



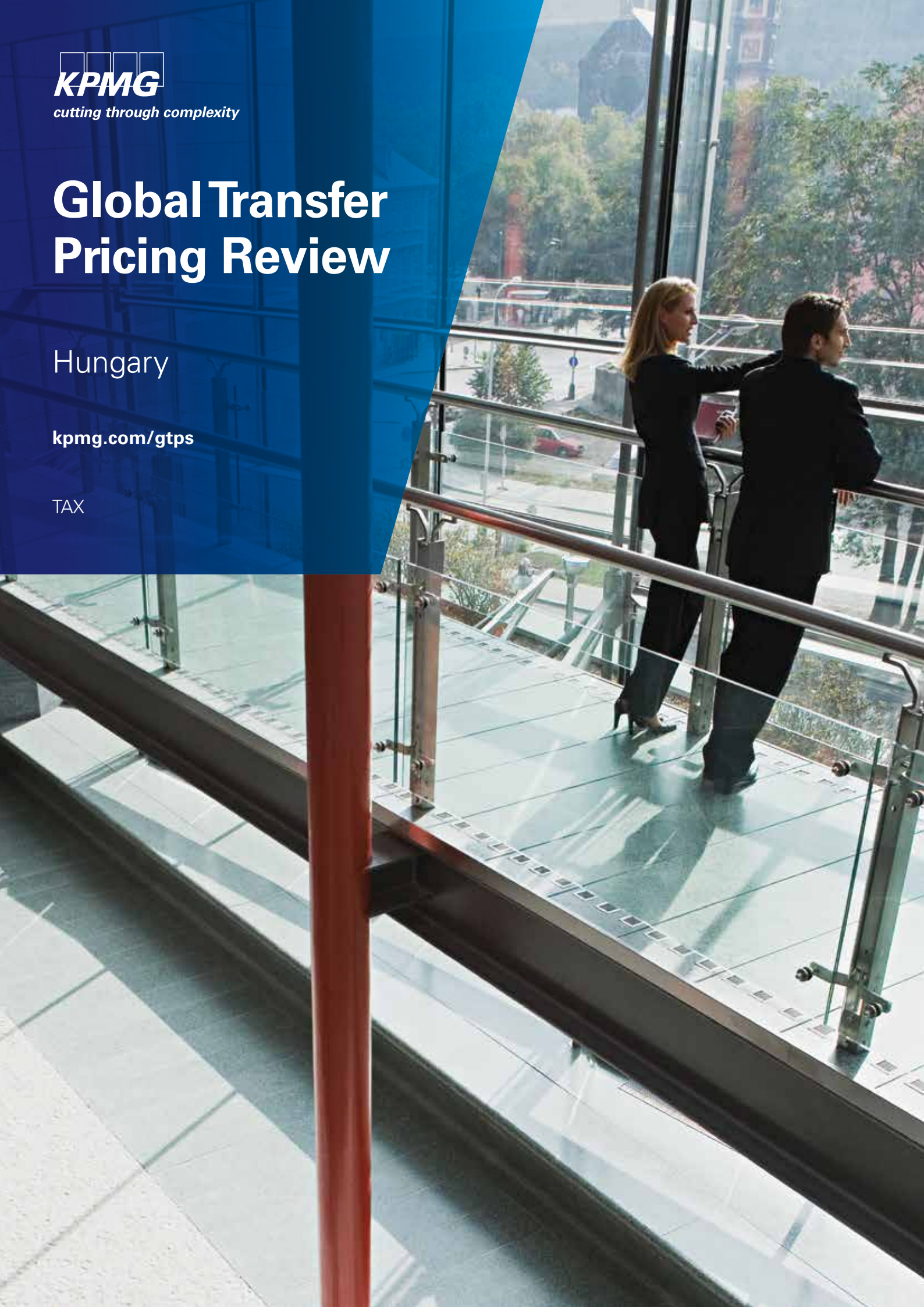
*cutting through complexity*

# Global Transfer Pricing Review

Hungary

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TAX



# Hungary



## KPMG observation

The Hungarian tax authorities are paying special attention to transfer pricing issues. Previously, the mere existence of transfer pricing documentation was sufficient, but recent experience shows that tax audits are moving towards more in-depth analysis of transactions (questioning qualitative screening, testing comparables, challenging particularly benchmarking studies, examining or excluding loss making comparables in the benchmarking set and functional analysis). In addition, the Hungarian tax authorities are focusing on a comprehensive review of documentation (including contracts, back-up calculations that support the arm's length pricing of transactions and deductibility of costs) and challenging loss-making entities.

In line with Organisation for Economic Co-operation and Development's (OECD) Base Erosion and Profit Shifting (BEPS) initiative, tax avoidance and harmful tax structures will likely be met with challenges by the Hungarian tax authorities.

## Transfer pricing study snapshot

### The purpose of a transfer pricing study

	Applicable	Not applicable
Legal requirements	●	
Protection from penalties		●
Reduce risk of adjustment	●	
Shifts burden of proof	●	

## Basic information

### Tax authority name

Nemzeti Adó- és Vámhivatal (NAV) — National Tax and Customs Administration of Hungary.

### Citation for transfer pricing rules

Act LXXXI of 1996 on Corporate Income Tax and Dividend Tax (CIT):

- Section 4 (23) a–e determines the concept of related parties
- Section 18 (1)-(4) regulates the determination of the arm's length price and the applicable methods
- Section 18 (5) determines transfer pricing documentation requirements for taxpayers. Decree 22/2009 of the Ministry of Finance effective from 1 January 2010 determines the formal requirements for transfer pricing documentation
- Section 18 (6)-(8) special cases (e.g. dividend payment in-kind, capital decrease/increase in-kind etc.) are listed which have to be supported by transfer pricing documentation; and
- Section 18 (9) determines a new rule regarding the rules of the application of the interquartile range.

Act XCII of 2003 on Rules of Taxation:

- Section 23 (4) (b) notification of related parties (both the start and the cessation of relationship)
- Section 172 (16) default penalty
- Section 132/B-C Advance Pricing Agreement (APA); and
- Section 178.17 definition of the related parties.

## Effective date of transfer pricing rules

- the new Decree (MF Decree 22/2009) on detailed regulation of transfer pricing documentation was effective from 1 January 2010 and is generally applicable for the 2010 financial year. However, if a company wished, the new regulations could be also applied for the fulfillment of the obligations in connection with financial year 2009
- from 1 January 2011, Section 18 of the CIT incorporated profit split and transactional net margin method (TNMM) as equivalent approaches with traditional transactional methods. However, note that this modification is only applied on business years starting in 2011 and onwards
- as of 1 January 2012 certain sections of 22/2009 MF Decree changed. These modifications aimed to decrease the administrative burden on taxpayers. However, note that the understanding of the new regulation is still uncertain due to possible differences in the interpretation of the wording of the new sections. Further clarification was published in 2013
- as of 21 June 2013 a new modification of the MF Decree 22/2009 was released. The purpose of the Decree was to decrease the administrative burden on taxpayers — which was the aim of the previous change as well — and also to clarify some vague provisions of the former regulation
- effective from 1 January 2015, certain sections of 22/2009 MF Decree changed. The regulation introduced special rules in connection with the application of the interquartile range
- for 2009 and prior financial years, transfer pricing obligations were regulated by the 18/2003 MF Decree.

## What is the relationship threshold for transfer pricing rules to apply between parties?

Direct or indirect ownership with greater than 50 percent voting power, or the existence of majority control. Majority control means when any party has the right to appoint or dismiss the majority of executive officers and supervisory board members. Due to recent changes, in certain cases overlap in managing directors could also trigger related party status.

## What is the statute of limitations on assessment of transfer pricing adjustments?

Five years after the last day of the calendar year in which taxes should have been declared or reported, or paid in the absence of a tax return or declaration.

## Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be submitted to the revenue authority on an annual basis (e.g. with the tax return)?

Yes. A company should declare in the tax return that the transfer pricing documentation has been prepared in line with the European documentation standards (EU Master file concept).

## What types of transfer pricing information must be disclosed?

A company should declare in the tax return that the transfer pricing documentation has been prepared in line with the European documentation standards (EU Master file concept).

## What are the consequences of failure to submit disclosures?

If the taxpayer does not prepare its transfer pricing documentation before the statutory deadline, a default penalty can be imposed.

## Transfer pricing study overview

Can documentation be filed in a language other than the local language? If yes, which ones?

Yes. English, German and French.

Can documentation be filed in a language other than the local language? If yes, which ones?

Yes, for all transactions. It should be noted that Chapter V is not directly applicable, rather only through the 22/2009 MF Decree on detailed regulation of transfer pricing, which is based on the OECD Guidelines, including Chapter V.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

No.

## Transfer pricing methods

Does your country follow the transfer pricing methods outlined in Chapter II of the OECD Guidelines? If exceptions apply, please describe.

Yes.

## Transfer pricing audit and penalties

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? And if so, how many days?

Yes, three days.

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? Please explain.

Normal practice is to expect documentation within three days of request (documentation should be prepared together with the CIT return, therefore it is assumed that documentation is already prepared).

If an adjustment is proposed by the tax authority, what dispute resolution options are available?

After unsuccessful exhaustion of administrative procedures, a company is entitled to bring the matter before the competent court or in certain cases might initiate a supervisory procedure at the head of Tax Authorities and Ministry of National Economy.

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

If the applied price is not in line with arm's length prices, the adjustment will have an effect on the amount of tax payable. Accordingly, a default penalty of 50 percent and a late payment penalty interest might be levied on the basis of the tax arrears due to such adjustments.

### To what extent are transfer pricing penalties enforced?

Unknown.

### What defenses are available with respect to penalties?

Default penalties can only be avoided by complying with transfer pricing requirements.

### What trends are being observed currently?

More and more attention is being paid to the transfer pricing requirements during tax audits, and tax authority inspectors are being trained accordingly. Although special industry focus or transaction focus has not yet been observed, management fees and royalties are usually inspected thoroughly, as well as benchmarking studies (the screening steps, geographical selection, qualitative screening, and loss making comparables in the benchmarking set, etc.) and financial transactions.

## Special considerations

### Are secret comparables used by tax authorities?

Generally no.

### Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

Yes. The tax authorities prefer local comparables (or at least regional ones). Where existing local comparables are left out of the benchmarking set, the tax authorities may challenge the benchmarking study prepared by the taxpayer and perform its own search.

### Do tax authorities have requirements or preferences regarding databases for comparables?

Databases used by the taxpayer are obliged to be publicly available or verifiable by the tax authorities. The preferred database is Amadeus, published by BvD, but not required (online version is not appropriate).

### Does the tax authority generally focus on the interquartile range in a TNMM analysis?

Yes, always.

### Does the tax authority have other preferences in benchmarking? If so, please describe.

The tax authority prefers the benchmarking study to be prepared according to the Hungarian legislation (appropriate independence criteria, region). Furthermore, the tax authority is very keen on comparables with negative profitability.

### What level of interaction do tax authorities have with customs authorities?

Medium, but cooperation is increasing due to the merger of the National Tax and Customs Administrations in 2011.

### Are there limitations on deductibility of management fees beyond the arm's length principle?

Yes, some. There are limitations if it cannot be supported that the management fees incurred are in the interest of the company.

### Are management fees subject to withholding?

No.

### Are there limitations on the deductibility of royalties beyond the arm's length principle?

Yes. There are limitations if it cannot be supported that the royalties incurred are in the interest of the company.

### Are royalties subject to withholding?

No.

### Are taxpayers allowed to file tax return numbers that differ from book numbers?

Yes. Year-end adjustments are permitted, but they should be sufficiently justified by the taxpayer as to economic necessity (e.g. in order to achieve a targeted level of profitability in line with the functional profile of the taxpayer etc.) i.e. their business nature should be defensible. Where the tax authorities do not recognize such adjustments — true-ups — as costs that arose in the business interest of the taxpayer, its tax base might be increased with the amount of the true-ups and taxed accordingly.

In certain cases, such adjustments might also entail VAT or local business

tax issues (e.g. if the adjustments are directly related to transactions subject to VAT, the costs of goods sold or services intermediated are adjusted etc.).

Year-end adjustments are generally recordable in the financial statements, pursuant to Hungarian generally accepted accounting principles (GAAP), i.e. no special treatments are required.

### Other unique attributes?

Effective from 1 January 2012, no documentation is required if the transactional value is below 50 million Hungarian forint (HUF) (approximately 170,000 euros (EUR)).

Effective from 1 January 2012, in the case of certain low value-added services (as defined by the 22/2009 MF Decree e.g. IT services, translation, interpreting, accounting and legal activities, language education, administrative services, storage, canteen service, etc.) special rules were introduced in order to ease the associated burden to prepare transfer pricing documentation. This rule was further modified as of 21 June 2013.

According to the new rules on simplified documentation applicable for these services, if the service provider applies a margin between 3 and 10 percent, the price applied is qualified as an arm's length price without any further analysis or benchmark study. Accordingly, the transfer pricing documentation can be prepared with limited content. However, the condition for applying the new rule is that the arm's length price of the service needs to be assessed by means of the cost-plus method.

Please note that, pursuant to the MF Decree, there are a limited number of conditions that if not met, can result in the simplified documentation being rejected. First, if the margin applied falls outside the previously mentioned range of 3 and 10 percent or the pricing method of cost-plus 3 and 10 percent does not reflect the arm's length price, the taxpayer is not entitled to apply the simplified documentation. Furthermore, the net value of the services, taking into consideration all transactions which can be consolidated in one document, cannot exceed HUF 150 million (EUR 526,000), five percent of the seller's net sales revenue and 10 percent of the operation costs of the purchaser in the tax year.

According to the latest modification, the Hungarian legislation incorporated the application of the interquartile range. The 22/2009 Decree introduced special rules when the interquartile range must be used, and when it is appropriate to apply the full range.

However, note that the understanding of the new regulation is currently uncertain due to possible differences in the interpretation of the wording of the new sections.

## Tax treaty/double tax resolution

**What is the extent of the double tax treaty network?**

Extensive.

**If extensive, is the competent authority effective in obtaining double tax relief?**

In the case of transfer pricing issues, it is not usually effective.

**When may a taxpayer submit an adjustment to competent authority?**

The taxpayers are entitled to submit an adjustment to the tax authorities, as competent authority, at any time. However, we would note that such claims made directly to the tax authorities are very rare in the Hungarian market.

**May a taxpayer go to competent authority before paying tax?**

Yes. The possibility to file an APA exists.

## Advance pricing agreements

**What APA options are available, if any?**

Unilateral, bilateral, multilateral.

**Is there a filing fee for APAs?**

Yes. The filing fee depends on the type of APA (unilateral, bilateral, or multilateral procedure) and on the type of applicable approach (transfer pricing methods).

- for unilateral procedures with traditional methods (i.e. CUP method, RPM and CPLM), the fee payable is from HUF500,000 (approximately EUR1,700) to HUF5 million (approximately EUR17,500)
- for unilateral procedures with other methods, the fee payable is from HUF2 million (EUR7,000) to HUF7 million (approximately EUR24,500)
- for bilateral procedures the fee payable is from HUF3 million (approximately EUR10,500) to HUF8 million (approximately EUR28,000); and
- for multilateral procedures the fee payable is HUF5 million (approximately EUR17,500) to HUF10 million (approximately EUR35,000).

If the exact arm's length price could not be established or the subject of the agreement is only the methodology, the filing fee is the minimum amount of the fee ranges shown above.

**Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?**

No.

**Are there any difficulties or limitations on the availability or effectiveness of APAs?**

No. Unilateral APAs are quite common now due to the 2009 decrease in procedure fees. Contemporaneously bilateral APAs, nontraditional approaches or more complex cases may cause difficulties for the tax authorities. Based on general experience, an APA procedure might be time consuming (depending on the type of the APA, the complexity of the intra-group transaction as well as the capacity of the tax authorities).

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Publication name: Global Transfer Pricing Review

Publication number: 132762-G

Publication date: October 2015