hungarian tax office and the local city councils levying local taxes, the latter is detailed below.

Tax reports and tax liabilities

The majority of taxes in Hungary are reported and paid on a self-assessment basis. This means that taxpayers must report and pay their tax liabilities by the due dates instead of paying taxes as levied by the tax authorities. Taxpayers must submit their corporate income tax reports by the 31st of May of year following the tax year in question, and pay their liability to the tax office. This is the due date not only for the submission of the corporate tax reports, but also that of the annual financial statement (with the closing date of 31st December of the previous year), that serve as the basis of the tax reports. If a taxpayer opts for a financial year that differs from the calendar year, the taxpayer is to submit its corporate tax report to the tax authorities and pay its liability to the tax office not later that the 150th calendar day following the last day of its chosen financial year. The data of the tax report submitted should be based on the data of the annual financial statement. Advances for the corporate income tax are also to be paid monthly by 20th of the given month, as have been reported by the taxpayer as 1/12 of the tax reported on the latest corporate income tax report.

However, if the reported corporate income tax liability for the previous year did not exceed HUF 5 million, advances are due quarterly. The advances are to be determined according to the tax liability reported for the previous year. Advances paid should be increased to minimum 90% of the actual corporate income tax liability till the 20th of December of the tax year in question if the sales revenue of the taxpayer exceeded HUF 50 million in the previous year. If a taxpayer chooses a financial year that differs from the calendar year, the taxpayer is to complement its corporate income tax advances to 90% the due amount expected till the 20th day of the last month of its financial year. In the case of a tax report submitted on the 31st May does not indicate the settlement of minimum 90% of the actual tax liability till the 20th of December of the previous year, a default penalty is levied on the taxpayer up to 20% on the difference (the difference between the 90% actual tax liability and the sums paid by 20th December). This default penalty is not deductible for corporate income tax purposes.

Refunds in cases of eventual excess payments are paid only after the 31st of May, but the tax office does not pay interest in cases of excess payments to the taxpayers. In the course of the given financial year, the reduction of advances could be requested prior to their due date if it can be supported that the expected tax liability will be covered by the already paid and the reduced advances.

As a general rule, taxpayers should report VAT quarterly. If the net VAT liability reported for the previous year exceeds HUF 1 million, the taxpayer must file monthly reports. Taxpayers, whose total setting VAT in absolute value does not exceed HUF 250 thousand, have to report annually. It is also possible that the taxpayer switch to a more frequent reporting on a basis of a licence that should be requested from the tax office.

The due date for both VAT reporting and paying, if the taxpayer has a net VAT payer position, is 20th day of month following the reporting period, and February 15th of the following year in the case of annual reports.

Taxes on all other kinds of business transactions or withholding taxes should be paid by a day set by law of the month following the transaction date. In cases of taxpayers that opted for a financial year that differs from the calendar year, in addition to the corporate income tax, the tax withheld from dividends, tourism taxes, of local communal tax and of local business tax fall in the same calendar period as their financial year. This means, that the obligations of reporting and of tax paying liabilities of these forms of taxes and contributions will be different in the cases of a taxpayer operating in a financial year that differs from the calendar year. In the cases of all other forms of tax liabilities, as VAT, personal income tax, payroll contributions etc. they will fall under the clauses of the law that apply for standard calendar year operations.

Value-added tax (VAT)

VAT (general sales tax or ÁFA in Hungarian) is by far the most significant indirect tax for most companies. A business must register for VAT if it performs income-earning, economic activities in Hungary in a business-like manner or on a regular basis.

The standard VAT rate is 20% for goods and services, but certain items such as books, newspapers and some medical supplies, attract a reduced rate of 5%. Postal and banking services, stock exchange, gambling and other supplies are exempt. Exports and some medical supplies are zero-rated.

Excise and consumption tax

Excise goods, including petroleum and tobacco products, beer, wine, champagne and other alcoholic products, are subject to a percentile or fixed amount tax. In the case of percentile rates, tax is assessed based on the price, while in the case of fixed amount taxes, the tax is calculated based on the quantity of the excisable goods. Tax rates are progressively approaching EU levels and in terms of excise taxes, the Hungarian system is already quite similar to the internal EU regime. Cars, jewellery and coffee are taxed at rates of between 10 and 35 percent.

Both taxes are single phase and are levied on the manufacturer, wholesaler or importer. Neither is levied on export sales. Accordingly, there are only a small number of businesses that pay excise and/or consumption tax, although these taxes are of considerable importance to the state budget. The main distinction between the two taxes lies in the differing record keeping and reporting requirements (which, in both cases, is extensive).

Motor vehicle tax

Motor vehicle tax is paid by the owners or operators of most motor vehicles. This tax is levied on vehicles by its weight or the power of engine. It is not a significant business burden, except for transport companies.

Taxation of individuals

Territoriality and residence

Individuals who are considered to be tax residents in Hungary are taxed on their worldwide income; non-tax residents are taxed on their Hungarian-source income only.

Under domestic law, individuals are tax-resident in Hungary if they have Hungarian citizenship (unless they also have citizenship of another state and do not maintain a permanent home or a usual place of abode in Hungary). Furthermore, individuals are tax resident in Hungary if they maintain a permanent home only in Hungary. Tax residence is reviewed in each tax year (which is concurrent with the calendar year).

If an individual does not have a permanent home in any country or has a permanent home in Hungary and elsewhere as well, the residency will be determined on the basis of his or her centre of vital interest (i.e. the country with which he or she has the closest family or business ties), and if this cannot be established the residency will be determined on the basis of his or her usual place of residence (i.e. if his or her stay within the country is for at least 183 days in the calendar year).

Tax rates

Tax laws make distinctions between different classes of income because different rules apply to the assessment of taxable income. Some classes are aggregated and taxed at progressive rates, while others are taxed separately at linear (flat) rates.

Categories of aggregated income are as follows:

- Income from independent business activities (e.g. income of artists and persons working under contracts of assignment).
- Income from dependent activities (e.g. employment income, remuneration of elected officials)
- Other income (e.g. cancelled and assumed debts, interest income from non-treaty countries, etc.).

The 2009 rate table for aggregated income is shown below.

Taxable income	%
Up to HUF 1,700,000	18%
Over HUF 1,700,001 HUF 306,000, plus for the amount over HUF 1,700,000	36%

Tax rates for income under separate regulations (%)

Type of income	Tax rate
Non-business sale of property	25

Transfer of Real Estate, right of property value	25
Real Estate rental income – lease of agricultural land	0
Real Estate rental income – apartment, office, garage, etc.	25
Real Estate rental income – apartment as local authority tenement flat	0
Income of condominium	25
Interest	20
Stock market gain	20
Other yield on price	25
Lending of financial instruments	25
Dividend	25
Dividend prepayment	25
Income withdrawn from enterprise	25
Privatisation leasing	25
Money prize	25
Non-money prize	33
Allowance contract with no counter-performance*	54

* Tax free income if the provider of the allowance, annuity or the beneficiary of the inheritance contract is a private individual. Also tax free income if such a contract is concluded by a Local Authority towards a private individual receiving pension allowance

Income in foreign currency

Since residents are taxed on their worldwide income, foreign-source income forms part of the gross income regardless of whether or not it has been remitted to Hungary. For tax purposes, it is translated into HUF at the official (mid) rate of exchange on the 15th day of the month preceding the month of receipt. The same applies to deductible expenses paid in foreign currency, but in such cases the actual exchange rate may be applied. Foreign taxes paid are translated at the year-end rate when computing tax credits.

Income from employment

The gross income of employees includes all cash remuneration received in respect of the employment. Employment income is taxable in the year in which it is paid. For benefits in kind, this is the year in which the benefit is made available to the individual. An exception is wages and bonuses paid by a Hungarian employer on or before 15 January in respect of employment carried out in the previous year; such income is taxable in the previous year.

An expatriate employee remunerated under a contract with a foreign employer for work performed in Hungary will be regarded for Hungarian tax purposes as being a person carrying out 'dependent business activities'. Accordingly, all income received under such a contract is taxable and only certain reimbursed expenses are deductible. Such expenses typically include apartment rent and expenses of business trips. No expense is deductible if the related business documents are not available. Examples of business documents include official invoices and mileage logs.

Benefits, allowances and bonuses

Most benefits are taxed separately at 54%. This tax is paid by the Hungarian employer and is a tax deductible expense for the employer. Individuals are not required to include the benefits that are taxed separately at 54% in their annual tax returns.

Corporate tax

The most important type of tax imposed on profit from an activity of an enterprise is corporate tax and the corporate income surtax. With the exception of private entrepreneurs and companies in effect of Simplified Entrepreneur Tax, all business enterprises are subject to corporate tax and the corporate income surtax. The obligation to pay the corporate taxes applies to the branch offices of foreign companies in Hungary with some minor differences from the general legal statutes. On the basis of this, the selection from the company forms in Hungary – limited liability company, share holder company, limited partnership or co-partnership, branch office – is influenced by the tax circumstances according to the country of the investor and the regulations of the agreement on the avoidance of double taxation, rather than those, which derive directly from the Hungarian regulations.

Tax rate and total tax burden

Corporate tax of 16% and corporate income surtax of 4% must be paid on the taxable income.
Another 25% dividend tax is charged on the payment of dividends if the payment is made to private individuals.
The dividend payment to individuals is charged with an obligation to pay a 14% heath care contribution above the income taxes. This contribution has a maximum level of 450,000 HUF in a year.

The dividends paid to Hungarian companies and other corporate taxpayers are exempt from tax except where it is received from foreign controlled corporations.

The dividend tax can be decreased according to the regulations of the agreement on the avoidance of double taxation. Every such agreement decreases the dividend tax to 5, 10 or 15%, if it is paid to foreign-owned companies having significant investments. The 'significant investment' means generally at least a 25% business share in any Hungarian company. Most of the agreements decrease the source tax in cases where the dividends originated from portfolio investments and were paid to private individuals.

Dividends to non-Hungarian companies will be exempt from dividend tax if they have qualified as a parent company of a local entity for at least two years (a parent company is a 'company' that owns at least 25% of another company's registered capital).

Local Taxes

All the local governments are entitled to levy local taxes on the basis of the Act on Local Taxes, according to its regulations, up to the extent maximised there. Of the local taxes, local business tax is usually the most significant cost burden to enterprises.

The base of the local business tax is the net sales revenue decreased by the material cost, purchase value of the goods sold and subcontractors' fee. The tax rate is determined by the local government within the field of competence of which the company carries out its business activities. The tax rate determined by the local government cannot exceed the maximum tax rate, some local authorities cannot exceed the maximum determined in the Act on Local Taxes (that is 2%).

Summary of tax forms and rates

DESCRIPTION RATE

(a)

(b) **Corporate Income Tax**: (after adjusted profit before taxation)………..……**16%**

(Act 1996/LXXXI.)

- Tax rate for tax base under 50 million HUF is 10% if company meets specified preconditions.

(c) **Corporate Income Surtax**: (after adjusted profit before taxation)…….……**4%**

(Act 1996/LIX.)

Tax after dividend paid to private persons:

(Act 1995/CXVII.)

- For dividend, prepayment of dividend…...……………………....**25%**
- 35% tax rate for dividend is no longer applied.

(in case of foreign persons the highest rate specified in bilateral treaty is applied)

Tax after dividend paid to companies:

(Act 1996/LXXXI.)

- No tax obligation exists in Hungary if domestic or EU resident company receives dividend……………...………………………………….…… **0%**

EVA (Simplified Enterprise Tax) Tax paid after current year earnings (maximum 25 million HUF)…………………………………………………...**25%**

(Act 2002/XLIII.)

Sum of minimal wage from 1st January 2009:………………**71,500 HUF/month**

Social Security Contribution after gross wage:…………..…………………**29%**

29% paid by employer consists of 5% Health Insurance and 24% Pension Insurance contribution. Cost of first 15 days of employee sick leave and 30% of further costs is payable by employer.

(Act 1997/LXXX.)

Health Benefit Contribution (non-percentage) Sum of **non-percentage health benefit contribution** to be paid after employees.......**1 950 HUF/employee/month**

(Act 1998/LXVI.)

Health Benefit Contribution (percentage)……...............................**11% or 14%**

(Act 1998/LXVI.)

Employer contribution after gross wage:...**3%**

(Act 1991/IV.)

Employee training contribution after tax base of social security obligations……………………………………......…………….………..**1.5%**

(Act 2003/LXXXVI.)

Rehabilitation contribution companies with over 20 employees have obligation of quarterly prepayments based on 5% of number of employees…………………………………………..**164,400 HUF/employee/year**
(Act 1991/IV.)

Personal Income Tax cumulative income category tax rates:
for income between 0 and 1 700 000 HUF:……..…..**18%**
for income over 1 700 000 HUF:……...……………..**36%**
(Act 1995/CXVII.)

Personal Income Surtax payable after income exceeding 7,446,000 HUF:…..**4%**
(Act 1996/LIX.)

EKHO **(**Simplified Common Charge Contribution)
company rate:…………………...……..……….............................**20%**
private persons deduction rate:…...……….……………………..……**15%**
deduction rate for private persons receiving pension income and for income exceeding social security ceiling……………...............……**11.1%**
(Act 2005/CXX.)

"**Withholding Tax**" (in non-cumulative income categories – tax after income from rental/real estate/property/financial instruments etc.)…….……………..**25%**
(Act 1995/CXVII.)

Employee pension insurance contribution is deducted from employment income until limit **7,446,000 HUF** is reached……........………..……..……...**9.5%**

Employee health insurance contribution (to be deducted from all employment income, not only income from over 36 hours weekly employment)……………………………………………………………………**6%**

Employee contribution deduction……………………..……………..……...**1.5%**
(Act 1991/IV.)

Value Added Tax…………………...…………………………………...**20%, 5%**
Export of goods 0%; Inter-Community tax free sale; Sale outside territorial scope of VAT; Individual tax exempt sale; Special exemptions from the supply of goods and services; Margin scheme applied for VAT exempt sale
(Act 2007/CXXVII.)

Innovation Contribution:
paid after Local Business Tax base by medium or large enterprise categories:……………………………...…………………………………**0.3%**
(Act 2003/XC.)

Energy Tax:
tax paid by producer/importer/trader of electric energy and coal
(Act *2003/LXXXVIII.)*

Environment Pollution Tax (tax paid after air/water/soil pollution).

Tax obligation most generally applied for air pollution produced by heating furnace owned by company.
(Act 2003/LXXXIX., Government Regulation 270/2003. (XII.24.))

Local Taxes as specified in Act *1990/C.***:**
Local Business Tax
(paid after adjusted net revenue, with deduction for revenue generated at foreign business location):………………………………………………………….. **2%**

Communal Tax: paid based on Local Authority ruling after number of employees …………………...…………………………………….**2.000 HUF/employee/year**

Building Tax
Generally applied maximum sum:……………………….………**900 HUF/m2**

Land Tax for land not occupied by buildings (or construction site). Generally applied maximum sum:…………………………………………...**200 HUF/m2**

Property Gain Duty general rates:………………………….….**2%, 6% or 10%**
(Act 1990/XCIII.)

Inheritance, Gift Duty paid after commercial value with progressively increasing rates depending on type of (family) relationship between parties………………………………......……..**11%, 15%, 21%, 30% or 40%**
(Act 1990/XCIII.)

Legal Proceedings Duty individually specified sums based on company type
(Act 1990/XCIII.)

Registration duty for sale of vehicles 18 HUF/cm³ or 24 HUF/cm³ depending on engine specifications.
(Act 1990/XCIII.)

Environmental Product Fee: Paid after packaging materials, rubber, cooling appliances, electric appliances, advertisement materials etc. Calculated based on classification of product. To be paid by first domestic distributor or consumer company.
(Act 1995/LVI.)

Excise Duty paid after specified range of products: mineral oil, alcoholic beverages, beer, wine, champagne and other alcoholic products.
(Act 2003/CXXVII.)

Vehicle Tax calculated based on engine specifications and production year.

Company Vehicle Tax paid after company vehicles
under 1,600 cm^3:…….…………..…………………..**7,000 HUF/month**
over 1,600 cm^3:…….…………...…………………..**15,000 HUF/month**

Registration Tax paid for vehicles put into domestic traffic based on type of vehicle, engine volume and environmental pollution category:……………………..………………………….…...**250,000 to 9,622,000 HUF**
(Act 2003/CX.)

National Cultural Contribution: paid after specified products/services categories – books, newspapers, records, plastic/metal/glass/ceramic ornaments, writing/copying appliances, telecommunications equipment, jewelry, music instruments, toys, duplicates of artwork, antiques, rental of video-cassettes and CD/DVD discs, advertisement services, photography services, fashion services, radio/TV programs, other art services, architectural services etc.
Paid each quarter after net revenue ……………..……………………**1-3%; 25%**
(Act 1993/XXIII.)

Games Tax: Special tax paid after slot machines/game arcades/casinos operated with license from National Gaming Authority. Also payable after lottery/betting services. Concession fees for operating casinos, betting services, bookmaker services is 50 – 600 million HUF/year. Tax paid after prize base or net games income of lottery draws at 17-30% rate. Monthly games tax after slot machines is 100 000 HUF/location, for other games machines 60 000 HUF/item.
(Act 1991/XXXIV.)

"Robin Hood" Tax: income tax introduced for years 2009-2010. To be paid by companies producing or trading with fossil fuels, mineral gas or electric energy. Payable after corrected earnings before tax:……………………………………**8%**
(Act 2008/LXVII.)

7. Accounting & reporting

All Hungarian companies and other business entities are required to keep proper books of account in Hungarian in accordance with the provisions of the Accounting Act, which follows the EU Directives in all significant respects. The business year (on which a financial statement must be prepared) ends on 31st of December. However, there are exceptions; Hungarian branches of foreign-based companies and Hungarian businesses involved in the consolidation of their foreign parent companies.

Almost all business entities that are obliged to apply double-entry bookkeeping, including branches, of foreign corporations, are subject to a statutory annual audit. The few exceptions relate mostly to certain types of small business (annual sales of HUF 50 million or less).

The Accounting Act also requires the audit and publication of the consolidated financial statements of all companies (or other business entities) with at least one subsidiary. A subsidiary is a company (or other business entity) in which the parent company has, directly or indirectly, effective control. There is an exception relating to Hungarian intermediary holding subsidiaries of Hungarian parent companies. Furthermore, small parent companies whose total assets, sales revenues and number of employees, combined with those of their subsidiaries, are below certain limits over two consecutive years are not required to prepare consolidated accounts.

Accounting principles

The Accounting Act also sets out Hungarian accounting principles, the form and content of financial statements, and related matters. The Act is augmented by government decrees dealing with the special circumstances of banks, insurance companies, stockbrokers, investment funds, pension funds and various non-profit-oriented institutions.

The financial statements must show a true picture of the capital, financial and earnings positions of the business and of their changes since the previous year in accordance with the actual circumstances. The accounting principles applied by a business must meet this overall requirement and must also be in accordance with the following fundamental principles:

- Going concern
- Completeness (i.e. all transactions and other relevant factors must be included)
- Truth
- Clarity of presentation
- Consistency of accounting principles with those of the prior year

- Agreement of the opening balance sheet with the closing balance sheet of the previous year (Continuity)
- Accrual accounting and matching
- Prudence
- Gross disclosures (i.e. assets and liabilities or income and expenditure should not be netted)
- Individual valuation of assets and liabilities, accruals and deferrals
- Substance over form
- Materiality
- Cost-benefit comparison.

Hungarian financial statements generally follow the historical-cost convention with full allowance for depreciation or other loss in value of assets since their acquisition. Liabilities must generally be taken up at their anticipated repayment values, although there are provisions requiring appropriate accounting for interest or similar costs inherent in higher repayment value but properly chargeable to future periods (e.g. Bonds).

Appropriate accruals must be made for expenses as incurred or as their necessity arises. Subsequent events are taken into account insofar as they reveal relevant facts and circumstances that existed prior to the balance sheet date. If their cause and effect both relate to the following year but are sufficient to cast doubt on the relevance of the financial statements to the business position at the time they are issued, they must be fully disclosed.

Form of the financial statement

- Annual report
- Simplified annual report
- Consolidated annual report
- Simplified report.

The form of the financial statement depends on the following factors:

- Total assets (500 million HUF)
- Sales revenue (1.000 million HUF)
- Number of employees (50 head).

Content of the financial statement:

- Basic financial statements
- Balance sheet and income statement
- Notes to the accounts
- Business report

8. UHY firms in Hungary

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9. UHY offices worldwide

For contact details of UHY offices worldwide, or for details on how to contact the UHY executive office, please visit www.uhy.com