

Tax Newsletters

Local Business Tax



Increased attention to the local business tax!



Sándor Szmicssek

It is expected that the subsidy received by local authorities from the central budget will be decreased by HUF 200 billion next year. Local authorities will do everything in their power to increase their revenues from other sources. For this reason, and also due to the new regulations entering into force in 2010, the thoroughness and frequency of tax audits is likely to increase.



Zsolt Nyári

The statutory background

In accordance with Article 39 of Act C of 1990 on local taxes, in case of pursuing business activity of a permanent nature, the tax base is the net revenue less

- the acquisition costs of goods sold,
- the cost of services intermediated, and
- the cost of materials.

Establishing the tax base may appear simple at first sight; however, ensuring compliance with the administrative requirements necessary for deducting the cost of intermediated services or deciding what indeed qualifies as the cost of materials can be problematic in many cases.

Under the law, the condition for deducting the cost of intermediated services, (Article 52, item 40) is that:

- the possibility for intermediation is apparent from the contract with the customer, as is also the actual fact of the intermediation from the invoice; and
- in case of performance by a subcontractor, the tax subject has an engagement contract in accordance with the Civil Code for the performance of services with both the customer and its subcontractor.



Problems in practice

Unfortunately, in practice it often happens that the tax subjects do not or only partly satisfy the administrative conditions specified above (e.g. the fact of intermediation is apparent in the contract, but not in the invoice). In addition to the administrative conditions, however, the concept of intermediated services must be satisfied from a substantial point of view as well. If a third party is involved in the transaction whose performance is integrated into the service rendered to the customer, then we cannot talk about an intermediated service, even if the invoice otherwise satisfies the administrative conditions. Intermediation, therefore, means in all cases that the services received are passed on in an unchanged form. In the course of tax audits, a typical debated point is the issue of intermediation in an unchanged form, and the findings of many tax audits are submitted to court due to such debates.

If the required conditions are not satisfied in full, then we can be certain that the tax audit will question the legitimacy of the tax base reduction, even if the substance of the transaction is intermediated service or performance by a subcontractor.

Unlike in the case of intermediated services, the deduction of the costs of materials from the tax base is not so much subject to administrative conditions; however, the proper classification of the individual costs can pose difficulties in many cases. Examples include sewage service fees, which are to be treated as services used, or protective clothing, which are to be handled as material costs. In addition, it also often happens that certain items are not posted to the correct cost centre.

It should be noted that local authorities also have the right to audit the local business taxes if the given period qualifies as being closed by way of a tax audit with respect to other taxes. Therefore, in addition to the correct classification of costs and the administrative tasks, special attention should be devoted to the question of whether an earlier audit by the tax authority has any findings that may also have an effect on the amount of the local business tax.

Although the consequence of failures is “only” 2%, as a result of several years’ of wrong practice, the tax authority may also find a tax shortfall of significant amount. For this reason it is advisable that the relevant contracts, invoices, records and earlier decisions of tax authorities be checked as soon as possible and, if necessary, the corrections be made.

New regulation

It is important to call attention to the fact that in 2010 the task of collecting and auditing the local business tax will be transferred from the local authorities to the Hungarian Tax Authority (APEH). Pursuant to the related transitory regulation, the right of levying taxes for tax years preceding 2010 will expire on 31 December 2011, which is partly good news, since the statutory limitation period will be shorter; however, it is likely that the frequency of tax audits will be increased, since this situation will motivate the tax authority to examine the periods not yet closed with an audit as soon as possible. Therefore, it is highly advisable to pay more attention to the local business tax than before.

Should you have any question about the topic discussed in this Newsletter, we are always happy to be of service.

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