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# Tax News+

**Below you will find the tasks and potential issues arising from key tax law changes of the past month and recent weeks. We would be ready and glad to discuss with you any of your company specific issues.**

## **The social security treaty (Treaty) between Hungary and the United States is waiting for ratification**

The future insurance obligations and eligibility for benefits (primarily pension benefits) of those who are employed or self-employed in Hungary and the United States or are subject to the social security regulations in both countries are beginning to take shape based on the new social security treaty between Hungary and the United States (Treaty).

The bill issued by the Ministry of Human Capacities is currently awaiting approval. The entry into force of the Treaty requires ratification by the United States of America as well. The ratification of similar treaties dealing with social security and concluded by the United States took several years in certain cases. Currently, the date when the Treaty enters into force is unknown.

If the Treaty does not come into effect prior to 30 June 2015, then it must be examined whether US citizens who have been working in Hungary on assignment (secondment) for several years will be subject to the Hungarian insurance obligation after 1 July 2015, or whether the Parliament will pass an amendment to continue to provide exemption from the Hungarian social security obligation to persons from third countries on assignment in Hungary if certain conditions are met.

Key points of the bill (the Treaty):

- The Treaty applies not only to Hungarian and US citizens, but also to any person who is or has ever been covered by either the Hungarian or the US social security system or is entitled to benefits under the relevant regulations.
- In terms of benefits, the Treaty only covers pension and other cash benefits and does not regulate issues concerning in-kind benefits (such as medical care).
- Under the general rule, employed persons will be insured in the country where they work, with the exception of situations in which that person temporarily works in the other country as part of a foreign assignment. In such cases, the employee would remain insured by the home country and, at the same time, would be exempted from social security obligations in the host country.
- Temporary activities include those whose duration is not expected to exceed 5 years. Such a 5-year period would have to be calculated from the date upon which the Treaty enters into force.
- The employee and the employer may file a joint request in order to request that the employee remain insured in the home country even after the 5-year period, without being subject to any time limitation.
- Separate rules regulate the aggregation of the years of service and insurance periods required for the provision of cash benefits:
  - The general rule is that the insurance period earned in the other country may be taken into account if the person requesting benefits has not yet earned the insurance period necessary for eligibility for benefits in the given country.
  - An important condition is that if the benefit is linked to the earnings or contributions paid during the insurance period then, under the Treaty, the authorities are required to take into account the insurance period earned in the other country, but not the earnings or contributions paid in that country.
- The most important aspects of the benefits are as follows:
  - Under the Treaty, eligibility for benefits only applies after its entry into force. Previously awarded benefits (e.g. old-age benefits) cannot be revised with a view to the entry into force of the Treaty.
  - Benefits may only be paid by both countries in their own currency.

### Increasing focus on the business purpose of related party transactions

The Hungarian tax authority is increasingly focusing on the business purpose of the taxpayers' operation, with special regard to the related party transactions. If a company fails to appropriately support the business purpose and completion of a related party transaction, then multiple negative tax consequences may be triggered. In a negative case scenario, the tax authority may set forth that the company is obliged to increase its corporate tax base under two titles simultaneously as a result of a given transaction. In addition, the deductibility of the VAT indicated on the received invoice may be challenged. This approach may have a critical effect in the case of purchasing management services in a significant amount. As a result, companies should be prepared for potential questions from tax inspectors in this regard by means of gathering the underlying business reasons and supporting facts.

Certain taxpayers already focus on gathering the aforementioned supporting documentation in a timely and structured manner. Furthermore, Deloitte has provided professional assistance to its Clients in several cases in the preparation of a "defence file" which serves to support the deductibility of the incurred costs, including completion and business purpose of the given transactions.

In this respect, we note that detailed transfer pricing documentation may assist the company in avoiding deductibility issues. However, a standard transfer pricing documentation may not be sufficient to support the deductibility of costs. This is based on the fact that transfer pricing documentation generally sets forth the given transaction from the perspective of the party providing the services.

Based on Deloitte's experience, numerous companies only recognize the relevance of the abovementioned issue during the course of a tax audit carried out several years (potentially 4-5 years) following the completion of the transaction, facing difficulties in gathering all the documentation supporting the completion of the given transaction due to strict deadlines for providing the requested information as well as due to the potential change in the professional staff once involved in the given transaction.

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