

Challenges faced by international companies in Hungary in 2018

Foreword

Business gate, GDPR, online invoicing or labour shortage? If we look back in a few years' time, which challenge will have had the biggest impact this year?

The life of a company director, a finance or HR manager has never been easy. Planning and managing a financial year is a complex task with many ordeals. This spring we tried to obtain and provide a clearer picture of these ordeals, economic goals and the potential hindrances.

We asked more than 100 managers like you about their current objectives and the obstacles they face. We did this in order to see that we are not alone. We focus on similar issues in our everyday life, and there is a tried and tested solution for everything.

On the following pages you can familiarise yourself with the results of our research as well as the proposed solutions for the most frequent challenges.

Zoltán Lambert
WTS Klient
managing partner



Research methodology

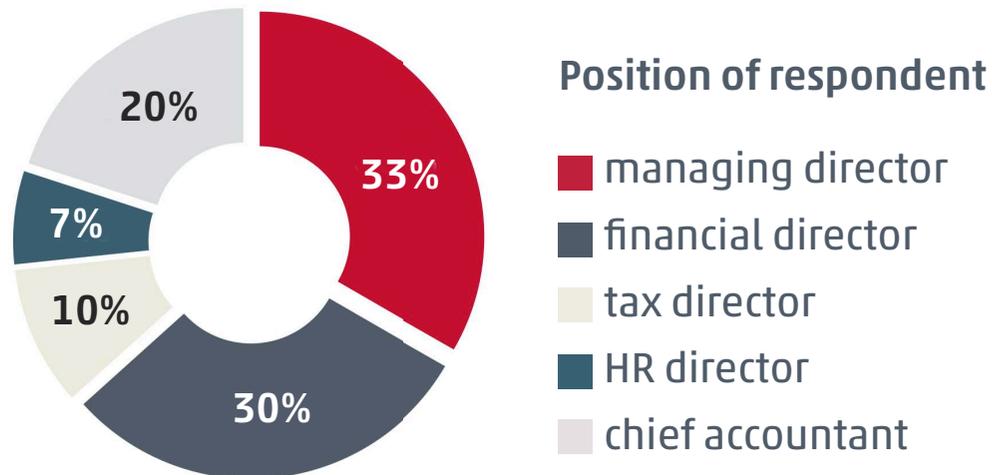
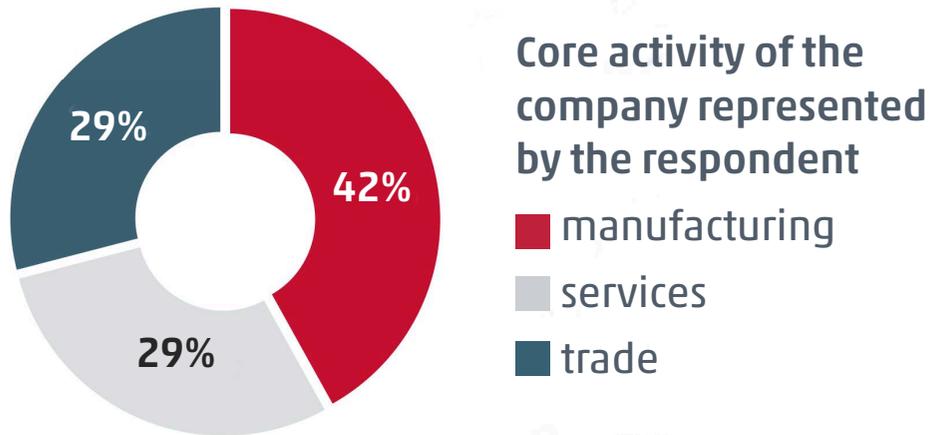
Between 3 January 2018 and 14 March 2018 we asked the heads or financial managers of 145 companies about their plans for 2018 and the challenges their companies face in 2018. Participation in the research was anonymous and voluntary, the responses were collected either personally or by phone or email.

Some 42% of the responding companies work in manufacturing, 29% in trade and 29% in the services sector. One quarter of the participating companies have their registered office in Budapest, almost half of them are in cities outside Budapest, and 27% of them operate in smaller municipalities in the countryside. 33% of the respondents were company managers or managing directors, 30% finance directors, 20% chief accountants, 10% tax directors and 7% HR managers.

On the graphs in the study, the percentages show the distribution of the total responses (100%). During the interviews, respondents could give multiple answers to a specific question. In the study, all the quotes besides the questions are from the respondents, anonymously of course. The quotes beside the compiled summaries and the outlined solutions are from our experts. The copyright to the "Challenges faced by international companies in Hungary in 2018" research belongs to WTS Klient Ltd., any reference or quote is allowed only with the written permission of the copyright holder.

WTS Klient Research
First half of 2018

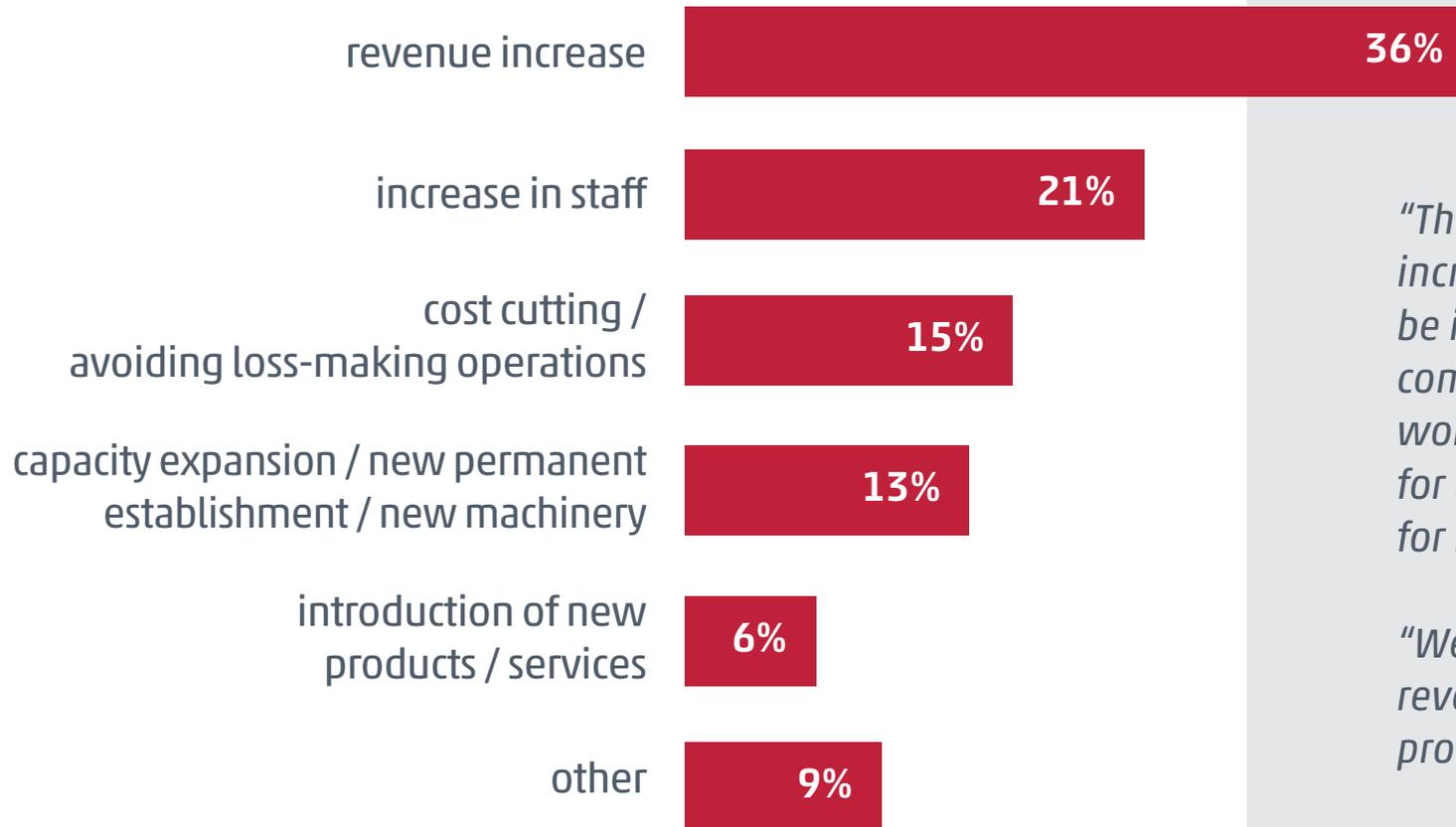
Participants in the research



At the beginning of 2018, WTS Klient asked the financial experts of more than **100** international companies cooperating with the group and operating in Hungary about the most challenging **tax, legal and accounting** issues for them in 2018.

Focus in 2018

What goals have you set for 2018?



"Our goal is maintain the company's profitability despite the increased wage costs."

"The number of staff has to be increased, investments have to be increased. The appropriate combination of machinery and workforce provides the capacity for us to achieve the quantities for manufacturing."

"We expect a strong rise in sales revenues, which will trigger a profit increase too."

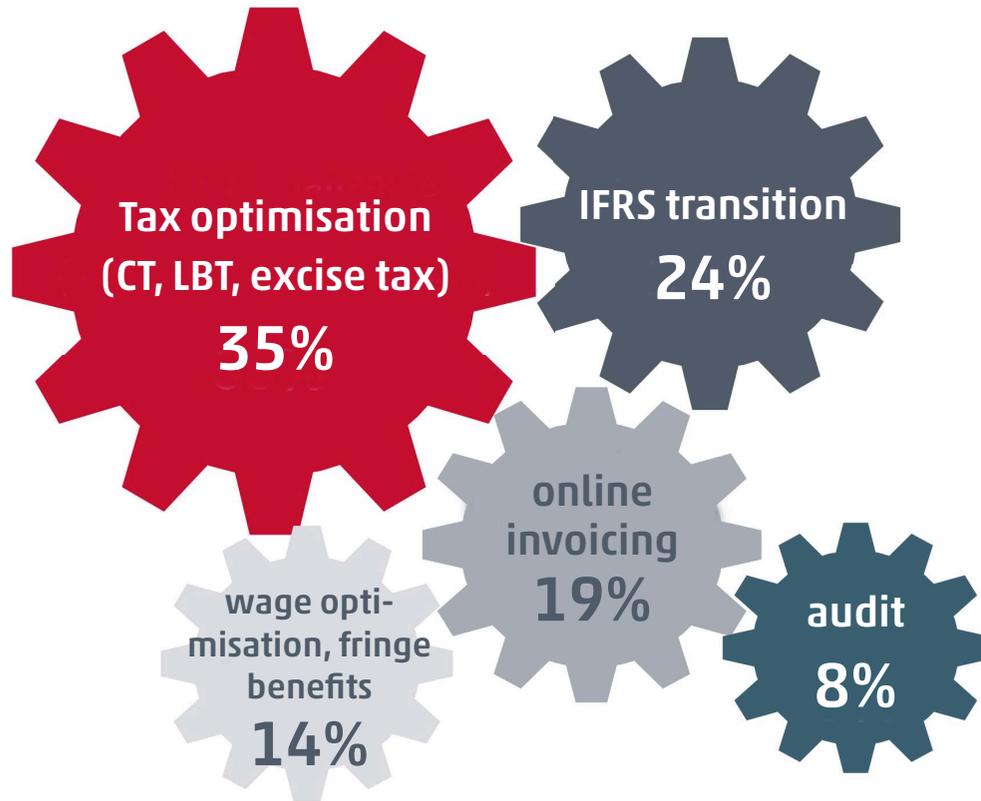
WTS Klient Research
First half of 2018

“Although we are still incapable of cloning employees, we can certainly assist you in optimising taxes and reducing expenses.”

Zoltán Lambert
WTS Klient, managing partner

Planned changes

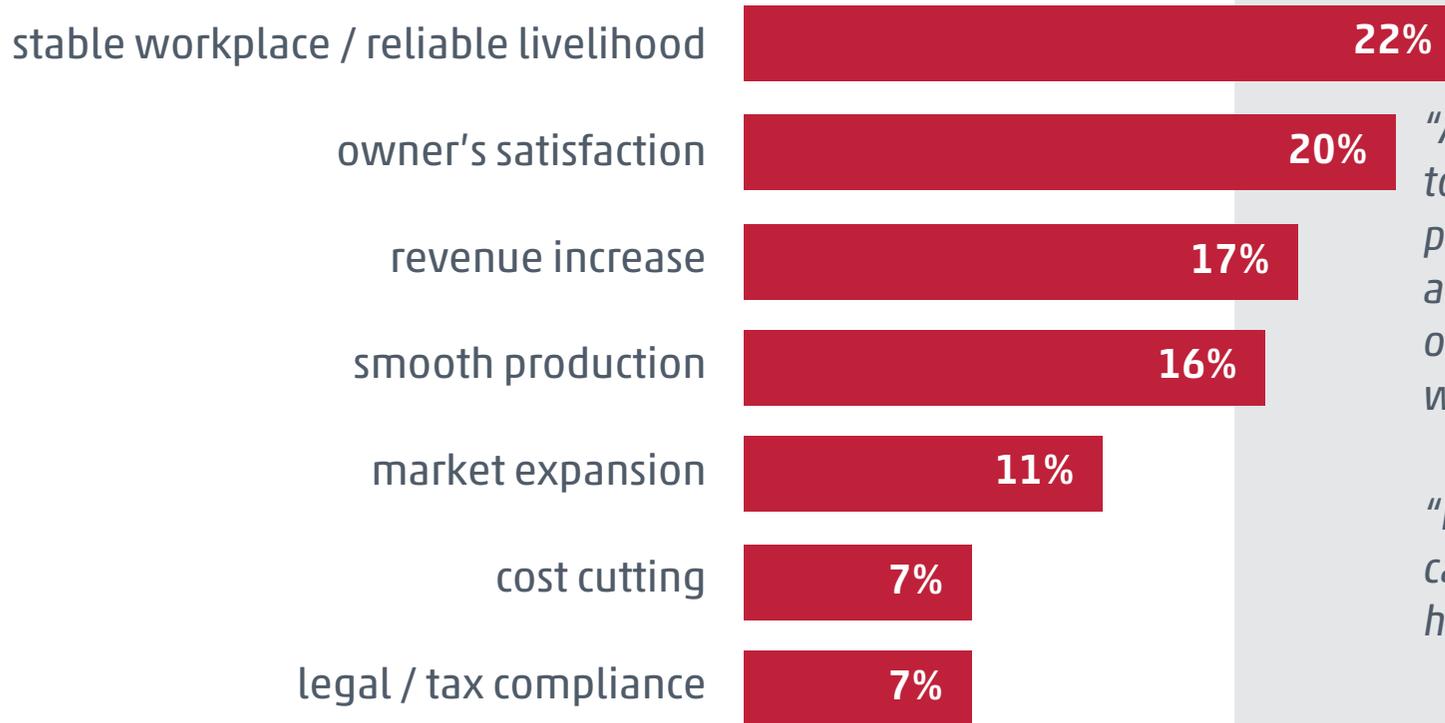
Which significant changes are you contemplating in your tax procedures, accounting and payroll systems?



"Tax optimisation is very important this year because it contributes to cost cutting, thus we can be more competitive in the region."

Satisfied employees, satisfied owners

What benefits are you expecting from realising your ideas?



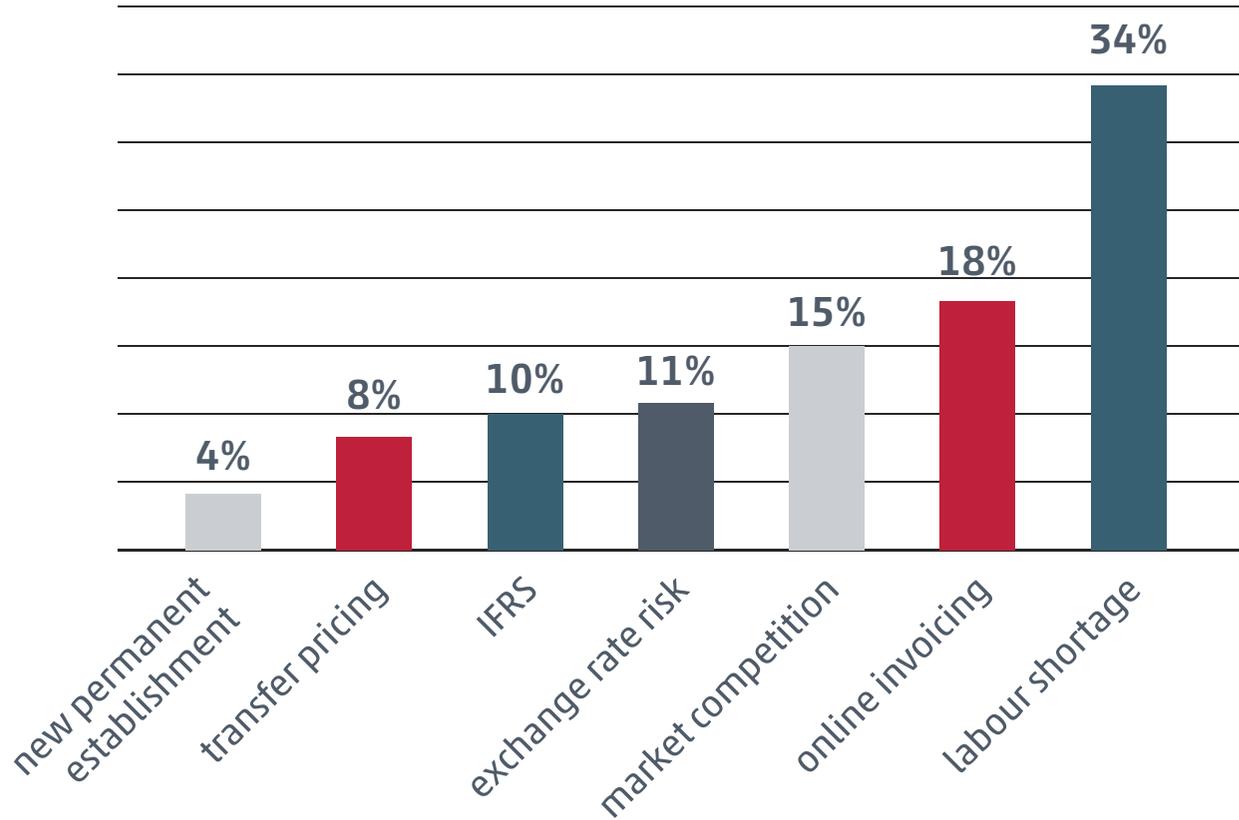
"If we find the right workforce, production will be smooth."

"A virtuous circle comes to fruition: if the company prospers, we will be more attractive as a workplace, our staff stay and production will grow."

"If we achieve the goals, we can ensure work and a livelihood for many families."

The greatest challenges in 2018

What challenges have you faced in connection with the goals set and the changes planned?



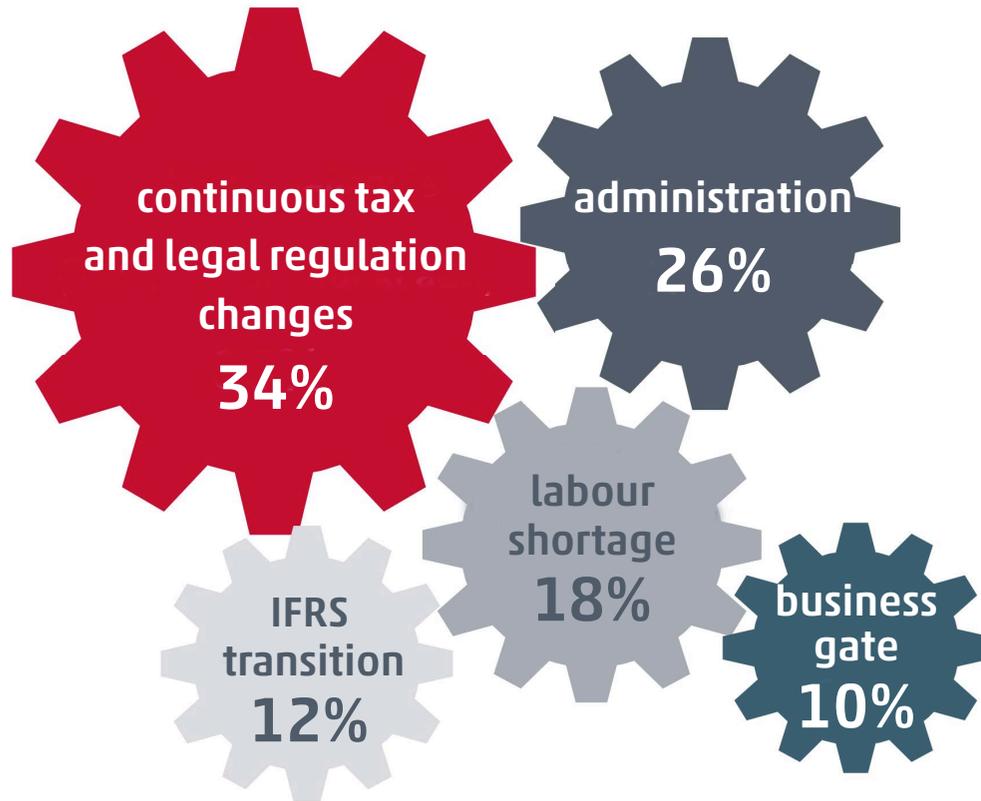
"We receive many orders. If we do not top up our workforce by the summer, we will have problems keeping to deadlines."

"We have posted the ticket to SAP, I hope they will be prepared on time."

"There are not enough qualified workers with foreign language proficiency."

5 most important obstacles

What legal and other obstacles have you identified in realising your goals?



"It is difficult to always keep up with the permanently changing Hungarian legal regulations and to comply with them."

"In Hungary, the administrative workload related to payroll is particularly high, this is why we chose an external service provider."

Value added by a consultancy firm

What is the main added value that a consultancy firm could give you?



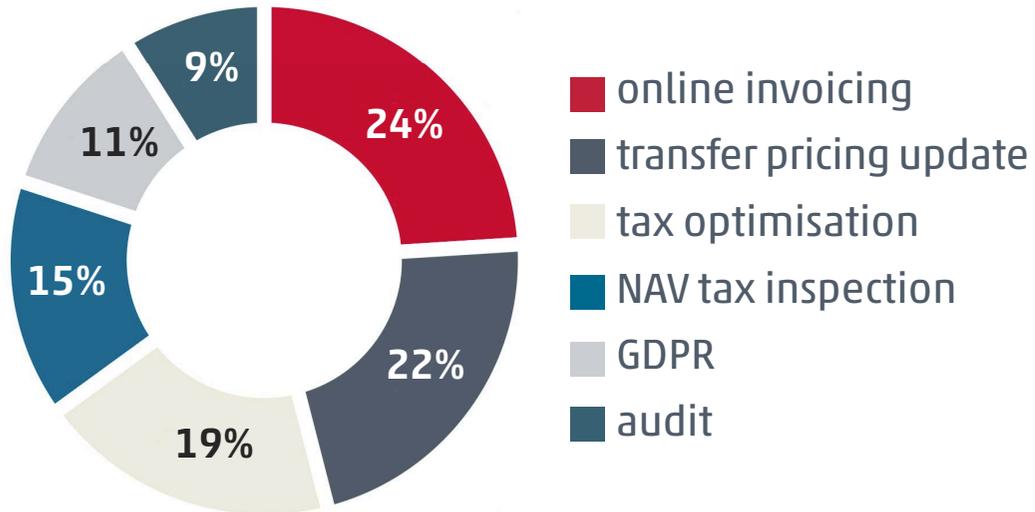
"It is good to know that an external expert confirms our decisions."

"We are good in transportation, someone else should be up to date in taxation."

"Thanks to our professional experience, we can realise our projects more smoothly, thus achieving our goals sooner."

How can a consultancy firm help you?

Would a tax consultancy or accounting service provider help with tackling any of the challenges?



“Updating transfer pricing documentation helps mitigate tax risk significantly.”

“It is possible for taxpayers to decrease their pre-tax profit with the amount determined based on the direct cost of research and development activity performed by a related company in its own sphere of activity.”

*“Some of the main tax-related findings of the research include issues of **online invoicing**, which will go live on 1 July 2018, the challenges related to **transfer pricing** documentation and inspections based on a new decree effective from 2018, as well as **tax optimisation opportunities** and the challenges of tax inspection risks.”*

Béla Kovács
WTS Klient, senior manager

WTS Klient Research
First half of 2018

Most important information and misconceptions about online invoicing 1

As our research pointed out, after the labour shortage, online invoicing will be the second biggest challenge for companies this year.

1

Mandatory from 1 July 2018

Mandatory data reporting shall only be applicable to the mandatory elements of invoices based on the rules known at the time of the research. Not everybody is well informed regarding this issue. There were companies in our survey who understood data reporting to be just the online forwarding of the amount on the invoice. This was not due to clients' lack of information, but rather to the fact that although we have long been aware of the new system, we could not report on any final status in the research phase. Indeed, the majority of the respondents are rather waiting for the final rules, having learnt from the situation where, compared to the end of 2017, they faced a newly planned concept and testing system in 2018.

2

Rollout costs

One of the most frequent criticisms of the system introduction related to costs. Similar to the introduction of the EKAER system it seems clear that the majority of taxpayers have to pay extra costs, and in the case of staff involved in invoicing they also expect increased working hours (some do not rule out having to recruit extra people if warning and error messages from the system cannot be managed otherwise).

"One important prerequisite of successful online data reporting is preparing our systems for the change in good time, we should not wait until 30 June."

"All taxpayers registered in Hungary are subject to the data reporting obligation, so this includes foreign – i.e. not Hungarian-resident – taxpayers registered for VAT."

Most important information and misconceptions about online invoicing 2

3

HUF 100,000 limit (roughly EUR 320)

Although online data reporting currently affects invoices including charged VAT of at least HUF 100,000 (roughly EUR 320), issued for transactions between domestic taxpayers, some of our respondents believe it would be easier if the data reporting covered all invoices. However, a significant number of the respondents already believe reporting the invoices within this limit is a big challenge.

4

Technical specifications difficult to understand

Another problem is that the technical specification of the data reporting is too technical (IT language) for finance directors and managers, and this cannot be managed without external help. It means that IT experts are always needed since the data has to be forwarded from the invoicing software to the NAV right after completion of the invoice, without human intervention.

5

Hungarian accounting software

The situation is exacerbated at companies where more than one invoicing software programme is used, possibly alongside handwritten invoices as well. For handwritten invoices the invoice data needs to be entered into the online platform within 5 days (in the case of invoices with VAT of HUF 500,000 (roughly EUR 1,600) or more: on the day after the issuance of the invoice). Relief may come for those working with Hungarian accounting software in that the software will likely handle online data reporting by default.

"The data structure of the data reporting is not integrated into the schedule of the invoicing decree, the NAV must publish a statement on this instead."

Most important information and misconceptions about online invoicing 3

6

Integrated invoicing software of parent company

Numerous respondents of the survey indicated that they use invoicing software integrated with their foreign parent company, and they are only users who have no higher-level technical rights. In these cases, compliance with online data reporting must be resolved in other ways as the system is expected to be launched, and taxpayers may face a default penalty of up to HUF 500,000 (roughly EUR 1,600) per invoice in the case of inadequate data reporting.

7

Warning & Error

Besides the opinions of clients, the tax consultancy team at WTS Klient found on many occasions that the data exporting function, which has long been obligatory, is not fully operational either. According to our tax consultants, perhaps the greatest problem and challenge is how warning and error messages received during individual cases of incorrect data reporting can be processed and managed.

8

Benefits of online invoicing

The majority of the companies participating in the research still do not view online invoicing positively, although the advantages communicated by the NAV can undoubtedly help businesses. The advantages include the database in which issued invoices can be queried by both the receivers and issuers of the invoices (trusting that information qualifying as business secrets can only be viewed by authorised parties, and the authorisations can be narrowed). Another positive result is that the new system will replace the aggregate data reporting of invoice issuers. One question that the companies surveyed are not dealing with yet is whether the NAV could prepare VAT returns instead of the taxpayers. In this respect, taxpayers would like to keep certain decision-making rights to themselves.

“Taxpayers using invoicing software will not be exempt from the data reporting obligation for reasons such as the program it uses was developed abroad.”

“Online invoicing will also replace the issuer’s item-by-item outgoing domestic summary report.”



“Transfer pricing is one of the unavoidable issues of recent times, it is a constant fixture in inspection guidelines, a target of Hungarian legislation changes, and one of the topics affected by the change in international laws.”

This trend is here to stay too: the experience of NAV inspectors gained during recent years and their increasing resources require a greater level of preparedness from companies and consultants.”

András Szadai
WTS Klient, senior manager

WTS Klient Research
First half of 2018

Transfer pricing – raising awareness of new rules 1

1 Default penalties may even amount to HUF 4 million (roughly EUR 12,700)

Transfer pricing has become a focal area of inspections recently, and this is not expected to change in the future either. While the emphasis used to be placed on the availability of the documentation and the threat of a default penalty if it was missing, today we more frequently see tax authority inspection reports disputing the applied prices and related tax penalties. This can amount to HUF 2 million (roughly EUR 6,400) per incomplete document, and as much as HUF 4 million (roughly EUR 12,700) in the case of a repeated failure to comply with the laws.

2 Foreign tax authority vs. NAV

The problem of transfer pricing arose frequently at the participants in our research. Many company managers do not know the new rules and rely heavily on the information received from their foreign parent company. At the same time, our experience shows that during Hungarian tax inspections it is not enough to present foreign documentation. The strictness of Hungarian inspections prompts many company managers to find a solution for the penalty risk that is independent of the parent company, and to use the assistance of a tax consultant. WTS Global's transfer pricing specialist team can find a solution for individual transactions. Some respondents indicated that in line with the BEPS action plan there is an increasing trend at parent companies where the foreign tax authority challenges the tax base and profit "left" in Hungary. However, the Hungarian tax authority does not give up on tax revenues easily either. To support tax inspections of this type, respondents always consider using tax consultants with an international background, and due to the mutual consultation process between the tax authorities of the two countries, they expect a lengthy process.

"Tax penalty can amount to HUF 2 million (roughly EUR 6,400) per incomplete document, and as much as HUF 4 million (roughly EUR 12,700) in the case of a repeated failure to comply with the laws."

"During Hungarian tax inspections it is not enough to present foreign documentation."

Transfer pricing – raising awareness of new rules 2

3

Master file & Local file

The respondents are not fully aware of the rules of the new TP decree that is valid from 2018. Based on the new transfer pricing documentation decree, from 2018 it is no longer possible to prepare independent documentation. This system has been replaced by one comprising two separate documents: the master file and the local file. Large corporate groups tend to prepare transfer pricing policies (or guidelines) at group level, describing related-party transactions from the perspective of the group as a whole. Preparing joint documentation was permitted based on the previous decree, but now, the master file and the local file have become mandatory elements of transfer pricing documentation.

4

Updating of financial data

The majority of clients have many questions regarding the frequency of updating financial data. For companies selected as comparables, it will suffice in the future to carry out database filtering every three years (the financial data of the companies used for the comparisons should be updated every year), provided that there is no significant change in the business activity over this time. The transfer pricing decree currently in force does not contain any such provision, and updating the financial figures of the compared companies can increase costs. This is because many firms did not deem it important to revise the data of the comparable companies, arguing that the market circumstances had not changed.

“Based on the new transfer pricing documentation decree, the master file and the local file have become mandatory elements.”

“Updating the financial figures of the compared companies can increase costs.”



“Tax optimisation is becoming riskier in light of the BEPS. The point is that tax inspectors should not be able to find any tax shortfall or levy penalties at companies.”

Tamás Gyányi
WTS Klient, partner

Tax optimisation – essential criteria 1

1

Development and projects

Tax optimisation is still a dominant topic among financial managers and managing directors. There are many opportunities to optimise tax burdens in the Hungarian tax system, but for lack of developments and projects, companies cannot take advantage of the development tax allowance, while bigger companies cannot utilise the SME allowances.

2

Company transformations

As for foreign-owned companies, the size of companies operating in Hungary is given, and is not essentially a planning tool, but many respondents indicated the possibility of a transformation. Transformations, changing a company's size, are on the agenda of many entities, i.e. whether operating several small companies or one big firm is optimal. In these cases it is not primarily the tax benefit that is the motivating factor, but the companies endeavour to utilise the legal opportunities inherent in the tax regime. Using losses is not as easy as it used to be, and for all transformations and tax optimisation it must be taken into account that the corporate tax act was also tightened up from 1 January 2017. If the main goal of a legal transaction is to achieve a tax benefit, then it cannot be enforced.

3

Fringe benefits

The respondents are aware of the management of taxation methods that are more favourable than wages (e.g. fringe benefits, range of PIT-free benefits). There are various reasons for not using this in practice. The extent of the tax benefit and the disproportionate administration associated with it can be a deterrent in the case of a specific profit or number of staff.

“The Act on Corporate and Dividend Tax as well as the Act on Duties offer tax allowances if preferential transformations are chosen and the conditions are met.”

“For reported shares, the devil is in the details.”

Tax optimisation – essential criteria 2

4

Donations for sports and performing arts

The majority of the companies surveyed were aware of the tax benefits of donations for sports and performing arts. However, tax donations were not made by many, otherwise very profitable companies to support sports, films or performing arts organisations, not even in the simpler tax donation regime. We found comments among the reasons that are worth being considered by legislators. Companies in German ownership in particular would be more willing to offer their taxes for education or healthcare purposes.

5

The key person program

The key person program has been on the agenda of an increasing number of companies. In addition to tax-free benefits, the possibility of an ESP (employee shareholder program) also arises, where the business entities participating in the survey would use the assistance of a tax consultant and a law office in each case.

6

Tax inspections

The need for the support of a tax consultant is also an important issue during tax inspections. In our experience the majority of clients increasingly choose deliberate and planned tax consultancy support instead of ad-hoc help to put fires out later on. With this help, finance managers and managing directors feel more comfortable during tax inspections, they are aware of the risk areas and encounter fewer surprises.

“Fringe benefits are still tax-efficient alternatives to wages.”

“Local business tax is the third largest income-generating tax after sales taxes and personal income tax at the level of the national economy.”

Thank you!

A special thanks to our partners who participated in the research, who spent their time and energy going through our questions and responding to them either verbally or in writing.

Each conversation was a great experience for us, and we are thankful for their openness and trust.

Should you have any questions regarding our research, please get in touch.



If you wish to participate in the 2019 research and would like to be among the first to get information on the challenges international companies face in Hungary, as well as their solutions, please contact us at the following email address: info@wtsklient.hu or on the following phone number: +36 1 887 3744.

After the evaluation of the results, the participants of the research will be invited to a small-scale interactive workshop where they will have an opportunity to discuss any of the tax and financial or legal issues they face with our consultants.

WTS Klient

H-1143 Budapest • Stefánia út 101-103.

Telephone: +36 1 887 3700 • Fax: +36 1 887 3799

info@wtsklient.hu • www.wtsklient.hu

- » Tax consulting
- » Financial advisory
- » Legal consulting
- » Accounting
- » Payroll

