

2023 Transfer Pricing Overview

Hungary



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Introduction

Related party definition

Transfer pricing rules are the applicable regulations for transactions between related parties as defined by the Hungarian Act on Corporate Income Tax (CIT). In general, we can say that if a company meets at least one of the following criteria, then it will be deemed as related parties for income tax purposes:



- connected by direct or indirect majority (more than 50%) shareholding (voting rights)
- have a common direct or indirect majority shareholder
- is entitled to appoint/dismiss the majority of the executive officers or the supervisory board members of another company

In addition, the Hungarian head office and the foreign PEs/branches, as well as the Hungarian PEs/branches and the foreign head office qualify as related parties; thus, the transfer pricing rules also apply to these enterprises.

Furthermore, the definition of related parties was supplemented as of January 1st, 2015. As a result of the changes, the concept of common directorship was added to the definition. Thus, even if the ownership (voting) rights of one entity in another entity do not exceed 50%, but the entities in question have the same management, then the two entities are considered related parties and are subject to the obligations prescribed by transfer pricing rules.

Transfer pricing adjustment

The Act on CIT defines the cases when entities are obliged to apply transfer pricing adjustments. According to paragraph 18 of the Act on CIT, transfer pricing adjustment is required if the price used between related parties based on their agreement is lower or higher than the consideration used by independent parties within comparative conditions. The profit before taxation shall be modified by transfer pricing adjustment in the following cases:



if the profit before taxation is lower due to the agreed consideration between related parties, the tax base shall be increased by transfer pricing adjustments



if the profit before taxation is higher due to the agreed consideration between related parties, transfer pricing adjustment could be made as tax base decreasing items

Reduction of the tax base is only allowed if both parties are in possession of a declaration signed by both, declaring the difference between the arm's length price and the price used, and the other party is subject to Hungarian corporate tax or a similar tax abroad and increase(d) its tax base with the similar amount. The reduction cannot be validated if the related party is considered as a controlled foreign company (CFC).

On 19 July 2022, the Hungarian Parliament government has submitted the proposal for the 2023 tax package, that sets out important changes to the transfer pricing (TP) rules, requiring TP adjustments to be made to the median.

The new rule says that if the remuneration applied by the taxpayer is outside the arm's length range, the median of the arm's length range shall be considered as the arm's length price. There is an exception, if the taxpayer demonstrates that another value of the arm's length range (deviating from the median) appears more suitable for the transaction under review, in which case this value can be applied as the arm's length price instead of the median.

Transfer pricing adjustments are to be applied irrespective of other tax base increasing and decreasing items.

Struggling with corporate income tax? Get it all sorted:

- Registration for CIT, preparation and submission of statutory tax returns
- Processing of tax liability payments to local authorities

Stay compliant with the latest legislation

Applicable legislation



The transfer pricing rules are determined by different legislations in Hungary, as well as by the Double Tax Treaties.

Act LXXXI of 1996 on Corporate Income Tax (CIT) determines the description of affiliated companies and the tax base modifying items related to the arm's length principle. When applying the arm's length principle, the CIT Act refers to the OECD Transfer Pricing Guidelines as the basis of the legislation.

The rules of Advance Pricing Agreement (APA) are included in Act CL of 2017 on Taxation, together with the sanctions applicable in case of missing transfer pricing documentation. The details regarding the submission of APA request can be found in Decree No. 48/2017 of the Ministry of Finance on Advance Pricing Agreements.

The details of requirements on transfer pricing documentation are included in Decree 32/2017 (X.18.) of the Ministry of National Economy on TP Documentation Requirements.

Also, Double Tax Treaties include necessary information when preparing transfer pricing documentation, as they define the place of taxation of the concerned entities.

Arm's length principle



Comparables

Local comparables are preferred. However, if the reliability of these comparables is not sufficient or limited data is available from the region of Hungary, the use of pan-European comparables deriving from similar economic circumstances are acceptable as well. The tax authority also uses the same database as applied by the taxpayer for its reviews.

Arm's length Range

Section 18 of the Corporate Income Tax Act was modified as of January 1st, 2023, to make the application of the interquartile mandatory for comparable searches based on a public database.

According to the new legislation retrospectively applicable for FY2022, the interquartile range must be used if it is applied to publicly available data stored in a public database or from other public sources (also accessible by the tax authority) – i.e., they are not comparative data available from the affiliated companies' independent transactions. The definition of the interquartile range remains unchanged, i.e., the first and last 25% of the sample should be eliminated.

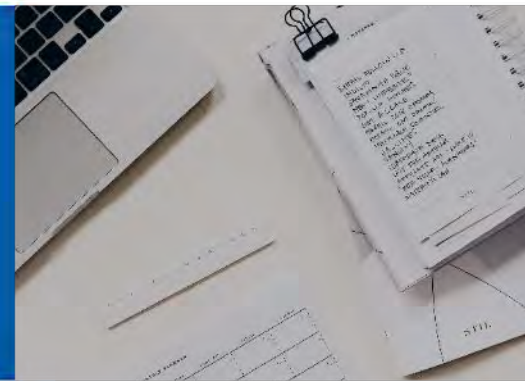
Cost-benefit principle

The Decree assigns that the taxpayer is obligated to consider all facts and conditions available during contracting, modification of the agreement and at the time of fulfilment, which are relevant for determining the arm's length price.

However, the legislation defines the cost – benefit principle, based on which the taxpayer cannot be expected to bear disproportionately high costs related to completing the records. It is worth being aware of this principle, because the taxpayers have the possibility to refer to the abovementioned principle in case a fact or a circumstance was not detailed deeper in the documentation due to its high cost burden.

The above does not exempt, however, the taxpayer from the transfer pricing record keeping obligation.

Exceptions from transfer pricing



According to the Decree no. 32/2017 on transfer pricing documentation requirements, a company is obliged to prepare transfer pricing documentation if it had transactions with related parties within the given tax year.

There are some cases when the company has no transfer pricing documentation preparation liability, even though there was fulfilment with related party:

- the transaction was made based on agreement with an individual
- the company is considered as small-sized enterprise (according to the Act on CIT)
- the arm's length price was determined by the tax authority in the form of a resolution as provided by the Rules of Taxation (in the framework of the so called "Advance Pricing Agreement" (APA) - if there was no change in the facts fixed in the APA resolution
- recharge of consideration for the sale of product or service in the same amount to related party or parties - if the seller or party bearing the cost is not affiliated company
- free cash transfer and takeover between associated companies
- transactions performed on stock exchange being subject to the Act on Capital Market, and for applying other official price or the fixed price specified by law
- the arm's length value of the transaction (excluding VAT) between associated companies does not reach HUF 100 million (~ EUR 250,000) within the tax year (the contracts which may be consolidated are to be considered together)
- for intercompany transactions between members of a Corporate Taxpayer Group, following the establishment of such a Group (The opportunity to create a Corporate Taxpayer Group for corporate income tax purposes is available for Hungarian resident taxpayers from 1 January 2019)

When calculating the limit set by the Decree it is important to know that if the annual report is prepared in foreign currency, the exchange rate of Hungarian National Bank valid on the last day of the tax year is to be used to determine the value of related party transactions in Hungarian Forint.

Methods



According to the Hungarian transfer pricing regulations, the designated methods are:



the comparable uncontrolled price (CUP) method



the resale price method



the cost plus method



the transactional net margin method (TNMM)



the profit split method

Hungarian rules rely on the principle of “the most appropriate method”, meaning that the designated methods are equal. Although, there is no hierarchy between the methods, CUP method is preferred against the others (if comparable uncontrolled prices are available, those shall be examined in the first instance). Other methods may be used after the listed ones have been eliminated.

Documentation



As of January 1st, 2018, taxpayers may choose to prepare documentation based on the “master file – local file” concept. The documentation regarding FY 2017 can be prepared based on the former rules as well. Applying the new concept is, however, obligatory from FY 2018.

For low value adding services, simplified documentation may be prepared if certain conditions are met.

As of 1 January 2020, based on an amendment of the CIT Act, transfer pricing rules shall be applied in the event of a capital increase as a result of contribution in kind provided by a shareholder, who prior to the contribution, did not have majority ownership in the company, but acquires majority ownership through the contribution. The application of transfer pricing rules is also required in case of repurchasing of own shares, or transfer of such shares free of charge.

Documentation requirements

Consolidated transfer pricing documentation



According to the Decree, as a general rule, companies are obliged to prepare transfer pricing documentation for each transaction separately.



However, the Decree gives the possibility for taxpayers to prepare consolidated documentation on transactions meeting the following requirements:

- the subject matter of the agreements and the relevant conditions of the fulfilment of the subject is the same and pre-recorded, or the differences of the conditions are not significant, or
- the agreements are closely related, provided that the consolidation does not jeopardize the comparability.

In case of choosing the preparation of consolidated documentation, the company shall present the reason for the consolidation in its documentation.

Updates and modification of the documentation

There are no specific rules under the Hungarian regulations regarding the annual updates, however, based on the general rules, the transfer pricing report must be updated if certain conditions have changed in the tested financial year, and those changes influence the pricing mechanism.

Regarding the benchmarking analysis, the Hungarian tax authorities prefer database search updates on a yearly basis.

Retrospective modification of the documentation was allowed without limitations before the Decree 32/2017 entered into force. From FY2018, making changes in the transfer pricing documentation is allowed only in the case if an error affecting taxes or arm's length prices was detected in a completed document.

Deadlines

Documentation does not have to be submitted to the tax authorities, however, it should be provided immediately upon request. The statutory deadline for the preparation of transfer pricing documentation is the filing date of the corresponding year's corporate income tax return.



The deadline for finalizing the corporate income tax return is May 31st for calendar year taxpayers. For non-calendar year taxpayers, the filing deadline is the last day of the fifth month following the balance sheet date of the financial year.

If the taxpayer has prepared the Local file until the deadline, the term for the preparation of the Masterfile may be prolonged until the foreign parent company's documentation deadline but no later than 12 months following the last day of the financial year.

Statute of limitation

5 years

The statute of limitation is five years from the last day of the year when the concerning tax return is due.

Language



Transfer pricing documentation and supporting documentation may be compiled in languages other than Hungarian, but the taxpayer is liable to present a Hungarian translation of documentation prepared in languages other than English, French, and German, at the tax authorities' request, by the deadline specified.

Masterfile-local file concept

Hungary adopted the OECD's Masterfile-local file concept, which can optionally be used for FY2017, but obligatory from FY2018, meaning that from 2018 it is no longer possible to prepare standalone documentation. Hungarian legislation basically follows the OECD recommendations on this two-tier documentation structure, but the Decree 32/2017 (X.18.) of the Ministry of National Economy specifies some additional requirements which shall be met by the structure and substance of the Hungarian transfer pricing documentation.

Regarding the purpose of the documentation, the Masterfile presents the common characteristics of the group's general business strategies and operations and the comprehensive functional analysis, and a Local file presents the local subsidiary's contractual details and elaborates on the arm's length price of its intra-group transactions.

Documentation of low value-adding intra-group services



Simplified transfer pricing documentation can be prepared for transactions with low value-adding if the requirements determined by the Decree are met.

The conditions are as follows:

- The arm's length value of the transaction does not exceed HUF 150 million (~ EUR 430,000) in a tax year and
- The revenue from the transaction does not exceed 5% of the sales revenue of the service provider.
- The cost of the transaction does not exceed 10% of the operational costs and expenses of the service recipient.
- The arm's length remuneration is established upon the cost-plus method.
- The applied mark-up is in the range of 3-7% (This constitutes an arm's length mark-up).

Are your transactions covered?

- Due diligence and structuring of the transactions, documentation and set-up of processes
- Financial and accounting consultancy
- Mergers and acquisitions

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Mandatory data provision



General information

Based on the 2022 amendment of Act LXXXI of 1996 on Corporate Tax and Dividend Tax, in addition to the previous documentation (transfer-pricing documentation) obligation related to the determination of the arm's-length price, taxpayers will also have to meet a new data provision obligation as part of the annual corporate tax return.

Scope of the data provision

The detailed rules are included in the amended Decree 32/2017, which defines the scope of transactions subject to the data provision, which can be divided into three categories:

Exemption from the data provision

- Transactions where the aggregated annual value not exceeding HUF 100 million (at an arm's-length price)
- Stock-exchange transactions
- Transactions applying a fixed price determined by authorities/laws

Limited data provision

- Transactions that the taxpayer concluded with individuals not in the capacity of private entrepreneur
- Recharge of independent third-party costs in an unchanged amount and value
- Transfer of liquid assets without consideration

Full data provision

- Transactions that do not belong to the above-mentioned categories,
- Transactions covered by an advanced pricing agreement (APA) resolution

The data provision obligation must first be fulfilled for corporate tax returns filed after 31 December 2022. For FY2022 (ending by 31 December 2022), recharges of independent third-party costs in an unchanged amount and value are not subject to this obligation yet.

Content elements of the data provision

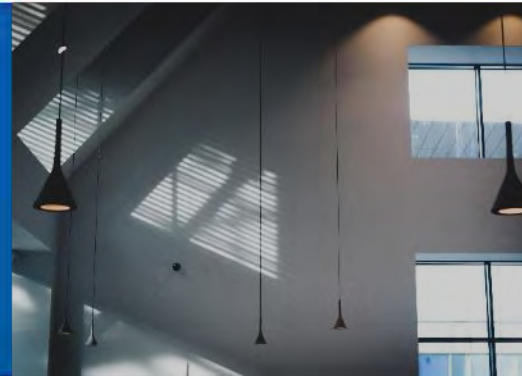
The provision of data per transaction or, where appropriate, per consolidated transaction, includes the following:

1. Designation of the type of the related-party transaction, based on a predefined list
2. Assignment of the most appropriate NACE code
3. Tax number and tax residency of the related parties involved in the transaction
4. The net annual value of the transaction determined in HUF, per related party
5. The value of CIT base adjustment in respect of the transaction, per related party
6. The transfer pricing method selected for the determination of the arm's-length price of the transaction
7. Additional transaction-specific information (e.g. profitability indicator, etc.) in some cases, depending on the selected TP method or the type of the transaction
8. Accounting standard used for the financial analysis of the company selected as the tested party
9. Arm's-length price (value/range) determined for the transaction
10. The transfer price applied in the transaction, also considering the tax base adjustments

All the above requirements are to be complied with in the case of full data provision obligation, while only points 1-5 should be applied for limited obligation.

These changes also have significant implications for the timing of preparing the documentation; from then on, not just the data provision must be compiled by the submission date of the CIT return, but the preparation deadline of the transfer pricing documentation will also be strictly enforced.

Advance Pricing Agreements (APA)



General information

Advance Pricing Agreements (APAs) are determined by the Rules of taxation and have been available since January 1st, 2007. The taxpayer has the possibility to request the tax authority to define the method to be applied, considering the facts and conditions and range of prices to determine arm's length price to be used between the related parties in the future.

The tax authority includes the outcome of the examination in the resolution.

The term of the resolution is a fixed term of three to five years. But it could be extended by an additional three years, based on the request of the involved related parties.

APA filing fee

As per the modified legislation, effective from 1 January 2023, the fee for an APA with the Hungarian Tax Authority has been increased to 5,000,000 HUF for a unilateral procedure. In the case of bilateral or multilateral procedure, the fee is 8,000,000 HUF.

85% of the fee is payable in case of rejected filing, or in case of withdrawal of the request.

50% of the originally paid fee is the fee payable in case of request for prolongation or modification of statement.

HUF 500,000 is the fee of personal consultation.

The detailed rules are included in Act CL of 2017 on Taxation.



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Penalties



If the tax base adjustments required by the tax authority based on transfer pricing rules result in tax default, the standard assessments — tax penalty and late payment interest — will be due in accordance with the general rules.

Furthermore, the default penalty for violating the TP documentation requirements or missing the obligation is up to HUF 5 million (~EUR 12,500) per documentation (Masterfile and Local file qualifies as two separate documentations). In the case of repeated infringements, the maximum default penalty can be HUF 10 million (~EUR 25,000).

Late payment interest may be levied based on the additional tax assessed by the tax authority. No late payment interest should be assessed on default penalties levied due to not having appropriate transfer pricing documentation.



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Contact us in Hungary

hungary@accace.com | [+36 141 235 30](tel:+3614123530)

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