

Examiner's report

F6 (HUN) Taxation

June 2015

General Comments

There were two sections to the examination paper and all of the questions were compulsory. Section A consisted of 15 multiple choice questions (two marks each) which covered a broad range of syllabus topics. Section B had four questions worth 10 marks each and two longer questions worth 15 marks, each testing the candidates' understanding and application of Hungarian taxation in more depth. This is the first examiner's report since the introduction of the new exam format and question types. The following paragraphs report on each section and focus on some of the key learning points.

Specific Comments

Section A

It was very pleasing to see that all candidates attempted all of the questions. Section A questions aim to provide a broad coverage of the syllabus, and future candidates should aim to revise all areas of the F6 (HUN) syllabus, rather than attempting to question spot. The following question has been reviewed with the aim of giving future candidates an indication of the types of questions asked, guidance on dealing with exam questions and to provide a technical debrief on the topics covered by the specific question selected.

Sample Question for Discussion

Ibolya is a private individual. She gives accounting advice occasionally, and the basis for the payment for the services provided is a contract of services (megbízási szerződés). In 2014 Ibolya recorded fuel expenses in her mileage records for engagements on the following dates:

- 15 April 2014
- 23 May 2014
- 22 July 2014
- 25 July 2014
- 1 November 2014.

Ibolya deducted no other expenses in relation to her private car in her personal income tax return for 2014.

In which months of 2014 did Ibolya have a liability to pay company car tax?

- A In May, August and December
- B In May, July and November
- C In April, May, July, and November
- D In May, June, August and December

This question tested the application of company car tax. Company car tax is payable if anybody (corporations or individuals) deduct expenses in their tax return in relation to a company car. Candidates must know that in the case of private individuals the tax obligation commences on the first day of the month following the month in which expenses in relation to the car were deducted. Tax obligation terminates on the last day of the last consecutive month in which expenses were deducted.

Applying this rule the first month of obligation is May as expenses were deducted in April 2014. The next month when expenses were deducted is May which is a consecutive month but since no expenses were deducted in June this is the last month of obligation for this period. Using the same logic for the July expenses the month when tax is payable is August, and in case of the November expenses December will be the month when payment obligation arises.

This example shows that candidates are not only required to learn the tax rules but they also must be able to apply the rules correctly.

The correct answer was A.

Section B

Question One

This 10-mark question covered the topic of value added tax (VAT).

Part (a) for three marks required candidates to list any six compulsory elements of a VAT invoice. Candidates' performed extremely well on this question, with the vast majority of candidates able to gain maximum marks.

Part (b) for seven marks required candidates to calculate the VAT balance of a company for February 2014. Many candidates performed well on this requirement, with some candidates achieving full marks.

Most candidates correctly stated that for the translation services provided by a German company the place of performance is Hungary, in other words, this is an 'import service' so VAT is payable and deductible at the same time in the same VAT return. However, there were a number of common mistakes which are discussed below.

A frequent mistake was observed in relation to the marketing services provided to a Slovak company by the Hungarian entity. In the case of marketing services (expert services), if the service is provided to a buyer subject to VAT the place of performance is the registered seat of the ordering party, i.e. Slovakia. This means that this is an export sales revenue which is zero rate, so no VAT is payable in Hungary. Some candidates calculated the VAT payable as if it was a domestic sales revenue which is incorrect.

Some candidates struggled to establish the date of performance in relation to the accounting services. For the accounting services the date of obligation is the due date of the invoice so the January invoice with a due date in February was relevant for the February VAT return.

The mobile phone invoice also presented some difficulty for a number of candidates. Since employees of the Hungarian entity are not obliged to separate private and business calls, and they do not need to reimburse any private usage, the assumed private usage of 30% is applicable resulting in deductible VAT of 70% of the total VAT amount. Some candidates calculated with a deductible VAT of 80% which is incorrect.

Question Two

Part (a) of this 10 mark question required the calculation of the local municipality tax liability of a Hungarian company. Performance on this question was mixed. Most candidates recognised that the net sales revenue of Xilo Kft was above HUF 500 million and therefore a regressive portion of cost of goods sold and cost of mediated services should be deducted from the tax base. Candidates who failed to score good marks simply deducted cost of goods sold and cost of mediated services in full from the sales revenue rather than calculating the deductible portion as per the tax law.

Another source of error for a number of candidates was that they added other revenue and financial revenue to the tax base, and typically these candidates reduced the tax base by the cost of other services, cost of labour, other expenses and financial expenses. These items are not relevant when calculating the local municipality tax base.

In part (b) of this question candidates had to explain how local municipality tax advances are paid, stating the deadlines for the advance payments.

This requirement was not well answered by the majority of candidates. Although most candidates were able to correctly identify that there are two advance payments dates per annum they were unable to correctly specify the deadline dates of 15 March and 15 September.

Even those candidates that did not have problems with the deadlines struggled to explain the amount of advances payable. The September advance payment is the difference between the prior year's liability and the current year's March advance payment. The March advance payment is 50% of the prior year's local municipality tax liability. Some candidates assumed that equal amounts are paid in both cases, simply taking 50% of the prior year's liability.

Many candidates missed out on the marks available for stating that taxpayers are obliged to make a balancing payment for local municipality tax liability by 20 December if they are required to do so for their corporate income tax liability.

Question Three

This 10-mark question covered the topics of taxation of companies registered for simplified taxation for small entrepreneurs (EVA).

Part (a) for six marks required the calculation of net dividends that can be distributed to the owners of a company registered in the EVA-regime. The level of answers was again quite mixed. Approximately half of the candidates were able to apply the principles of EVA correctly, i.e. EVA of 37% is payable on the gross sales revenue and no VAT can be reclaimed by these entities.

The other half of candidates, however, were quite confused about how EVA works. Many thought that EVA is payable in a similar way to corporate income tax, and incorrectly subtracted expenses from the revenue and applied the 37% on this "tax base".

This part of the question also contained company car tax payable. It was pleasing to see that the majority of candidates were able to correctly compute the company car tax based on the engine capacity and the environmental category, however, only a minority demonstrated understanding that car capacity tax is deductible from the company car tax.

Part (b) was a two mark question requiring candidates to calculate the EVA payable where sales revenue exceeds the HUF 30 million limit. If the sales revenue (including VAT) exceeds this limit, the excess amount is taxable at 50%. A large number of candidates did not know this rule and were unable to calculate the EVA payable.

Part (c) examined the rules governing the frequency and deadlines of the EVA-advances. It was disappointing to see that only a small number of candidates were able to set out these rules effectively. EVA-advances are payable quarterly and for the first three quarters the deadline for payment is the 12th day of the month following the end of the quarter. A lot of candidates mistakenly stated that the deadline is the 15th or 20th day of the month following the end of the quarter, others thought that advances are payable twice a year – this is perhaps an application of the local municipality tax advance rules instead. Also only a few mentioned that the fourth quarter balancing payment is due on 20 December where the payment is based on the total expected annual liability. Even fewer stated that the deadline for the annual EVA-return is 31 May of the year following the tax year. The question included a Kft and this type of entity must always keep their records according to the rules of the Act on Accounting (they cannot opt to apply the simplified revenue-based record keeping rules).

Question Four

This 10-mark question covered the topic of development relief.

Part (a) for four marks required an explanation of the SPECIAL qualifying criterion the company in the question will have to meet in order to claim the development relief in 2014 and in the subsequent four years. Many candidates did not read the question carefully and explained the general qualifying criteria instead of the special ones. Those, however, who explained the special criterion usually scored very high or maximum marks.

Part (b) for six marks required the calculation the maximum relief available to Devorient Kft and its corporate income tax liability for 2014 taking into account the development relief. Candidates were generally able to correctly calculate the relief and the income tax liability. One common mistake, however, was that instead of using the limit for the relief which is 80% of the calculated tax as stated in the tax law some candidates used a 70% limit.

Question Five

This 15-mark question focused on the corporate income tax regulation for commercial companies.

Part (a) for four marks required the explanation of the rules for using tax losses incurred in 2013 or later. This part of the question was answered well, only a few candidates confused the rules applicable for 2013 losses with rules in force previously.

Part (b) for 11 marks was a computational question where the calculation of the corporate income tax liability of Horizon Zrt needed to be performed for the year 2014. This part of the question was answered very well by most candidates. They were able to identify the tax base by correctly identifying the increasing and decreasing items so many scored excellent marks.

Candidates that lost marks made the following mistakes:

- Incorrectly calculating the accounting and tax depreciation because it involved a simple time-apportioning element. Several candidates also incorrectly treated the accounting depreciation as a decreasing item and the tax depreciation as an increasing item, as the converse is the appropriate treatment.
- Not recognising that in case of impaired debts the limit of the tax base reduction is the amount of impairment recognised. So even if 20% of the receivables outstanding for more than 365 days is a tax base reducing item, if the impairment actually accounted for is below this limit then only the actual impairment recognised can be considered when reducing the tax base.
- Failing to realise that the reversal of impairment losses on non-current assets is a tax base reducing item. Some candidates mistakenly considered it as an increasing item which is not the case.

Question Six

This 15-mark question covered several aspects of personal income tax and the social security contributions payable on benefits in kind.

Part (a) for eight marks required a calculation of the total personal income tax liability of Mr Szalai, a private individual. Performance on this question was satisfactory.

Many candidates were able to correctly classify the different types of income within the consolidated tax base. Income from supervisory board fees seemed unfamiliar to many candidates many did not know how to treat this type of income. Surprisingly quite a few candidates overlooked the information that this income was only received from 1 July 2014 so only 6 months were relevant.

A common mistake in this requirement was treating the interest from a controlled foreign corporation wrongly. This type of income should be classed as 'other income'. Since the Hungarian tax rate is a flat 16% for most types of income this did not result in an inappropriate tax payable but classification is also an important aspect of personal income tax law.

It was pleasing to see that most candidates were able to correctly calculate the tax on income taxed separately (capital gain).

Part (b) addressed three different types of benefits in kind and their taxation. Candidates had to calculate the personal income tax and social security and/or health care contributions payable by a private individual or her employer in respect of the three items. This area of the syllabus is regularly examined so it was rather surprising that the performance of candidates was poor in many cases.

The first item was the internet service of the private individual paid by her employer. This is a non-salary related non-defined benefit in kind so it is taxed on the individual as part of the consolidated tax base. This item was predominantly well answered. Some candidates "grossed up" this item by 19% but this was not necessary and resulted in an incorrect numerical solution for the tax base.

The second and third items, however, were less well answered. Meal vouchers (not exceeding HUF 12,500 per month, usable in the workplace only) are salary related benefits in kind and tax is payable by the employer only. The tax base is 119% of the amount and personal income tax of 16% as well as health care contribution of 14% is payable on that. Some candidates incorrectly used a 27% health care contribution rate.

The third item, namely the food relating to a business trip reimbursed by the employer is a defined benefit in kind so the benefit is taxed on the employer as follows: personal income tax of 16% and health care contribution of 27% are payable. Some candidates thought that this item was part of the salary of the private individual, others were confused which rate of health care contribution to use here and applied a rate of 14%.

Candidates are strongly encouraged that they learn the classification and taxation of each item of benefit in kind since they form an important part of this exam.