

# Transfer Pricing Country Summary

## Hungary

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## 1. Introduction

The application of the arm's length principle between related parties is prescribed by Section 18 of the Act LXXXI of 1996 on Corporate Income Taxation (CIT Act). In late 2017, the Hungarian Ministry for National Economy issued Decree 32/2017 - on the basis of Article 18 (5) of CIT Act -, based on which related companies shall document the arm's length price, the method used for establishing the arm's length price, and all evidence or circumstances supporting them, for the intra-group transactions. When applying the arm's length principle, the CIT Act refers to the OECD Transfer Pricing Guidelines as the basis of the legislation. Act XXXVII of 2013 incorporates the Country-by-Country Reporting ("CbCR") requirements in the Hungarian legislation. CbCR requirements have been implemented in line with the BEPS Action Plan and Council Directive (EU) 2016/881. The first year to be covered starts from January 1, 2016 for Hungarian parent companies and surrogate parents, whereas other group entities are affected from January 1, 2017 onwards

## 2. Laws & Regulations

### a) References to OECD/EU/Local Rules

- Section 18 of the Act LXXXI of 1996 on Corporate Income Taxation (CIT Act)
- Decree 32/2017
- Act XXXVII of 2013

### b) Definition of Related Party

Related parties are defined as enterprises that would meet any of these:

- Connected by direct or indirect majority (more than 50%) shareholding (voting rights);
- Have a common direct or indirect majority shareholder;
- One is able to appoint or dismiss the majority of the key management or the supervisory board of the other enterprise;
- Foreign entrepreneur with domestic branch;
- Domestic entrepreneur with foreign branch; or • Have the same managing directors or have the same management.

### c) Nature of Transfer Pricing Documentation

A transfer pricing documentation should be prepared if the taxpayer performs a controlled transaction with any of its related parties. Taxpayers are exempted from documentation obligation in any of the following cases:

- The taxpayer qualifies as a small-sized entrepreneur;
- Transactions performed with private persons in a status other than private entrepreneurs (such as transactions with the owners);

- The arm's length price of the given transaction had been assessed and agreed with the tax authority in the frame of an APA;
- Cost recharges;
- Money transfers made free of charge;
- Transactions performed on the stock exchange;
- The price of the transaction is fixed by legislation or authority assessment; • The arm's length value of the intra-group transaction does not exceed 50 million HUF (approximately 165,000 EUR) per fiscal year

#### d) Tax Havens & Blacklists

Hungary does not have an official tax haven list. Further, it shall be mentioned that many countries, as well as the European Parliament has put Hungary in the list of countries with traits of a tax haven.

#### e) Advance Pricing Agreement (APA)

APAs are available as from January 1, 2007. Applications can be made for future transactions on a unilateral, bilateral or multilateral basis for a period of minimum 3 and maximum 5 years (with a possible extension for further three years). An application fee of 2 million HUF (~6,500 EUR) will be charged per each agreement. The fee of preliminary consultation is 500 thousand HUF (~1,625 EUR) per consultation. The maximum timeframe for making a decision on the application is 120 days, which may be prolonged by 60 days twice.

#### f) Audit Practice

Transfer pricing has been in the focus of the Tax Authority since 2004. Transfer pricing may be audited during a general examination or audits only with transfer pricing focus can be ran. Those taxpayers may expect tax audits with a higher probability that generate losses on a continuous basis, or that pay a high-volume management or royalty fee. Entities paying or receiving a loan interest are also in the focus.

### 3. Transfer Pricing Documentation

#### a) Level of Documentation

The Hungarian legislation follows the BEPS recommendations. In line with Decree 32/2017, the documentation consists of the master file and the local file, therefore the subsidiaries themselves are ultimately liable for the preparation even for the master file. The master file-local file approach is mandatory from 2018 onwards, however, taxpayers may satisfy their documentation obligations upon

the formerly effective legislation and prepare a standalone study in respect of 2017 for the last time. The content and formal requirements of the local file are as follows:

- **Administrative information**

- o Date of preparing the documentation;
- o Registered seats and tax ID numbers of the parties;
- o Copy of such effective unilateral, bilateral and multilateral APAs and other taxation agreements should be attached, that were issued by an authority other than the Hungarian Tax Authority;
- o General administrative information on any closed authority and court cases related to the assessment of the arm's length price of the transactions covered by the documentation.

- **General information on the local entities and its operations**

- o Detailed information regarding the local entity's management and reporting flow, the business strategy and the list of the competitors;
- o Information on business restructurings and transfer of intangible assets;

- **Information specific for the local entities' intra-group transactions**

- o General presentation and the general administrative information of the concerned intragroup transactions;
- o the copy of the intercompany agreements, or a detailed presentation of the contract if the parties entered into a verbal agreement;
- o Detailed functional analysis in respect of all parties engaged in the intercompany transaction, mentioning any changes having taken place compared to the previous years;
- o Identification of the most appropriate transfer pricing method with respect of the nature and type of the intra-group transaction and the availability of the comparable data;
- o Methodology for the comparability analysis;
- o Source of data to be used in the course of the comparability analysis;
- o Presentation of the selected internal and external comparable transactions, including the financial data of the independent comparable entities used in the comparability analysis for identifying the arm's length remuneration.
- o Selection of the tested party (when using a one-sided transfer pricing method),
- o Providing an explanation for using a multi-year comparability analysis.
- o A conclusion determining whether the applied transfer prices were at arm's length.

## b) Industry Analysis

By identifying value drivers for the relevant industry, a first indication of the level of profitability common in the industry is being given.

## c) Company Analysis

A description of the management structure of the local entity, a local organisation chart, and a description of the individuals to whom local management reports and the country(ies) in which such individuals maintain their principal offices.

A detailed description of the business and business strategy pursued by the local entity including an indication whether the local entity has been involved in or affected by business restructurings or intangibles transfers in the present or immediately past year and an explanation of those aspects of such transactions affecting the local entity.

## d) Functional Analysis

In conducting a functional analysis, an assessment is made of the significant activities and responsibilities that are performed by the related parties relevant to the Intercompany Transactions under review, the tangible and intangible assets that are employed and the risks that are borne in undertaking the business activities. Such an assessment is consistent with the recommendations that have been made in the OECD Guidelines at paragraph 1.51.

## e) Choice of Transfer Pricing Method

The OECD methods are generally acceptable depending on the facts and the circumstances of the case. There is no hierarchy of methods. The following methods are accepted in the CIT Act:

- Comparable Uncontrolled Price Method
- Resale Price Method
- Cost Plus Method
- Transactional Net Margin Method
- Profit Split Method If none of these methods is applicable, the tax payer may use another approach.

### f) Economic Analysis – Benchmark Study

Taxpayers are required to provide a BM study to determine the arm’s length range of the transactions. Hungarian comparables are strongly preferred though in case the comparables are lacking, the taxpayer may use international comparables.

### g) Inter-company (IC) Legal Agreement

Although an Inter-company legal agreement formalizes the business and financial relationship between group entities, the legal agreements have a lower ranking since the OECD 2017 Guidelines made the “conduct of parties” the prevailing concept.

### h) Financial Statements

Taxpayers are required to disclose intra-company transactions in their Financial Statements.

### i) Production Process for TP Relevant Returns, Documents, Forms and Financials

In the chart below, the existence of the filing requirements with the details of which format is used, the latest filing date, notification requirement and its deadline, thresholds to be applied in case it exists, and the required languages are demonstrated. This information can be seen respectively for CIT, master file, local file, CbCR, local forms, annual accounts and segmented P&L documentations.

	Prepare or File?	Format	Deadline	Notification Deadline*	Threshold* (Yes/No)	Local Language (Yes/No)*(If “No”, it can be filed in English)
<b>Corporate Income Tax</b>	File	Local GAAP and IFRS	the last day of the 5th month from the end of the tax year	No	No	Yes
<b>Master File</b>	Prepare	OECD Guidelines 2017	within 12 months after the last day of the group’s financial year	No	Yes	No
<b>Local File</b>	Prepare	OECD Guidelines 2017	the last day of the 5th month from the end of the tax year	No	Yes	No

<b>CbCR</b>	File	OECD Guidelines 2017	within 12 months after the last day of the group's financial year	The last day of the given financial year	Yes – Annual turnover of EUR 750 million	No
<b>Local form X</b>	N/A	N/A	N/A	N/A	N/A	N/A
<b>Local form Y</b>	N/A	N/A	N/A	N/A	N/A	N/A
<b>Local form Z</b>	N/A	N/A	N/A	N/A	N/A	N/A
<b>Annual Accounts</b>	Prepare	EU IFRS	End of each business year	N/A	Yes	Yes
<b>Segmented P&amp;L</b>	N/A	N/A	N/A	N/A	N/A	N/A
* Country has signed the MCAA agreement for the filing of CBCR.						
* Country does not request as much and detailed information from smaller and less complex enterprises (SME's included) than it does from large and complex enterprises.						

### j) Mandatory Language

Hungarian, English, German and French documents must be accepted by the Tax Authority. However, it is recommended having a Hungarian summary as the Tax Officers may not speak all of these languages

### k) Notification Requirement

Upon request, taxpayers have 3 days to submit their TP documentation to the tax authority.

### l) Record Keeping

Records must be kept in Hungary for a period of 5 years.

### m) Penalties and Interest Charges

Lack of documentation: If a tax payer fails to comply with the transfer pricing documentation requirements, it would be subject to a default penalty. In line with the legislation, the lack of either of the master file and the local file would entail a default fine. A penalty up to 2 million HUF (~6,500 EUR) may be levied per missing documentation. For subsequent violation of documentation obligation, the Tax Authority may impose a default penalty of up to 4 million HUF (~13,000 EUR) per documentation. For repeated omissions in connection with the same documentation, the fine may be up to four times the amount first imposed (8 million HUF, that is ~26,000 EUR).

In the case of a missing, delayed, incorrect or incomplete fulfilment of CbC reports or CbC notification, the Hungarian Tax Authority may impose a fine up to HUF 20 million (~EUR 65,000) upon the taxpayer, or the reporting entity. Tax underpayment: A 50% tax penalty can be charged on the assessed tax underpayment, if any. Additionally, a late payment penalty equal to twice the base rate of the Hungarian National Bank (currently 0.9%) may also be charged.