

Investing Guide Hungary 2014

Why invest in Hungary?

A guide with useful
information and inspiring
success stories of
investors in Hungary.



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Partner letter



The Hungarian economy may gain new momentum this year from initial growth in Europe and expanding investment activity.

This year promises to be exciting for both the Hungarian and the world economy. The economic events of the past years have put corporations' adaptability to the test. Companies have been focusing on cost optimisation, realignment, and the re-interpretation of new challenges and growth potential. In Hungary, last year already conveyed an important message: the Hungarian economy has found its way back to balance, which is the basis for growth. The Hungarian economy may gain new momentum this year from initial growth in Europe and expanding investment activity. GDP might increase by more than two percent, which offers favourable opportunities to foreign investors. This country is still an attractive target market for foreign working capital. This is well proved by the development of manufacturing investments, for example. Crisis

has barely affected this sector. Therefore, capital inflow is still strong, especially to industries related to automobile manufacturing.

We are publishing the Investing Guide Hungary for the fourth time, in co-operation with the Hungarian Investment and Trade Agency (HITA). We hope that our publication provides you with useful information and an extensive insight into Hungary's economic developments.

Best regards,

TAMÁS LŐCSEI
Service Line Leader
Tax and Legal Services

I. What should you know about Hungary?



1. LOCATION AND CLIMATE

Hungary's central location makes it a favourite destination for foreign investors who intend to expand their operations in Central and Eastern Europe. The country's telecommunications, transport and logistics infrastructure, and the quality of education and life have attracted large amounts of foreign investment to Hungary in recent years. The capital, Budapest, is the center of the country's economic activity; however, the main cities are also gaining an increasing role.

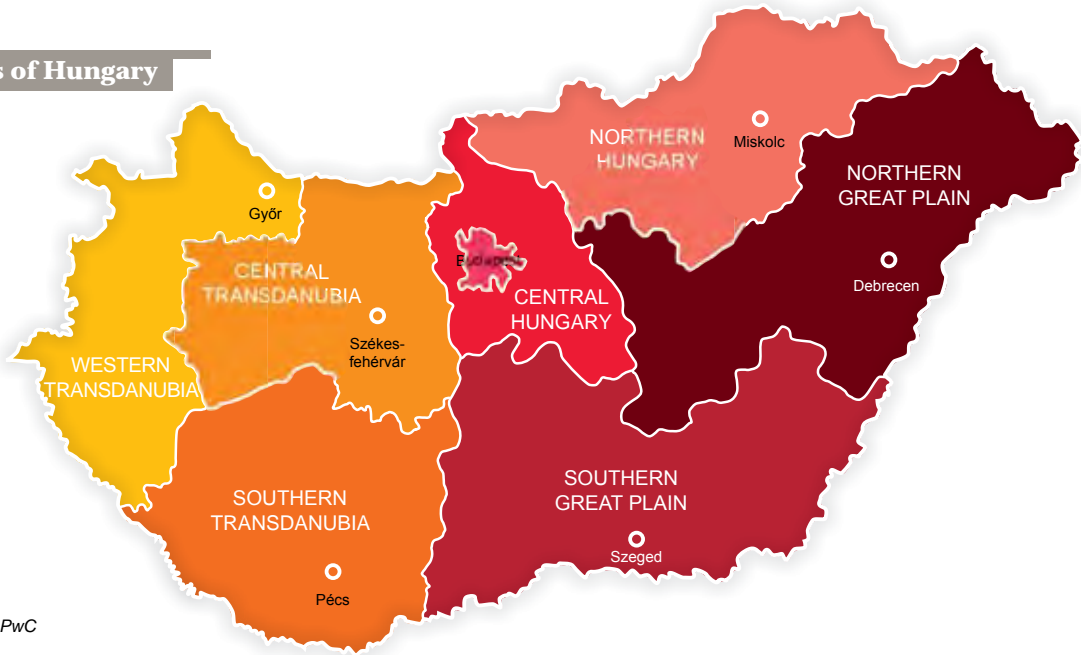
The country's favorable geographical location places it at the crossroads of main commercial routes. From

Hungary, a market of some 250 million people can be reached within 600 miles (about 1,000 kilometers).

EU accession in 2004 brought both commercial and regulatory advantages. Becoming an EU Member State brought a free trade system, the free movement of goods, services and labour, as well as capital.

In addition to all these advantages, another of Hungary's strengths is its well-qualified labour force. Due to the high standards of its education system, the country has a highly skilled and talented workforce, with professional foreign language skills and relatively low wage requirements.

Regions of Hungary



Source: PwC

2. INFRASTRUCTURE
IN HUNGARY

Road transportation

Hungary has a central location in Europe, at the crossroads of four main European transportation corridors, including:

- No. IV from northern Germany/ North Sea to the Black Sea;
- No. V from the Adriatic ports to Kiev-Moscow;
- No. VII – the Danube River and Rhine-Main canal, from the North Sea; and
- No. X the north-south corridor from the Baltic states to Turkey and Greece.

The largest Hungarian cities – Debrecen, Nyíregyháza, Miskolc, Kecskemét, Szeged, Pécs, Győr and Székesfehérvár – are all connected to the capital city, Budapest, by motorways (motorway total: 1,099 km).

Hungary has one of the highest motorway densities in all of Europe and the third highest road density, after Belgium and Holland. Highways reach the borders of the country and the different regions of Hungary. Neighbouring countries are, therefore, easy to access.

ECONOMIC DATA
AND OUTLOOK:

GENERAL INFORMATION

Location: East-Central Europe
Time zone: GMT+ 1 hour
Population: 9.909 million (2013)
Participation in international organizations: United Nations, NATO, European Union, OECD, IMF, Visegrád Group, Organization for Security and Cooperation in Europe (OSCE), Conseil Européen pour la Recherche Nucléaire (CERN), Duna Committee, Schengen Agreement, World Meteorological Organization, Bank for International Settlements, International Atomic Energy Agency, Wassenaar Arrangement on Export Controls for Conventional Arms and Dual-Use Goods and Technologies
Main industries: automotive, electronics, pharmaceuticals, ICT, food
Currency: HUF (forint)

ECONOMIC DATA

Labour force: 4.419 million (2013 Oct-Dec)
Employment: 4.015 million (2013 Oct-Dec)
Unemployment rate: 9.1% (2013 Oct-Dec)
Gross domestic product (USD, PPP/capita): 21,456 (2012)
Consumer Price Index: 1.7% (2013)
Inward foreign direct investment: USD 13.73 billion (2012)



The financial crisis has led to a slowing in foreign direct investment, not only in Hungary but also in other Central and Eastern European countries. In spite of this, Hungary continues to occupy a leading position in this regard. Based on the third-quarter figures for last year, Hungary's total FDI volume was EUR 76.4 billion, which, as a ratio of GDP, was the highest in the region, and, on a per capita basis, the second highest. Some 76.4 percent of all direct capital investments implemented in Hungary originate from the member states of the European Union, and 24.9 percent of this total comes from Germany.

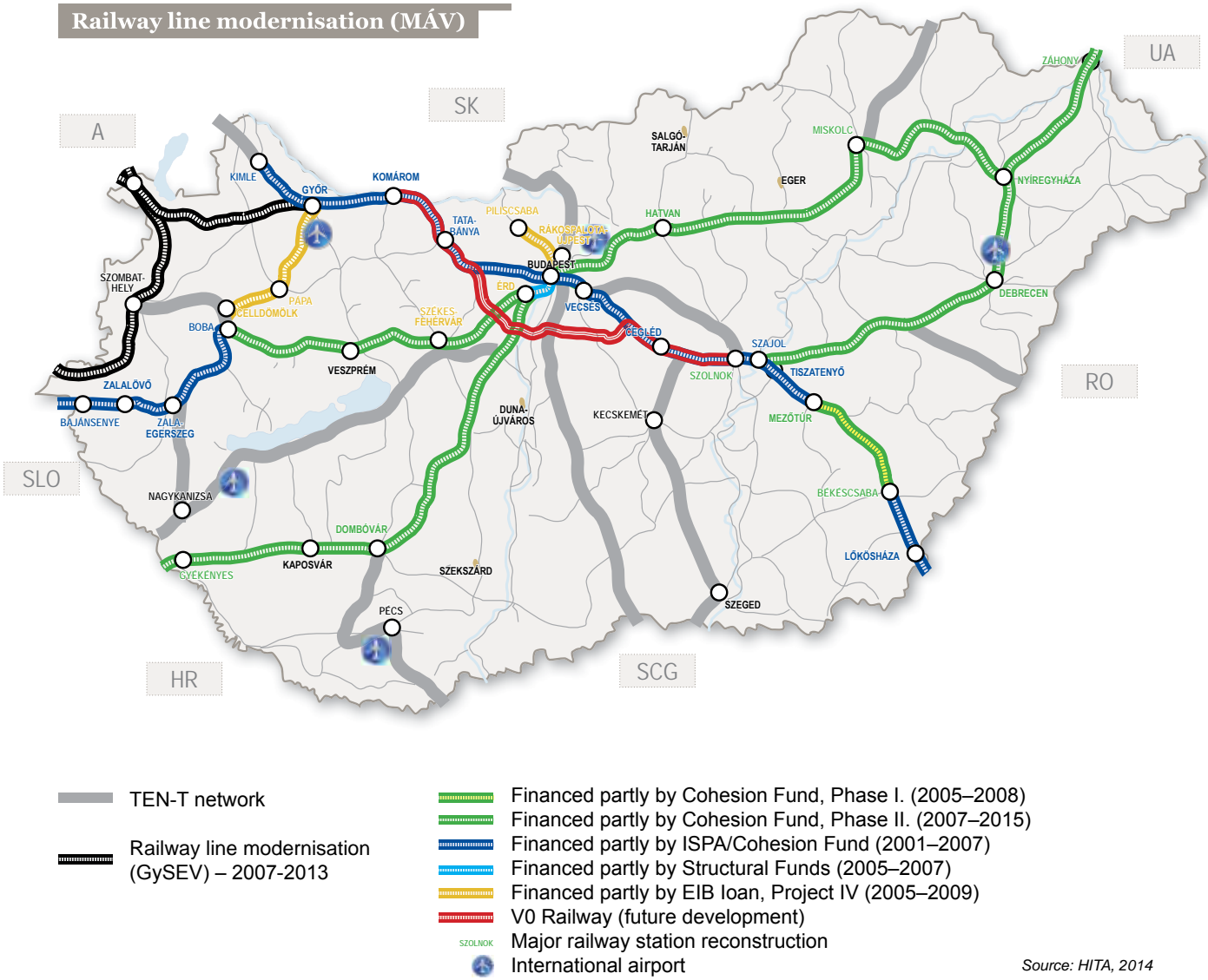
Based on the total number of foreign greenfield investments in Hungary, the percentage of those implemented in the Hungarian manufacturing sector was 37 per cent in 2011 and 2012, while last year this share jumped to 46 percent.

Motorway network in Hungary



Source: HITA, 2014

Existing
Future development



Railway transportation

Due to its central location, Hungary has an extensive railway network. Rail transport carries more than 20% of total freight, which is well above the EU average. Several main train lines connect Hungary with the main ports of Western Europe (e.g. Hamburg (D), Bremerhaven (D), Rotterdam (NL)) and the Adriatic (Koper (SI), Trieste (I)) with regular services.

The total length of the Hungarian railway system is 7,729 km, of which double-track is 1,335 km (17.3%) and the electrified railway network

is 2,628 km (34%). Záhony and its region is the junction and reloading center for European standard-gauge railways and the wide-gauge system of the CIS states. There is a direct railway connection between China and Záhony; the transfer takes approximately 19 to 22 days.

Air transportation

Hungary has a number of international airports: Budapest Liszt Ferenc International Airport, Debrecen, and Balaton – Sármellék. There are also airports that cater

for commercial and seasonal public flights in Győr and Pécs.

Water transportation

Hungary has excellent waterway connections, as the Danube crosses through the whole country from north to south. The Danube-Rhine-Main canal in Europe links the North Sea and the Black Sea: several scheduled block train lines connect Hungary with the seaports of Hamburg, Bremerhaven, Rotterdam, and Antwerp on the North Sea, and with Koper and Trieste on the Adriatic. The Adriatic seaports also



offer alternative shipping routes from Asia. Lead times from these ports are within 16-36 hours.

Industrial & logistics market

Hungary's geographical advantages make it a popular logistics location. The country is already a strategic location for many international distribution centers, and offers many advantages for companies that wish to develop their logistics centers here in the future.

Due to its infrastructure and central position, large-volume

The country is already a strategic location for many international distribution centers, and offers many advantages for companies that wish to develop their logistics centers here in the future.

development activity and transactions are concentrated in the vicinity of Budapest. To date, more than 30 modern logistics and warehouse parks of approximately 1.6 million square meters have been developed in a 30 kilometer radius around the capital, primarily along the M0 ring road. More than 200 industrial parks exist for greenfield or brownfield investment opportunities countrywide.

Logistics activities are the most often outsourced services in Hungary and the sector accounts for up to 5-6% of Hungary's GDP.



3. OFFICE MARKET

There are currently around 3.2 million square metres of office space on the Budapest office market, including owner-occupied buildings. The volume of modern owner-occupied buildings – properties built or renovated after 1989, excluding government-owned buildings – is estimated at 600,000 square metres. Modern office space

built as speculative investments in Budapest comes to about 2.6 million square metres. The majority of this (~70%) is Class A quality.

The Hungarian office market is focused predominantly in the capital city, although some modern office space has also been built in the biggest regional cities.

Vacancy level decreased in 2013 in every submarket of Budapest. By the end of third quarter of 2013 overall vacancy rate on the market of leased offices was slightly below 23%. (In the third quarter of 2012 the vacancy rate for offices built on a speculative basis came to 26%. At the end of 2007 the all-Budapest vacancy rate was around 12%.) Development activity and therefore new supply was limited in recent

The Hungarian office market is focused predominantly in the capital city, although some modern office space has also been built in the biggest regional cities.

years, only a few office buildings were handed over to tenants in 2012 and 2013.

The high vacancy rate and, of course, current market conditions have resulted in decreasing rental levels in the Budapest office market. The rental fee for a typical class 'A' office building in Budapest is currently 10-14 €/sqm/month, of course mainly depending on the location, but also on the standard

and services of the building. Rents generally reflect a 15-30% decrease compared to the 2007-2008 levels, when rental fees on this market were the highest. Rents have probably reached their lowest level and are not expected to decrease further in the new developments, but landlords in older projects and secondary locations may be forced to offer even more attractive rental packages.

4. MAIN INDUSTRIES

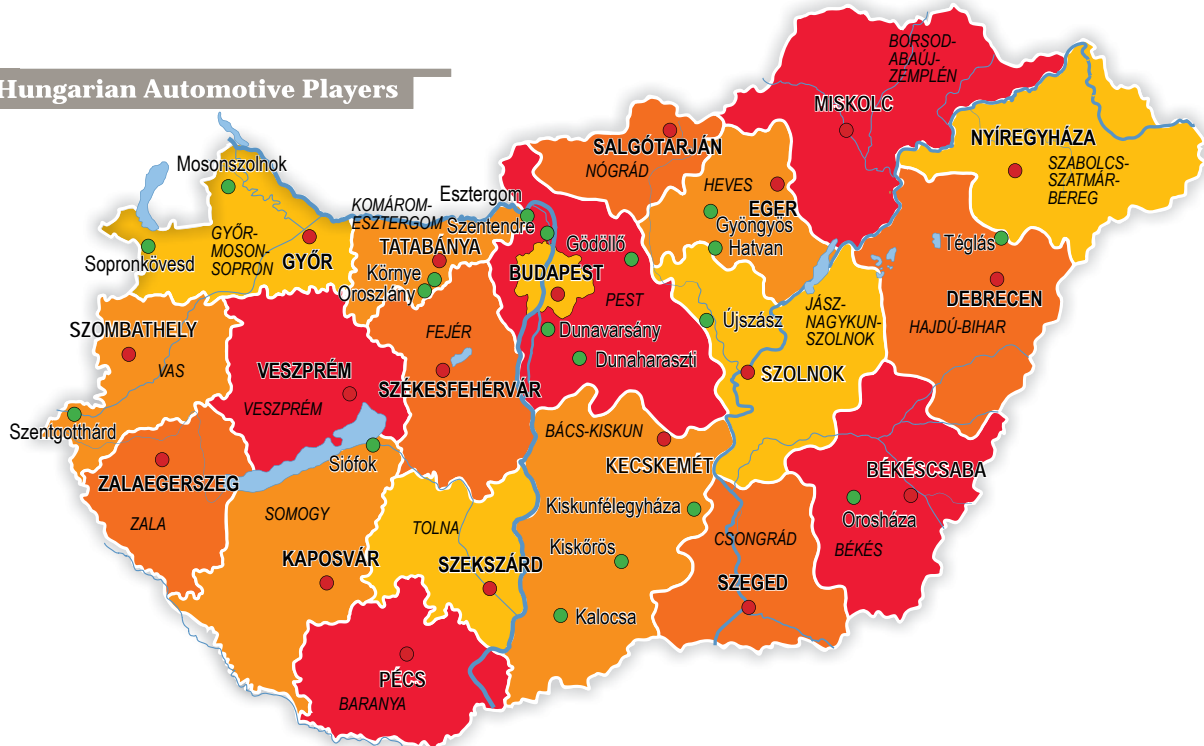
Automotive

The automotive sector is one of Hungary's core industries and generates almost 18% of total exports. More than 700 companies

employing a total of 115,000 people are active in the sector. Serial production of Mercedes-Benz cars began in March 2012 in Kecskemét. Audi has systematically been expanding since 2008 to establish the world's second biggest engine plant

in Győr, and established an R&D center as well as a full-fledged car production plant in 2013 in addition to the car assembly. GM and Suzuki are expanding their manufacturing process, too. Due to the fact that some large multinational companies have chosen Hungary to locate their capital investments, they have attracted a lot of equipment

Hungarian Automotive Players



BUDAPEST: Armafil, Autokut, Avvc, Bíró Kft., Bosch, Eltec, Fémalk, Kmg, Michelin-Taurus, Mikropakk, Porsche Hungaria, Siemens Vdo, Tauril, Temic Telefunken, TÜV-Nord, Webasto

GYŐR-MOSON-SOPRON
Győr: Audi, Rába, Lear, Nemak, Dana
Mosonszolnok: BOS, SMR Motherson
Sopronkövesd: Autoliv

VAS
Szombathely: LuK (Schaeffler Group), BPW, Delphi Packard
Szentgotthárd: Opel Szentgotthárd, Arcelor

KOMÁROM-ESZTERGOM
Tatabánya: Asahi Glass, Bridgestone, Euro-Exedy, Otto Fuchs, Westcast
Oroszlány: Borg Warner
Környe: AGC

VESZPRÉM
Veszprém: Bakony, Continental Teves, Valeo

SOMOGY
Siófok: Kongsbers

FEJÉR
Székesfehérvár: Alcoa, Denso, General Plastics, Karsai Holding, Loranger, Videoton, Visteon

TOLNA
Szekszárd: BHG, MMG, Pfannenschwarz

PEST
Esztergom: Albert Weber, Diamond Electric, Kirchoff, Suzuki
Szentendre: Ford
Dunavarsány: Ibsen
Dunaharaszti: Schwarz Müller
Gödöllő: Emt, Lear, Nief Plastic

BÁCS-KISKUN
Kecskemét: Thyssenkrupp, Knorr-Bremse, Daimler
Kiskunfélegyháza: Kunplast-Karsai
Kiskörös: Eckertle
Kalocsa: Emika, Kaloplasztik

CSONGRÁD
Szeged: Autofer

BÉKÉS
Békéscsaba: Csaba Metál
Orosháza: Linamar

JÁSZ-NAGYKUN-SZOLNOK
Szolnok: Eagle Ottawa, Euroszol, Isringhausen, Le Bélier
Újszász: Napi

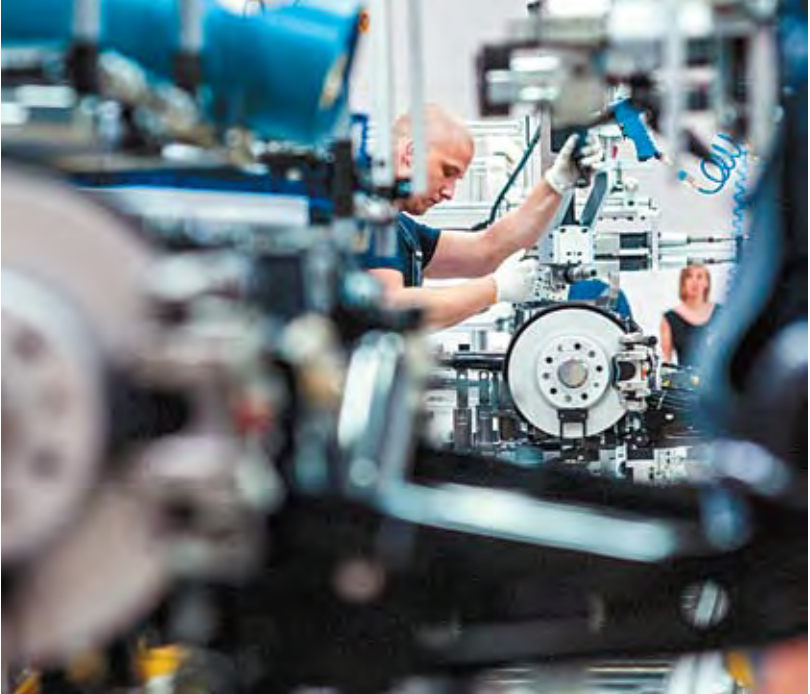
HEVES
Eger: Bosch-Rexroth, Firth Rixson, ZF
Gyöngyös: Stanley Electric
Hatvan: Bosch, Saia-Burgess

BORSOD-ABAÚJ-ZEMPLEN
Miskolc: Shinwa, Bosch

SZABOLCS-SZATMÁR-BEREG
Nyíregyháza: Michelin

HAJDÚ-BIHAR
Debrecen: FAG (Schaeffler Group)
Téglás: Hajdú

Source: HITA, 2014



Small and medium-sized local automotive companies have also become stable and strategic partners of both locally based and Western European car manufacturers.

manufacturers and other suppliers. Small and medium-sized local automotive companies have also become stable and strategic partners of both locally based and Western European car manufacturers.

The Hungarian automotive sector's cooperation with the local education system is strong and focuses on R&D and on the dual vocational training. Numerous multinationals have set up R&D

centers in Hungary, including Audi, Bosch, Knorr-Bremse, Thyssen-Krupp, Arvin Meritor, Denso, Continental, Visteon, WET, Draxlmaier, Edag, Temic Telefunken, and ZF.

BASED ON PUBLISHED 2012 financial statements



OEMs

	Net sales revenue (MHUF)	Number of employees
Audi Motor Hungária Kft.	1 612 480	8 177
Magyar Suzuki Zrt.	409 150	2 795
Mercedes Benz Manufacturing Hungary Kft.	267 919	2 542
Opel Szentgotthárd Kft.	25 579	656

TIER suppliers

Bosch Group	580 681	8 609
Continental Automotive Hungary Kft.	202 494	2 798
Michelin Hungária Abroncsgyártó Kft.	185 670	1 645
Hankook Tire Magyarország Kft.	162 449	2 169
Lear Corporation Hungary Kft.	156 260	3 494
LuK Savaria Kuplunggyártó Kft	141 370	1 757
Delphi Hungary Autóalkatrészgyártó Kft.	125 484	1 403
Denso Gyártó Magyarország Kft.	118 428	3 220

Source: Figyelő TOP 200 (2013)

Leading sector in Hungary: automotive

The automotive industry is the fastest growing sector of the Hungarian economy. It has undergone a quantitative and qualitative change in recent years. The Hungarian automotive industry may be described as clustered industry, resulting in companies being able to take advantage of the benefits of geographical proximity and the existence of critical mass. The automotive industry has significant role in the Hungarian economy illustrated by their added value, which is 10% of the Hungarian GDP and the number of employees, which is more than 115 thousand.

The basic pillars of the Hungarian automotive industry are the OEMs, which have been settled here as greenfield investments, like Audi Hungaria Motor Ltd. in Győr, Mercedes Benz Manufacturing Ltd. in Kecskemét, Opel Szentgotthárd Automotive Ltd. in Szentgotthárd and Magyar Suzuki Corporation in Esztergom. These OEMs created more than 17 thousand new jobs, they cooperate with several Hungarian universities and vocational schools.

Through the presence of OEMs, a significant number of suppliers has established production capacity in the country, in the entire automotive industry there are 712 companies. Trends in the Hungarian suppliers network typically follow global trends, namely a multi-level (TIER 1-4 levels) network. On the TIER 1 level there are mainly foreign companies, while Hungarian-owned companies are predominantly on the TIER 3-4 levels.

Many of the world's top TIER 1 suppliers are present in Hungary, like Bosch, Bridgestone, Continental, Delphi, Denso, Hankook Tires, Lear, LuK, Michelin.

Some of the TIER 1 suppliers have already established Hungarian R&D centers, of which Bosch Group deserves special mention. Bosch will employ around 1,000 engineers at its full capacity, and takes a leading role in the innovation capacity of the Hungarian automotive industry.

As Hungary lies along the Eastern part of the EU and is within the Schengen zone, the country's strategic geographical

position, highly developed logistics, utilities infrastructure makes it important as a regional distribution centre and a service hub for the CEE region. As a member of the European Union, Hungary has fully harmonised its legal system, adopting European safety and quality regulations related to automotive manufacturing. The success of the Hungarian automotive industry can be illustrated by the number of cars projected to be manufactured by 2019 comes to 697,000, out of which 561,000 will be in the premium category. Compared to other CE countries, this number of premium category cars is the highest in the region.

As Armin Krug, leader of the Hungarian PwC Automotive Group expressed:

"In a global comparison, the predicted growth of the European automotive industry for the upcoming six years cannot be considered significant growth. Regarding the EU countries, the car assembling industry by 2019 is estimated to take 11% of worldwide growth. In comparison to this, Hungary is in a much more comfortable situation."

"In order to fulfill the increasing demand, leading OEMs place their production onto a global level. We estimate that by 2019, seventy-one percent of German OEMs' global production will come from foreign factories. Hungary could gain a large role in the process because of its cost effective and labour-intensive high-level production capability."

"In addition, besides the factories, the major car manufacturers have realized the benefits of creating local R&D centres, which they have established many of worldwide. This trend offers opportunities for Hungary, as is shown by recent investments. Furthermore, these investments targeted the fastest rising segment: premium car production. So Hungary's production is extremely well positioned. The investments in the last couple of years demonstrate there are good initiatives in the field of R&D activities in Hungary, but I think there is still room for improvement in order to be more attractive to high-value-added activities. To create this attractive atmosphere, high-level cooperation is required between the companies, universities and research institutes."

TAKATA TO ESTABLISH FIRST PLANT IN HUNGARY

Production scheduled to commence in October 2014



It is the largest investment of a Japanese company in the region. The new plant is expected to contribute towards invigorating the local economy and employment market.

Tokyo, November 15, 2013

– Takata Corporation, a leading global supplier of automotive safety systems, announced that they have established a Hungarian subsidiary named Takata Safety Systems Hungary Ltd. to build a new production facility in Hungary.

The investment has been announced by the Hungarian Government on November 15. The announcement was attended by the Prime Minister Viktor Orbán and

several representatives from the Hungarian Government.

The new plant will be located in the city of Miskolc in Northern Hungary, some 180 km northeast from Budapest. The high-tech manufacturing plant will produce airbags and airbag components for car manufacturers in Europe. It is scheduled to begin operations in October 2014 and will employ up to 1,000 people. Total investment in the plant will be €68.3 million. It is the largest investment of a Japanese

company in the region. The new plant is expected to contribute towards invigorating the local economy and employment market.

The new plant marks Takata's entry into Hungary. This step is part of Takata's initiatives to strengthen its supply structure within Europe amid growing demand for airbags and is addition to the existing plants operating in Central and Eastern Europe. These include the recent 2013 inauguration of a new plant in Ulyanovsk, Russia in August.

INTERVIEW WITH JIRO EBIHARA, PRESIDENT OF DENSO MANUFACTURING HUNGARY LTD.

Re-invest in Hungary



DENSO Corporation, headquartered in Kariya, Japan, is a leading supplier of advanced automotive technology, systems and components for the world's major car makers. DENSO operates through more than 200 subsidiaries and affiliates in 35 countries. It employs approximately 130,000 employees across all aspects of the automotive business: from sales and product development to design and manufacturing. DENSO Manufacturing Hungary Ltd. was established as a Greenfield project in 1997 and is located in Székesfehérvár. Mass production began in 1999. The company started with diesel injection pumps, but has since experienced rapid growth and now manufactures a wide range of powertrain management products. In Hungary DENSO primarily manufactures diesel common rail system products (supply pump, injector, rail) and other engine control component parts. As the biggest employer in the region, DENSO Manufacturing Hungary Ltd. employs more than 5 000 people.

DENSO Manufacturing Hungary Ltd. is one of the biggest employers in the region, and has developed continuously in this country since 1997. What have been the biggest successes and difficulties in the past 17 years?

Our success is proved by the fact that, during the past 17 years our company in Székesfehérvár has developed into the biggest manufacturing plant within the DENSO Group outside of Japan. In contrast to our original activity, which was servicing European customers, currently we have

significant export activity to America and Asia. Throughout this development, the main challenge for us was to keep the customers' needs satisfied, which increased year by year. We had to pay a great deal of attention to the development of our production capacity, and to human resources. It was immense help for us that, in cooperation with the well educated Hungarian workforce, we could easily adapt the Japanese production systems into this factory, which contributed to the establishment of a strong and cooperative manufacturing plant. Of course, the economic crisis also affected us, propting us to restructure our product range. Thanks to these efforts, we got through the crisis.

How does DENSO Group evaluate its presence in Hungary?

As I already mentioned, DENSO Hungary is the biggest DENSO manufacturing plant outside of Japan, so it has a strategic significance in the DENSO Group. Because of this, the group headquarter always pays attention to activities in Hungary. Based on the past years' experience, we feel that it was a good decision to invest in Hungary, and we plan to increase our presence in Hungary in the coming years.

What does Székesfehérvár mean to DENSO and DENSO mean to the city?

Since our establishment in 1997, we have been given a warm response and support in Székesfehérvár that we appreciate greatly. We can return it by retaining the current workplaces. Besides this we are striving to create new ones and to have an active role in the development of the local community. As the biggest company in the region we feel we have social responsibility not only to our employees, but to the city and the region as well. Our aim is to live in harmony with the local community, to breathe together with this region and to contribute to a better world by developing our environment. It doesn't mean only theoretical policies; we are committed to realizing concrete efforts. For example, currently, in the frame of a CSR project (called 'KÉPES') we are working together with the local government and other local companies to renovate the washrooms in the local kindergartens. 2013 was the pilot year for this project, when we were able to carry out renewal works at the biggest and oldest kindergarten in Székesfehérvár. This year our aim is to renovate, altogether, 27 washrooms in five kindergartens, which will contribute to more pleasant days for more than 780 children.

How do you see the situation of a potential Japanese investor in Hungary, what kind of

advantages does the country have, from an investment point of view?

Hungary has a centralized location on the continent which is a huge advantage for the country. Besides the fact that Hungarian people are well qualified, they are honest, clever and hard-working, which human features are the cornerstone of a well-functioning and continuously developing company. During the past 17 years we have experienced that Hungarian people are really motivated, and they are always ready to develop themselves. Cost competitiveness, compared to other countries in Eastern Europe, is also a deciding factor when considering investing in Hungary. Hungary has long-standing traditions in the machine industry. Because of this, there are well-equipped and prepared machine making companies in the country with whom we can cooperate well as suppliers.

Have you experienced any cultural differences between Hungarian and Japanese business life?

It's a great experience of the past years that Hungary is easy to adapt to for Japanese people, who are also honest and hard-working. I think that Hungarian and Japanese people live their life on the same values, which makes cooperation and common development easy. Of course, there are also different cultural customs between the two countries, but it doesn't present any problem in business life.

DENSO won the European Environmental Award. How did you earn this prize?

DENSO Manufacturing Hungary's core products, such as the advanced fuel systems for diesel engines, known as the "common rail system" have established themselves in a growing market within Europe because of their class-leading performance and their positive environmental contribution. This positive contribution is reflected in the way the employees carry out their work, and these environmental efforts resulted in us winning the 'European Environmental Award' in the Management category in 2004. This is a great success because we won the award from among 17 countries and 100 candidates, and it was the first time that an automotive company won that prize. DENSO Hungary was able to show that there is a country and a company where the harmony between the environment and business is really important. Of course this award was the result of the hard work of the past years of operating in Hungary.

ELECTRONICS

The electronics industry is one of the largest industrial sectors in Hungary, accounting for 22% of total Hungarian manufacturing production. The country is the largest electronics producer in the CEE region, providing 25% of total regional production. Around 112,000 people are employed in the sector. In addition to several prestigious OEMs, six out of the top 10 Electronic Manufacturing Services (“EMS”) providers in Europe are present in Hungary (Jabil, Flextronics, Foxconn, Sanmina, Zollner and Videoton). Some of the companies, such as National Instruments and Jabil, also conduct R&D activities.



Major electronics manufacturing companies in Hungary



Source: HITA, 2014

PHARMACEUTICALS & MEDICAL TECHNOLOGY

With the most developed pharmaceutical sector in Central and Eastern Europe, Hungary provides an ideal base for life science companies planning further expansion in this region, or towards the Balkan states, and the more distant markets in Eastern Europe and Asia. In Hungary investors will find renowned R&D, a strong presence of large pharmaceutical companies, a growing number of small and medium-sized biotechnology companies, several fast-growing research institutions and skilled labour pool with relatively low wage requirements.

One of Hungary’s most traditional economic sectors is medical technology, a sector that has seen almost 100 years of widely acknowledged innovation, highly specialised technical development and notable exports to the global market. Several Hungarian companies have achieved international recognition with cutting edge products and technologies. A growing number of innovative domestic SMEs as well as several international medtech producers take advantage of the favourable environment and productive workforce in Hungary.



MAJOR PHARMACEUTICAL COMPANIES WITH MANUFACTURING BASE IN HUNGARY
Richter Gedeon, EGIS (Servier), TEVA, Sanofi, GlaxoSmithKline
COMPANIES WITH REGIONAL DISTRIBUTION CENTERS
Pfizer, AstraZeneca, Mylan, Sanofi, Janssen-Cilag
MEDICAL TECHNOLOGY COMPANIES WITH PRODUCTION ACTIVITY IN HUNGARY
Coloplast, GE Healthcare, B.Braun, BD, Hoya, Sauflon, Merck

INTERVIEW WITH ERIK BOGSCH, CEO, RICHTER GEDEON NYRT.

A flagship of the Hungarian pharmaceutical industry

Richter Gedeon Nyrt. is an innovative, specialised pharmaceutical company based in Hungary. It is one of the largest pharmaceutical companies in Central and Eastern Europe, and also has a direct market presence in Western Europe. In 2013 the company had a stock market value of EUR 2.8 billion and generated consolidated revenues of EUR 1.18 billion. Richter's product range spans most of the key therapeutic areas, including gynaecology, the central nervous system, the cardiovascular system, the digestive system, and muscle relaxants. The company, which has the largest R&D centre in Central and Eastern Europe, focuses its original research activities on disorders of the central nervous system. Richter's widely acknowledged expertise in steroid chemistry and its extensive product range for women's health protection have made it a world class pharmaceutical company specialised in gynaecology. The company also devotes significant resources to the development of biosimilar products.

In your opinion, what factors play the most important role in a foreign company's decision to invest in Hungary? Based on your experience of investments abroad, compared to the rest of the region, what is Hungary like as an investment location?

Broadly speaking, we can differentiate between two types of foreign companies – one type that aim to provide business or infrastructure services geared to the local market, and the other, global manufacturing companies that are looking to relocate certain of their production or service units. For both types of company the transparency of the regulatory and licencing environment and the competitive nature of taxation (corporate, local and personal) are important factors. For service companies, besides this, the size and growth rate of the local market and the limitations on competition are also of key importance. For global product-manufacturing companies, competitive labour costs,

an acceptable level of industrialisation, good logistical connections, and R&D or export incentives are important. Based on these considerations Hungary is not attractive enough for companies intending to provide services in the local market today, but for companies seeking a good site for certain manufacturing or service-provision activities conducted on a global or European scale, Hungary is definitively attractive.

What is the secret of successful operation in Hungary? Where do Richter's opportunities for further development lie?

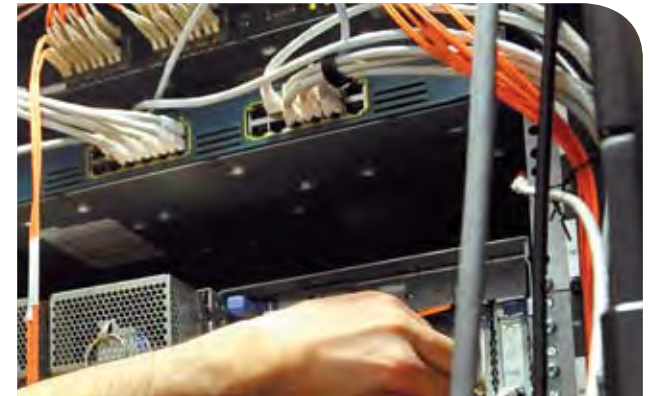
Committed employees, a stable ownership structure, a focus on innovation, and a marketing-oriented approach. Richter works consistently to implement its strategy, with the result that in several therapeutic areas (gynaecology, central nervous system and oncology), it is building a specialised and globally competitive product portfolio.

Richter engages in significant R&D activity in Hungary. How do you envision the trend in R&D investments in Hungary in the period ahead?

If the regulatory environment remains as supportive of R&D activity as it is now, then there's a good chance that Hungarian companies will spend even more on research and development, and that more R&D-intensive investments will be attracted to this country. To achieve this, it is essential to improve the attractiveness and quality of secondary and higher education in the natural sciences.

As a Hungarian large corporation, how do you see the chances of a Hungarian company embarking on foreign expansion?

The shortage of domestic capital represents an obstacle for Hungarian companies. The challenge for Hungarian firms wanting to expand is to raise sufficient capital for international expansion, but without losing control of the company in the process. The way that Richter achieved this was that the Hungarian state retained its 25% stake in the company while we primarily secured the amount necessary for international expansion through capital increases.



ICT SECTOR

Covering telecommunications, IT outsourcing, IT services, and software and hardware production, the Hungarian ICT market has grown fast in the last couple of years and leads the region in computer assembly and communications equipment manufacturing.

ICT sector was one of the economic sectors which has shown a constant growth even during the

economic downturn. Nowadays around 150,000 employees work directly in the sector.

The major global software developers and hardware producers are present in the country. Hardware production is centered in Central Hungary, including IBM in Vác. The majority of large software companies are located in Budapest. Several IT companies operate technology service centers and many of them have relocated their R&D activities here. ICT related R&D drives more than a quarter of total R&D expenditure.

Hungary has become a regional incubator for software development, including process control software, game programs and geographical information technology, focusing on car positioning ("sat-nav") systems. Hungarian software developers have achieved international success in several fields, such as virus protection, bioinformatics, and IT security. The presence and successful operation of companies such as Ericsson, Oracle and Gameloft show further evidence of the high quality of workforce in Hungary.

Discover ICT opportunities in Hungary

The Hungarian ICT (Information and communications technology) market – comprising telecommunications, IT services, IT outsourcing, software and hardware production – has grown rapidly in the last few years. The ICT sector accounts for around 10% of total Hungarian gross domestic product.

Global key market players in different ICT segments are present in Hungary. Among the big international vendors such as HP, Oracle, SAP, Ericsson (IT service providers); Samsung, Flextronics, GE, Nokia (producers); Vodafone, Deutsche Telekom, Telenor, Invitel (Telco), several influential local ICT providers and a new generation of world class startups have also emerged, such as Prezi.com, NNG or Log-me-in. Several global ICT companies have selected Hungary to establish their Shared Service Centers and have relocated their R&D activities, such as IBM, Vodafone, BT, Deutsche Telekom and Tata, due to the highly qualified but affordable workforce.

ICT networks, assets and services form a vital part of improving life quality, corporate competitiveness and government efficiency. The digital literacy of the Hungarian population is continuously growing; people tend to become more open to new technologies, and they are willing to invest in accessing them.

The country has reached a level at which almost everyone is a mobile customer. There are around 12 million subscriptions for a population of 10 million. The rising penetration of smartphones and tablets is expected to continue in Hungary, as they become more affordable; the desire of consumers for anytime Internet connectivity does not seem to be weakening, mostly due to social media

fever. The demand for the implementation of enterprise applications on mobile platforms and the growing space for "bring your own device" have helped to improve corporate efficiency. The increasing usage of mobile devices imposes a higher burden on telecommunications infrastructure, leading to system upgrades (i.e. fiber-to-the-premises, LTE enhancement).

Increasing Broadband Internet penetration is a priority goal of the Hungarian government.

Increasing Broadband Internet penetration is a priority goal of the Hungarian government. Almost half (49.04%) of all households internet connections are high speed (10Mbps) access, reaching the EU average, and very high speed (30Mbps) connections even significantly exceeding it. The mobile internet market is a high performing sector of telecommunications industry, covering 2.66 million active mobile internet subscriptions in mid-2013.

Following the global trend of more sophisticated and growing customer needs ICT services have become more diversified in the country. Due to the increasing development opportunities of IT services, Telco companies are looking for borderline areas, where IT and Telco services work hand in hand. A good example is cloud computing, which has great perspectives of 40-50% annual development, making one of the most dynamic sectors of Hungarian ICT market.

The new European Union 2014-2020 funding cycle offers great perspectives for ICT-related development programs, namely the development of broadband access, e-business

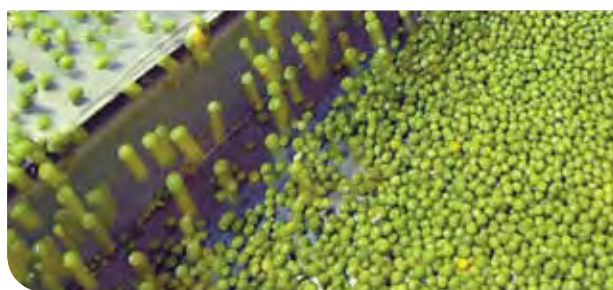


and e-government. The Hungarian government intends to maximize the absorption rate of funding available (ca. 1 bn EUR for the cycle), considering it a number one goal. A clear sign of this is the creation of the National Infocommunication Strategy 2014-2020, aiming to further increase citizens' access to the „digital ecosystem”.

Hungary has a highly qualified, flexible, but still affordable workforce in the ICT industry, creating a great competitive advantage regionally and globally. The government has significantly increased the number of state-subsidized students majoring in information

technology, natural sciences and engineering. The fact that from 2012, 31,000 students - as opposed to the previous 21,000 - have the opportunity to study these majors is a great achievement to ensure stable, long-term provision of talent.

Altogether several factors, such as the talented and qualified labour pool with competitive costs, the market growth opportunities, the central location infrastructure in terms of telecoms, power supply and office space, and the attractive EU and government incentives, make Hungary the ideal location for ICT sector investments.



FOOD INDUSTRY

Although its share in the output of Hungarian industry has decreased over the past eight-to-ten years, the food processing industry still remains one of the most important sub-sectors of the economy. The food industry employed 126,000 in 2012.

Its export revenues are vital to Hungary's overall trade balance. Hungary is the only net exporter of agricultural and food products in the CEE region. The industry generates 8% of the country's exports. Most food industry companies (more than 85%) are micro-enterprises that employ fewer than 10 people. The share of foreign capital in the industry is 47%. The processing

of meat, coffee and tea, and the manufacturing of soft drinks are the sectors with the highest share of FDI in the Hungarian food industry.

Multinational companies involved in vegetable oil processing, and confectionary and snacks, for example, dominate the sector. There are about 200 large food producers altogether, two-thirds of which are owned by investors from abroad. Large producers primarily use Hungarian raw materials. The processing and preserving of fruits and vegetables and the manufacture of pet food have also been popular targets. Major foreign investors include Bonduelle, Bunge, Givaudan, Globus, Mars, Nestlé, POPZ, and Unilever. In 2012 the share of food

The processing of meat, coffee and tea, and the manufacturing of soft drinks are the sectors with the highest share of FDI in the Hungarian food industry.

industry in Hungary's Foreign Direct Investment stock was 2.4%, which increased in 2013 with additional new investments and re-investments made by international companies.

Although industrial players can be found all over the country, the abundance of raw material resources determines certain concentrations in the regions of Central Hungary, the Northern and Southern Great Plain and Central Transdanubia.

II. Why invest in Hungary?

OVERVIEW ABOUT THE INCENTIVES IN HUNGARY



One of the competitive advantages Hungary has compared to other countries in the region is the Government's strong commitment to streamlining business processes and to increase the competitiveness of both SMEs and large enterprises through a wide range of available incentives.

Both refundable and non-refundable incentives are available for investors coming to or expanding in Hungary. The main types of incentives related to investments are cash subsidies (either from the Hungarian Government or from EU Funds), tax incentives, low-interest loans, or land available for free or at reduced prices.

2014 is a year of change in terms of incentives for the whole European Union and Hungary as well: new regulations and new funds will be available for the period of 2014-2020. As the Hungarian regulations on incentive opportunities are in accordance with EU state aid rules, significant changes are expected, along with state aid modernization initiated by the European Commission for the coming period. Most of the new EU regulations are not finalised yet and will come into force for the subsequent programming period from 1 July 2014.

2014 is a year of change in terms of incentives for the whole European Union and Hungary as well

REGIONAL AID INTENSITY MAP

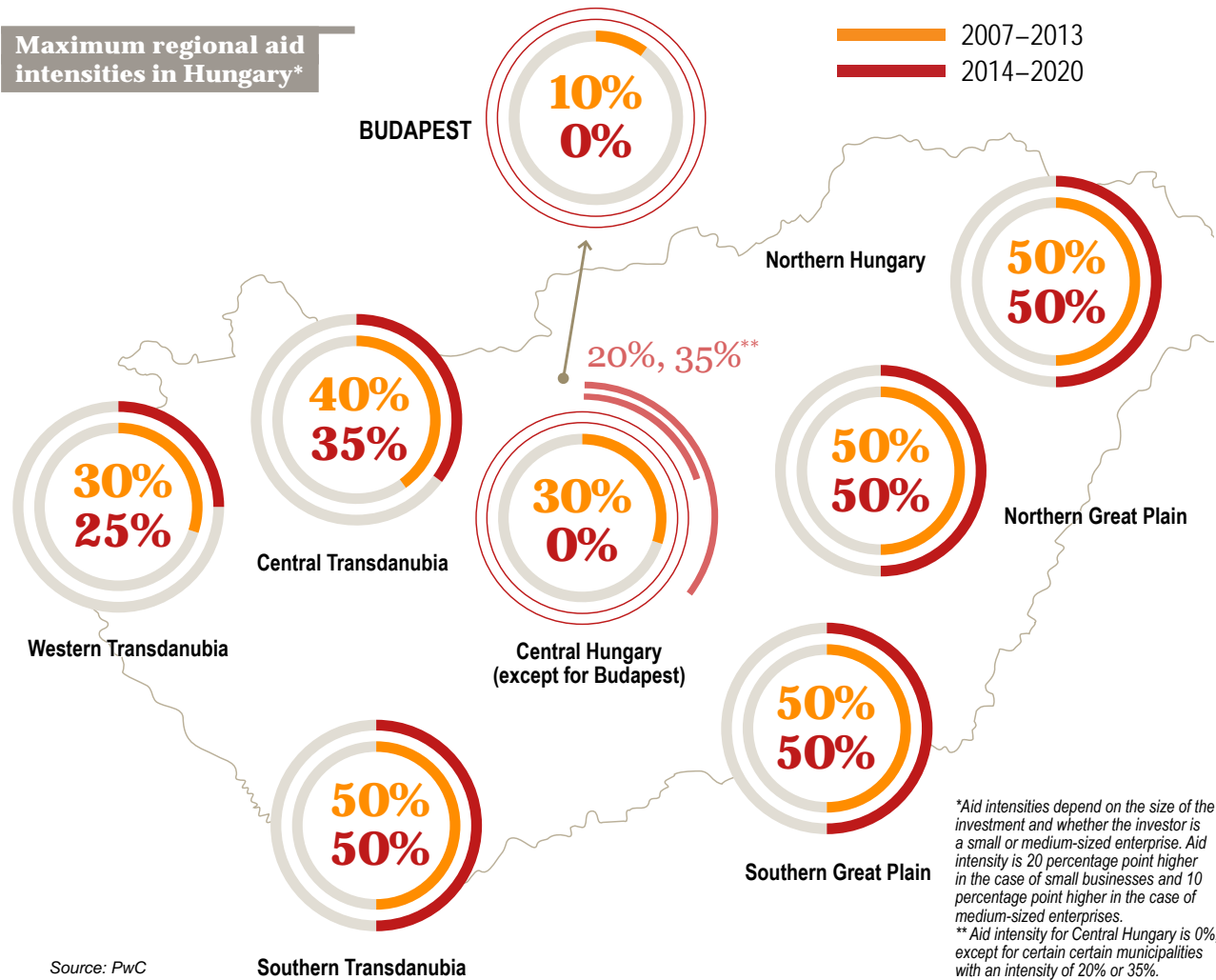
(2007-2013 vs. 2014-2020)

The maximum available amounts of regional incentives are based on a regional aid intensity map. The map for the period 2007-2013 is valid until 30 June 2014 i.e it applies to grants awarded before 30 June 2014. From 1 July 2014 the intensity ratio in most regions will change, except in less developed regions (50% intensity ratio remains). Small and medium-sized companies are able to increase the intensity by 10 or 20 percentage points.

The modifications strongly affect the Central Hungarian region where the regional aid intensity will vary between 0% and 35% from 1 July 2014 depending on the location. For Budapest, the intensity ratio will be 0% for investment subsidies, as in other capital cities in the region (e.g. Bratislava, Prague). Training and R&D subsidies will still be available in Budapest in the 2014-2020 programming period. The maximum available aid intensity decreases if the investment

is a large investment (exceeds EUR 50 million): 50% of the maximum aid intensity determined in the regional aid map is available for that part of the investment between EUR 50 million and 100 million, while 34% of the maximum aid intensity for that part of the investment beyond EUR 100 million.

When calculating the maximum available amount of regional incentives, all regional incentives – including cash subsidies, development tax incentive, etc. – need to be taken into account.



Source: PwC

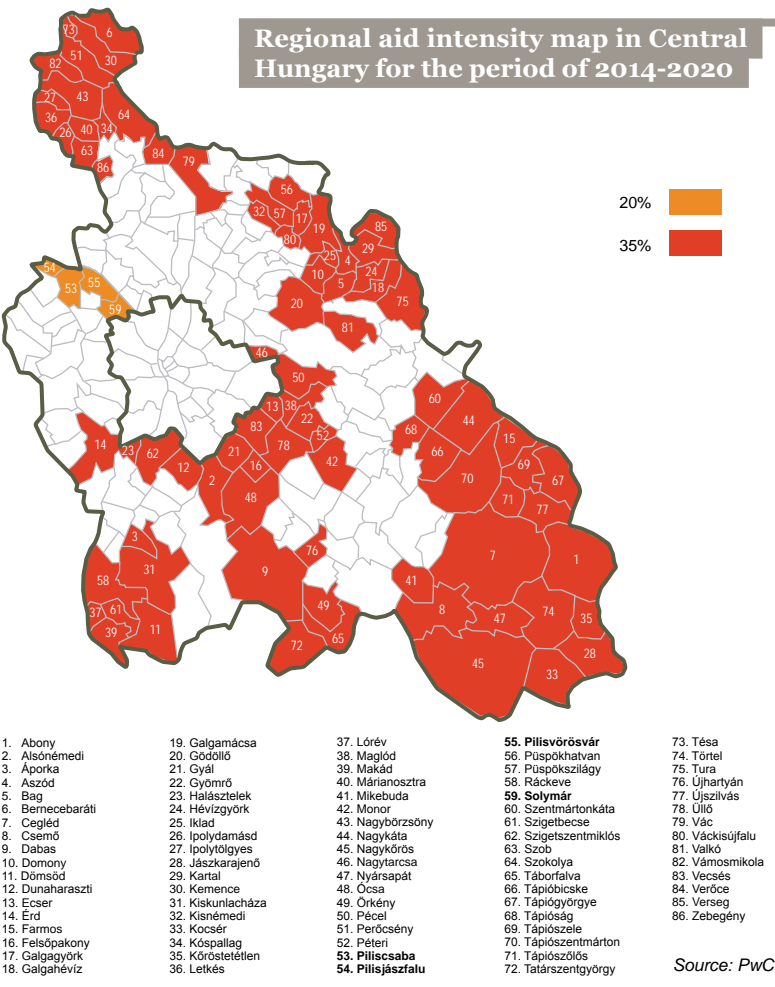
NON-REFUNDABLE CASH SUBSIDIES

1. Hungarian budget: Subsidies based on Governmental decision ("VIP subsidies")

The main types of cash incentives related to investments are focused on implementing the investment (e.g. purchasing assets, construction work, etc.), creating new jobs and training of employees. VIP investment subsidy can be granted under the current legislation until 30 June 2014, the VIP scheme available after 30 June 2014 will have a new legislation in line with the new EU rules. The summaries below contain the rules applicable until 30 June 2014.

1.1. "VIP" investment subsidy

The Hungarian Government makes a "VIP" subsidy opportunity available for investments greater than EUR 10 million that create a certain number of new jobs, depending on the purpose and location of the investment. The conditions of the VIP subsidy are determined in a negotiation procedure between the investor and the Hungarian authorities. If the investment is between EUR 10 and 25 million, the Hungarian authorities investigate the possibility of subsidizing the project from available EU Funds. Subsidy applications can be submitted to the Hungarian Investment and Trade Agency (HITA) either in English or in Hungarian.



Source: PwC

The main areas that attract support are investments in manufacturing (greenfield, brownfield or capacity extension), shared service centres ("SSCs") and research and development ("R&D").

Since the introduction of the VIP subsidy opportunity in 2004, 94 companies have already received Hungarian Government support. These companies had decided to carry out investments with a value of over HUF 2,211.05 billion (cca. EUR 8.5 billion) and to create, altogether, approximately 39,000 new jobs. The Hungarian Government decided to grant a total of HUF 174.8 billion (cca. EUR 582.9 million), paid in tranches, as the projects progress. A large number of projects have been located in Budapest, Central Transdanubia, Northern Hungary and the Northern Great Plain. Furthermore, investment volume has been especially high in Central Transdanubia and the Southern Great Plain due to some very large investments.

• **Manufacturing investments**

In order to be eligible for the VIP subsidy an investor has to create 50-100 new jobs, and for large investments of more than EUR 50 million 100-200 new jobs, depending on the region where the investment takes place.

The eligible costs for a manufacturing investment can be the purchase of the plot, construction costs or building rental fee, infrastructural costs, the purchase of new equipment and machines, intangible assets, etc. The investment period is determined by the investor, and usually does not exceed five years. The commitment period, starting after the completion of the investment, is five years in the case of large companies and three years in the case of SMEs.

• **R&D Investments**

The Hungarian Government places special importance on the development and support of R&D activity and R&D investments. Because of the world-class scientific knowledge

available in Hungary, it is an attractive environment for multinationals (e.g. telecommunications companies, the automotive sector, etc.), which often collaborate with Hungarian universities on R&D projects and expand their R&D capacities here.

In the case of R&D related investments, at least 10 new jobs have to be created in connection with the R&D activity in order to apply for VIP investment subsidy.

• Shared Service Centres

The number of inquiries and the expansion of already existing companies show that Hungary is an attractive location. A host of companies looking to streamline their global operations through BPO and SSCs (e.g. IBM, Vodafone, BP, Morgan Stanley, etc.) have already found attractive locations and a productive workforce in Hungary. In 2013 the following companies decided to invest or to expand their already existing operations in Hungary among them: Computacenter, Greif, Systemax, IT Services and Morgan Stanley.

In the case of establishing or expanding shared service centres, at least 100 new jobs have to be created in general, and at least 200 new jobs in Central-Hungary, to be eligible for VIP investment subsidy.

The eligible costs for VIP subsidies aimed at creation or expansion of SSCs are 24 months' salary and contribution for new employees employed within a three-year-period.

KEY ARGUMENTS FOR INVESTING IN THE HUNGARIAN SERVICE SECTOR

- Availability of skilled labour
- Cost savings
- Cultural compatibility and language skills
- Expertise in particular back-office or service activities
- Technological and other infrastructure
- Business security and strong intellectual property regulation

R&D&I in focus

The Hungarian Government continuously emphasizes the importance of domestic R&D&I improvement in order to reach the European levels. As a result of the latest developments, the European Innovation Scoreboard assesses the Budapest area as being on European standard level in terms of innovation capacity, although there is room for further improvement in all other regions of the country. In general, a positive trend can be observed in total R&D expenditure; corporate R&D resources are growing rapidly and now exceed public expenditure.

In 2012 HUF 336 billion was spent on R&D&I in Hungary, which is 1.2% of GDP. The National R&D&I Strategy published in 2013 aims at significantly higher innovation expenditure for the upcoming periods, 1.8% of GDP by 2020 and 3% by 2030.

Among the aims of the Strategy by 2020:

- More R&D innovation centers joining the world's innovation elite
- Establishing or strengthening global corporate R&D centers through promotion
- Growth-oriented R&D-focused SME's to find their global market expectations
- Promote innovative start-up companies

As proof of the development the number of R&D centers has been increased in recent years. Between 2006 and 2012, there was about 19% growth, which translates into 574 newly established R&D centres.

Although only 29% of Hungarian businesses have a centre dedicated to R&D or technology (compared with 42% internationally), they concentrate on research partnerships, with over 73% having an academic R&D partner (university or public research centre).

Hungarian Government has been advocating a strengthening of cooperation between research-centers with multinational background and the domestic universities, as well as SME's engaging in R&D.

In order to preserve the prominent position of multinational companies' Hungarian R&D centers in international competition, the availability of highly qualified human resources is guaranteed. For this purpose, the Hungarian education system ensures high-quality education and open cooperation and partnership between companies and universities.

Hungary aims to exploit the available resources as much as possible in order to hit the EU average in terms of R&D investment. The Government intends to provide the most extensive opportunities to improve companies' R&D-related activities.

As Zoltán Cséfalvay, State Secretary at the Ministry for National Economy stated "a development period is coming for Hungary with regard to the R&D sector; the Government intends to spend about 10% of its EU Funds on R&D approximately HUF 700 billion from the EU's 2014-2020 programming period." Beyond EU Funds, grants are also available from the national budget, either in the form of cash subsidy or tax incentive.

Fast growing and best performing sector

The first regional service centres appeared in Hungary at the end of the 1990's. There are around 80 Shared Service Centres (SSC) in Hungary, employing more than 30,000 workers by now. SSCs have a proven track record in the country and leading global corporations operate their centres in Hungary such as Exxon Mobile, British Petrol, Vodafone, IBM, Morgan Stanley, Citibank, British Telecom and Diageo. The SSC industry has become one of the fastest growing and best performing sectors in the Hungarian economy.

Based on a comprehensive and representative survey PwC conducted in 2013, SSC leaders are very pleased with the operation of their Hungarian centres: the initial targets have been met, and setting up the centre in Hungary proved to be the right decision. If the surveyed companies had to decide now, they would establish their SSC in Hungary again. The survey results also indicate a high degree of customer and employee satisfaction. More importantly, most of the participating centres are planning further expansion and growth in the country in the near future.

The key considerations for selecting a location for an SSC are generally consistent globally: relatively low labour cost and the availability of skilled workforce being the most decisive factors. Infrastructure and the economic environment of the country also play an important role when making investment decisions. Although quality of life and other subjective elements typically have less significance, often these make the real difference when similar countries or locations are in head-to-head competition. Hungary has a strong



competitive positions in all of these areas.

When comparing their current locations to other business jurisdictions, SSC leaders identified a number of areas in which Hungary is more favourable than others. These include the availability of a highly educated workforce, and the mentality, attitude, problem solving skills, and cultural and language diversity of people working in the sector. Hungary's IT, telecom and logistic infrastructures were also rated as very favourable. Another key area is that Hungarian SSCs have been very successful and have been delivering some very positive results with respect to quality, ability to quickly transfer activities from other locations and then increasing the quality and efficiency of such processes, and achieving a high level of customer satisfaction. Hungary was concluded to be an ideal location for SSCs that provide complex and high-value services.

Another important development to note is the increasing complexity of

the services provided. The past view that SSCs mainly provide simple and standardised low-value, transactional level services is no longer true for Hungary. The centres, which used to offer mainly relatively simple financial services, now manage many complex processes such as group treasury, external reporting, IT, HR, and financial modelling functions. Many activities have been transferred to Hungary from the group headquarters that only very few would have imagined 10 years ago. This could not have happened without the Hungarian SSC's strong, reliable and consistently high level performance.

Although the majority of the SSC sector is currently located in Budapest, the number of centres in the countryside is increasing. Larger cities with their own universities, such as Debrecen, Szeged and Pécs can provide great opportunities for new centres that are looking for young, ambitious, qualified skilled employees who speak foreign languages.

INTERVIEW WITH ANDOR FARAGÓ, GENERAL MANAGER

British Telecom in Hungary

BT (British Telecom) is one of the world's leading information and communications service providers, serving customers in more than 170 countries and employing close to 90,000 employees all around the globe. Its principal activities include the provision of networked IT services globally; local, national and international telecommunications services to its customers for use at home, at work and on the move; broadband and internet products and services and converged fixed/mobile products and services.

BT's office in Budapest, opened in 1999, marked the company's first foray into the rapidly growing markets of Central and Eastern Europe. The company's excellent position within the region today is a result of the in-depth local knowledge supported by a wide range of ICT offerings, and strong partnerships with regional providers.

In 2007 the company further enhanced its presence by opening its European Operations Centre, employing more than 900 employees in Budapest and Debrecen as of today. The highly skilled workforce of the centre supports 12 countries across Europe and focuses on customer service management, financial services, service delivery and various commercial & business support services.

What factors contributed to your decision to choose Hungary as the site for BT's service centre?

BT has been present in Hungary since 1999. At first, our activity was limited to conventional



telecommunications business in the CEE region. Besides our presence in Hungary and the successes of our first off-shoring projects, it was the availability of highly educated people with excellent foreign language skills, the state of the art infrastructure, combined with a supportive, investor-friendly attitude on the part of the Hungarian Government and the municipality in Debrecen that prompted BT to choose to locate its European Service Centre to Hungary. Ensuring the continuity of our business and our services is extremely important to us, and for this reason we set up offices in two locations from the very beginning – in Budapest and in Debrecen, and it is essentially because of this that some of our functions are now shared between these two sites.

What milestones have you reached since 2007 that you'd like to mention?

In 2007 we opened our new offices in Budapest and in Debrecen. In Spring of 2008 we signed an

incentive agreement with the Hungarian Government and, in that same year, as a result of the establishment of our Hungarian service centre, BT won the Investor of the Year award at the LA BAULE World Investment Conference (WIC). In 2011 the number of our employees reached the 500 mark, and in 2012 we won the Family Friendly Workplace award. Currently we employ more than 900 people in Hungary, and thanks to our continuous growth we will soon reach an important milestone, having 1,000 employees in Hungary.

What expansion and development opportunities are there for the Hungarian shared service centre (SSC), and what factors can assist with this?

One of the critical preconditions for further growth and new investments is the availability of labour in sufficient quantities and of an appropriate level of education. It is in a common interest that Hungary maintains its competitiveness and continuously improve the skills of its working population – particularly in the area of foreign languages. Most large global companies operate service and business support centres in several

geographical locations at the same time. Although these centres generally follow similar business strategies, they can nevertheless often become rivals when the firm's management is deciding what activity to centralise or relocate, to what extent, and where. For this reason it's important that the costs of employment and of conducting business (employers' taxes, contributions, duties, and so on) should, overall, remain competitive relative both to the region and to Europe's other developing countries. Besides this, a stable and predictable environment and preliminary consultations are critical for building the trust of potential investors.

What do you think of Hungary's investment incentives policy?

That Hungary should remain an attractive destination for investors is clearly an important goal. Executives around the world agree that the emphasis is increasingly shifting from crisis management to measures for ensuring sustainable growth, and my opinion is that it would be a good idea to align the country's investment incentives policy with this trend.





1.2. "VIP" training subsidy

The Hungarian Government offers "VIP" subsidy opportunity for training employees hired to new positions. The subsidy is available to investors creating at least 50 new jobs. The maximum amount of the training subsidy, if 50 to 500 new jobs are created, is EUR 1

million, or EUR 2 million if more than 500 new jobs are created. It is provided for both general and special trainings. The maximum aid intensity is 60% in the case of general training and 25% for special training. The aid intensity can be increased further in the case of small and medium-sized enterprises

The maximum amount of the training subsidy, if 50 to 500 new jobs are created, is EUR 1 million, or EUR 2 million if more than 500 new jobs are created.



and for training of disabled or disadvantaged workers. The training subsidy is not a regional incentive.

According to the new draft EU regulations, changes are expected regarding training subsidy as well.

1.3. "VIP" job creation subsidy

The Hungarian Government provides job creation subsidy for those investments entitled to VIP investment subsidy and that create at least 250 new jobs in disadvantaged- or 150 jobs in the least-developed micro-regions. The maximum available amount of subsidy is EUR 3 million, depending on the location and the number of new employees.

1.4. "VIP" vocational training facility subsidy

"VIP" subsidy opportunity is available for establishing vocational training facilities and the development of the equipment for practical trainings. In order to be qualified for the subsidy the number of vocational school students with training agreements has to be increased by at least 50 compared to the average number of trainees in the two school-years prior to the submission of the subsidy request.

The maximum subsidy amount is EUR 8,000 per student, and the total subsidy received can not exceed EUR 2 million per Beneficiary.

2. Subsidies from the research and technology innovation fund

Subsidy opportunities are available from the Hungarian national budget, primarily aimed at research and development activities involving a broad cooperation of companies, universities and research institutions. The subsidies are available through a tender application process.



3. Subsidies from EU Funds

A wide range of tender calls are available from EU Funds for which investments of less than EUR 10 million can also qualify. The conditions for applying, the timing, and the total amount of the subsidy available vary from tender to tender. These tenders reflect the importance given to supporting research and

development activities, the creation of new workplaces, environmental investments, and technological investments (with preference given to small and medium-sized enterprises).

The programming period of 2007-2013 is about to close, the EU Funds available can be disbursed

New funding will be available for Hungary in 2014-2020

till the end of 2015. Hungary's aim is to utilize this opportunity as much as possible. Therefore some tender calls financed from the Funds of the 2007-2013 period will still be published in 2014.

NEW PROGRAMMING PERIOD OF 2014-2020

New funding will be available for Hungary in the amount of EUR 20.5 billion regarding the programming period of 2014-2020. The first calls will be expected in the second half of 2014 after the new strategy plans and rules are finalized.

The main goals of the following programming period will be to increase the level of employment, to improve the competitiveness and global performance of the business sector, to encourage R&D&I activities and to increase energy and resource efficiency through the following main areas:

- Economic Development and Innovation
- Smart Transport Development
- Human Resources Development
- Environment and Energy Efficiency
- Territorial Development and Urban Development

The Prime Minister's Office coordinates the responsible Ministries in utilizing the new sources available for the programming period of 2014-2020.

All tender application have to be submitted in Hungarian, and the subsidy contracts are also in Hungarian.



TAX INCENTIVES

Tax incentives are available for companies' future transactions. Applications have to be submitted to the competent Authority in Hungary or to the competent EU institution before projects start.

Development Tax Incentives

Each development tax incentive may be claimed for a 10-year period (beginning once the development is completed) in Corporate Income Tax ("CIT") returns within a maximum period of 14 years from the original application for the incentive.

In any given tax year, the tax incentive is available for up to 80% of the tax payable, but in total up to the state aid intensity ceiling. Applications for tax incentives have to be submitted to the Ministry for National Economy, and the Hungarian Government has the right to grant permission if the aggregate eligible costs of the investment exceed EUR 100 million. If the investment is below this threshold, taxpayers need only notify the Ministry for National Economy before starting the investment.

Tax incentives are available for investments if, among other conditions:

- the current value of the investment is at least HUF 3 billion (cca. EUR 10 million) [at least HUF 1 billion (cca. EUR 3.33 million) in certain designated areas]; or
- the eligible costs come to at least HUF 100 million (cca. EUR 0.33 million) in the case of environmental protection projects, broadband Internet services, R&D projects, and motion picture and video production; or
- the company carries out an investment resulting in job creation. In the case of job creation projects, the tax



incentives are calculated based on 24 months' salary for new employees employed within the implementation phase and the subsequent three-year period. There are limitations neither on the amount of the eligible costs nor the number of newly created jobs;

The investment projects can only be subsidised if

- the investment results in the creation of new facilities or the extension of existing facilities; or
- the investment results in substantially changed products/services provided or production/service processes (excluding investments in basic research, applied research and experimental development).

In the case of HUF 3 billion (HUF 1 billion in certain designated areas) investments, the tax incentive is available provided that in the four years following the year in which the tax incentive is first used against the tax base:

- the annual average number of employees has increased by at least 150 (excluding the number of employees who are employed by a foreign branch) compared with either the year before the investment was made or the average number of employees for the three years preceding the investment (by 75 in certain designated areas); or
- annual wage costs have increased by 600 times the minimum wage (excluding the wage costs of the employees who are employed by a foreign branch) effective on the first day of the tax year (by a multiple of 300 in certain designated areas) compared with either the annual wage costs of the year before the investment was commenced or the average annual wage cost for the three years preceding the investment.

OTHER TAX INCENTIVES

TAX INCENTIVE RELATED TO R&D

A CIT base allowance and Local Business Tax ("LBT") base allowance apply to R&D activities if the taxpayer carries out R&D activities itself. The direct costs of an entity's own R&D, and also the value of purchased R&D services – if it was not incurred in connection with R&D services purchased from a Hungarian resident taxpayer, a private entrepreneur or a Hungarian permanent establishment of a foreign company – are deductible from the tax base. As of 2014, not only the taxpayer, but its related company may also deduct the direct costs of the taxpayer's own R&D efforts from its pre-tax profit, in the proportion agreed between them.

TAX ADVANTAGES FOR SHARED SERVICE CENTRES

Jobs created by SSCs may entitle the companies to obtain CIT and LBT incentives. For CIT purposes, SSCs may obtain a tax allowance for job creation and in this case, depending on the location of the SSC, the amount of the allowance may be up to 12 months' total salary expenses (50% of 24 months' salary for new employees) and contributions for newly hired employees. The LBT base may also be reduced by HUF 1 million (cca. EUR 3,333) per each additional employee in the year they are hired.

FILM, PERFORMING ARTS AND SPECTATOR SPORTS INCENTIVES

In Hungary companies are encouraged to subsidize film production, performing arts and spectator sports through the high rate of tax savings available. As sponsors, companies are able to achieve tax savings up to 104.75 % of the financial support they provide for film makers, performing artists or sport clubs.



III. How does one invest in Hungary?

1. ESTABLISHING YOUR BUSINESS

In Hungary the same rules for establishing a business apply to foreign individuals and legal entities as to Hungarian citizens and Hungarian entities. In the following table we have summarised the four main types of business associations most

commonly established in Hungary. Foreign businesses may also conduct the business activities in the form of a branch office or representative office established in Hungary. New corporate laws will enter into force in spring 2014. The table below reflects the new rules applicable

to companies established after 15 March 2014. Existing Hungarian limited partnerships have one year to adopt the new regulations; while limited liability companies and companies limited by shares are obliged to adopt these changes – principally – within two years.

	Limited partnership (Betéti társaság)	Limited liability company (Korlátolt felelősségű társaság)	Private company limited by shares (Zártkörűen működő részvénytársaság)	Public company limited by shares (Nyilvánosan működő részvénytársaság)
MAIN CHARACTERISTICS	<ul style="list-style-type: none">• Business association with legal personality;• At least one member with unlimited liability;• At least one other member is only obliged to provide a capital contribution (limited liability).	<ul style="list-style-type: none">• Business association with legal personality;• Established with an initial capital contribution, the amount of which is predetermined by law;• The members are only liable up to the amount of their capital contribution (limited liability).	<ul style="list-style-type: none">• Business association with legal personality;• Established with share capital consisting of shares of a pre-determined number and face value.• Invitations to the public to subscribe for shares are prohibited.	<ul style="list-style-type: none">• Business association with legal personality;• Only existing private companies limited by shares can be transformed into this type of business association.• The shares can only be subscribed publicly.
FOR WHOM RECOMMENDED	Founders who do not have the minimum capital required for a limited liability company.	Generally recommended because of limited liability.	Founders who have the required minimum capital and intend to provide different rights to the members of the company in the form of preference shares (i.e. preferred dividends, preference related to voting rights, etc).	It is usually recommended only if the company's activity requires public founding.
MINIMUM NUMBER OF FOUNDERS	Two	One	One	Two
MINIMUM AMOUNT OF INITIAL CAPITAL	HUF 1/member	HUF 3,000,000 (cca. EUR 10,000)	HUF 5,000,000 (cca. EUR 16,667)	HUF 20,000,000 (cca. EUR 66,667)

Source: PwC
Applied exchange rate: 300 HUF/EUR

ESTABLISHING A BUSINESS IN HUNGARY
STEP-BY-STEP

STEP 1

Preparation of corporate documents by a Hungarian attorney-at-law (certain documents must be countersigned by a Hungarian attorney). Time to complete: minimum one day. Costs: Attorney fees range widely.

STEP 2

Opening of a bank account
Time to complete: one day.
Costs: depending on the bank.

STEP 3

Registering the company at the Hungarian Court of Registry and obtaining a tax identification number. Time to complete: in the case of companies established using template constituting documents – one working hour from the issue of the company's tax identification number (NB: this simplified registration procedure is not available for public companies limited by shares), otherwise the registration procedure takes 15 working days. It should be noted that the process can be more time-consuming if the procedure is suspended because the tax authority needs more than one day to provide the Court with the tax identification number.

Costs:

Registration fees:

- for limited partnerships: HUF 50,000 (cca: EUR 167);
- for limited liability companies and for private companies limited by shares: HUF 100,000 (cca. EUR 333)
- for public companies limited by shares: HUF 600,000 (cca: EUR 2,000)

Simplified registration procedure:

- for limited liability companies and for private companies limited by shares HUF 50,000 (cca. EUR 167);
- for limited partnerships: HUF 25,000 (cca. EUR 83)

Publication fees: uniformly HUF 5,000 (cca. EUR 17). In the case of the simplified registration procedure, publication is free of charge.

STEP 4

Registration with the Hungarian tax authority, municipality, chamber of commerce and the Hungarian statistical office. Representative of the company or an authorised tax expert can perform the administration required for the registration. Time to complete: one day. Costs: free of charge.

Labour Law

An employment relationship can only be established through a written employment contract, regardless of the anticipated duration of the

employment. The employment contract must specify the employee's base salary and the employee's position. After the employment contract has been signed, the employer must provide the employee with a written description of his

or her most important rights and obligations within 15 days after signing.

Effective 1 January 2014, the mandatory minimum gross monthly wage is HUF 101,500 (cca. EUR 338), but for workers employed in positions requiring a secondary school diploma or advanced vocational training (or higher education) it is HUF 118,000 (cca. EUR 393) per month. Employers must pay additional premiums for shifts, nightwork and overtime.

Standard working hours for full-time employment are eight hours a day. The employer may set out a variable work schedule within a certain period of time, which allows an unequal allocation of working hours for a given employee. This period may last for four months or 16 weeks in general, but in specific cases – i.e seasonal work or standby – it can reach six months or 26 weeks. A specific provision in the collective bargaining agreement may extend this period to 12 months or 52 weeks.

Employers may not demand more than 250 hours of overtime a year, or more than 300 hours if a collective bargaining agreement is in place.

The statutory minimum amount of paid leave is twenty days, which increases with the employee's age (the first increase is when the employee reaches the age of 25). The maximum amount of paid leave is thirty days, which applies to employees over 45. Minors and employees with children are entitled to additional days. The paid leave days must be granted in the year in which they are due; however, there are exceptional options for taking them in the following year.

Employment may be terminated by mutual agreement, or by termination with notification, or immediate termination. The employees cannot be dismissed (except during the probationary period) without sufficient justification that clearly describes the reasons for the termination. The

EUROPEAN ECONOMIC
AREA (EEA) NATIONALS

An EEA national staying in Hungary for longer than three months needs to obtain a Registration Card and an Address Card from the Immigration Office.

The company where the EEA national carries out his/her activities must report the EEA national's position and nationality to the Labour Office.

THIRD
COUNTRY NATIONALS

The Hungarian entity is obliged to submit a workforce demand application form before a work permit application can be submitted.

When the workforce demand application has been accepted, the work permit application can be submitted. The permit must be obtained before commencement of the employment.

A Schengen visa has to be obtained for the individual to enter Hungary. The application should be submitted with the work permit application at the Hungarian embassy in the individual's home country.

After receiving the visa and entering Hungary, the individual needs to go to the Immigration Office to obtain the residence permit and register his/her Hungarian address.

option of immediate termination may be exercised if the other party violates an employment obligation substantially and wilfully or by gross negligence, or acts in a way that renders the continuation of the employment impossible. The reasons for termination with a notification period can be related to the employee's performance, to the employee's conduct in connection with the employment, or to the employer's operations.

Special rules apply to layoffs in which numerous employees are dismissed at the same time. There are specific situations during which an employment cannot be terminated effectively (i.e. during maternity leave). If the employer terminates an employment during such periods, the notification period shall start once the given situation ceases to exist. There are certain consequences if the employer unlawfully terminates employment (i.e. the employee may claim compensation). In the case of ordinary termination of employment, the termination period is at least thirty days, but the length of the termination period increases in proportion to the number of years the employee has spent at the employer, with 90 days as the maximum termination period.

Employees are entitled to severance payment if

- (a) the employer terminates the employment by termination with notification; or
- (b) the employer ceases to exist without a legal successor; or
- (c) the employee terminates the employment by immediate termination; or

- (d) the employer terminates the employment unlawfully and the employee would have been entitled to severance payment if he/she had been lawfully terminated.

Depending on the number of years the employee has spent at the employer, the amount of the severance payment can be between one month's and six months' absence



fee, which is not necessarily equal to the employee's salary (in specific cases, e.g. when the employee would reach the relevant age for retirement within five years, it can be even higher amount). However, the employee is only entitled to severance payment if he/she has worked for the employer for at least three years. No severance payment need be paid, if (a) the employee qualifies as retired at the time of the termination notification's delivery or when the employer ceases to exist without a legal successor; or (b) if the grounds for termination are related to the employee's conduct in connection with the employment or related to the employee's skills (except for health issues).

Foreign workers

Foreign nationals can work in Hungary under the terms of a Hungarian work contract or as assignees. The legal requirements for staying and working in Hungary applicable to the EEA (European Economic Area) and third-country nationals are different, as outlined below.



2. ACCOUNTING REQUIREMENTS

The statutory accounting records must be maintained in accordance with local GAAP. Bookkeeping has to be coordinated and reviewed, and Statutory Financial Statement (SFS) has to be prepared by an accountant certified and registered as auditor or chartered accountant at the Hungarian Ministry for National Economy. They are responsible for the Hungarian bookkeeping and for compiling and supplying true and reliable information, for maintaining and ensuring that the data disclosed in the SFS conforms to legal provisions, provide a true and fair view and are sufficiently documented in compliance with Hungarian accounting principles; furthermore their name and individual licence number are included in the SFS. Documents can be stored outside of Hungary. However, if audited by tax authorities, original documents and records must be made available within a maximum of three working days. Documents must be stored in a readable format for a minimum of eight years. Hungarian companies must file their local GAAP SFS and founder's resolution (regarding profit distribution) annually within five months of their financial year end. They must be filed electronically (not XBRL) using the mandatory pre-defined special pdf file format that is uploaded onto the website. Printed documents converted into an image file format (scanned) will not be accepted. A special file received from the Ministry of Justice must also be filed in order to support the payment of the publication fee. Non-compliance with the above-mentioned accounting requirements can trigger penalties and criminal law consequences.

In the event of non-compliance with the obligation to deposit and

to publish the SFS – following the penalties – the tax number of the company will be withdrawn and the company will be declared terminated.

Foreign currency bookkeeping

A company can prepare its annual financial statements in the convertible foreign currency specified in its founding document, provided that at least 25% of its (i) income, costs and expenditures; and (ii) financial assets and financial liabilities were earned or incurred, as applicable, in that convertible currency in both the current year and the previous year.

A company is in compliance with the conditions if the total amount of items listed in both points (i) and (ii) is at least 25%. Point (ii) does not include off-balance-sheet items.

Additionally, since 2010 all companies are permitted to prepare their annual financial statements in Euros, and since 2014 in USD (without the above limitation) if this is specified in their accounting policies. However, the accounting currency cannot be changed for five years after that.

Audit cycle

A company's supreme body is obliged to elect an auditor for a fixed term of not more than five years. Audits of annual financial statements are not compulsory if both of the following conditions are satisfied:

- The company's annual net sales revenue (calculated for the financial year) does not exceed an average of HUF 300 million (cca. EUR 1 million) for the two financial years preceding the financial year under review; and
- The average number of company employees for the two financial years



preceding the financial year under review did not exceed 50 persons.

One-stop shop

Companies automatically receive tax identification and social security numbers at the time they file their registration documents with the Court of Registration. The Court of Registration also forwards requests for VAT and statistical registration to the relevant authorities, at the company's request (thus steps 3 and 4 may be combined).

WHAT CONSTITUTES STATUTORY ACCOUNTING RECORDS IN HUNGARY?

	Type of accounting record	Required by local law	GAAP to be used	Specific format	Currency to be used	Language to be used	Frequency of update	Required for tax purposes
NOMINAL LEDGER	Nominal ledger	Yes	Local	Yes (specific chart of accounts)	Hungarian forint, Euro or functional	Hungarian	Monthly/ quarterly (depending on frequency of VAT return)	Yes – for CIT
	Journal book	Yes	Local	No	Hungarian forint, Euro or functional	Hungarian	Monthly/ quarterly (depending on frequency of VAT return)	No
	Trial balance	Yes	Local	Yes (specific chart of accounts)	Hungarian forint, Euro or functional	Hungarian	Annually	Yes – for CIT
PRIME BOOKS/ SUBLEDGERS	Fixed asset register	Yes	Local	No	Hungarian forint, Euro or functional	Hungarian	Annually	Yes – for CIT and VAT
	Cash book	Yes	Local	No	Hungarian forint, Euro or functional	Hungarian	Continuous (to reflect all events affecting liquid assets)	Yes – for CIT
	Purchase day book	Yes	Local	No	Hungarian forint, Euro or functional	Hungarian	Monthly/ quarterly (depending on frequency of VAT return)	Yes – for CIT and VAT
	Sales day book	Yes	Local	No	Hungarian forint, Euro or functional	Hungarian	Monthly/ quarterly (depending on frequency of VAT return)	Yes – for CIT and VAT
	Other - VAT subledger	Yes	Local	No (to be based on performance date)	Hungarian forint	Hungarian	Monthly/ quarterly (depending on frequency of VAT return)	Yes – for VAT

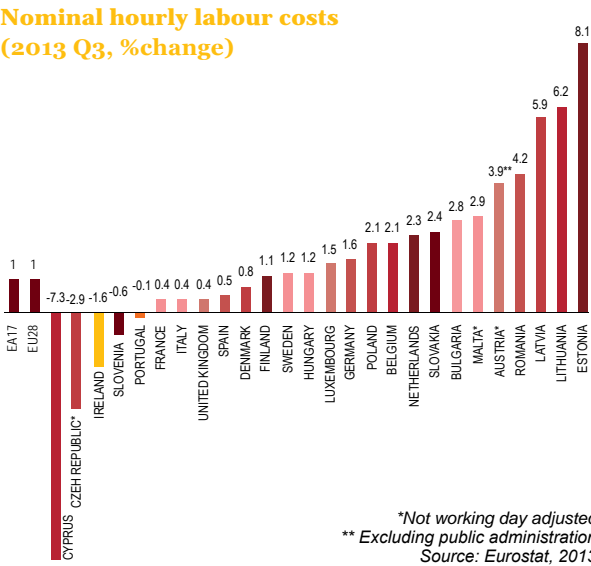
Source: PwC

3. HIRING AND EMPLOYMENT

Labour costs

Hourly labour costs in Hungary rose by 1.2% in the year up to the third quarter of 2013 compared with the same quarter of 2012.

The table below shows the changes compared with third quarter of 2012 (working-day adjusted).



Within the employed labour force, the following increase can be seen between 2001 and 2011 (according to the data of the last two population censuses). The proportion of daily commuters rose to 34% (2011) from 29.9% (2001). The majority of the commuter workforce is represented by the age groups of 30-39 and 40-49 (2011: 57.47%).

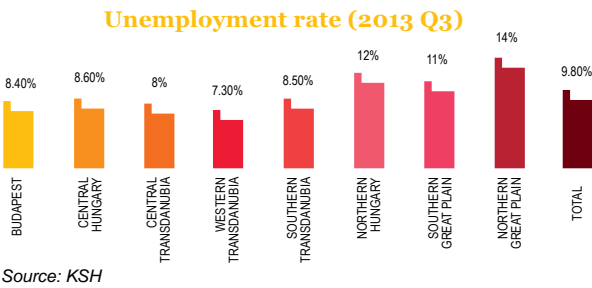
Unemployment

The impact of the global economic crisis can be still sensed on the Hungarian labour market. Due to declining labour market trends of preceding months, the unemployment rate in Q1 2013 reached 11.8%. This rate is equal to the historical peak (Q1 2010).

One of the most important goals announced by the Hungarian Government is to encourage companies to create jobs. The recently developed job protection plan entered into force on 1 January 2013 to moderate the consequences. The aim of the job protection plan is to preserve and create new jobs by reducing employer burden.

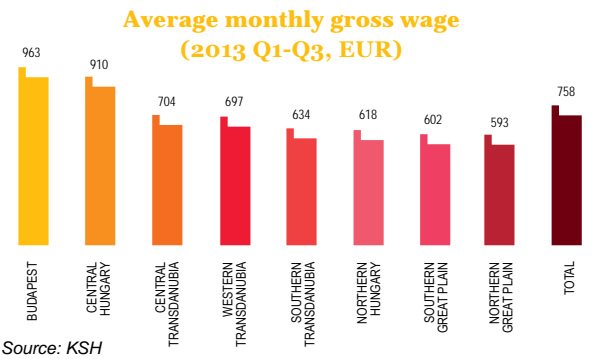
The programs of the job protection plan might have contributed to the fact that during the year prior the unemployment rate has showed continuous decrease

compared with previous quarters' data (Q2 2013: 10.3%; Q3 2013:9.8%).



Remuneration

The remuneration received for work should reflect the activity carried out and the qualification required for the job. The statutory gross minimum wage for 2014 is HUF 101,500 (cca. EUR 338) per month. Supplementary wages (e.g. evening and night shifts, weekend work and overtime) are additional items. Average monthly wages vary by region, as shown in the table below.



Demographic capital, education, language

In 2012 the number of students who acquired a degree (graduated with a qualification in university and college level education and tertiary undergraduate and postgraduate) reached nearly 64,000. The most common fields where fresh graduates finished studies were: business and administration; teacher training and education, engineering manufacturing and construction; social and behavioural science. The number of students in vocational education continues to increase (Source: KSH, 2013).

Strict language requirements of secondary and higher education, and several bilingual schools foster the development of language skills. Besides English and German there are also French, Spanish, Russian and Chinese bilingual schools available in Hungary.

Personal Income Tax

Tax and social security liabilities

The aim of the Hungarian Government over the next few years is to simplify administrative obligations and decrease labour costs borne by employers.

Employers can provide their employees (and in certain cases the employee's close relatives) with fringe benefits (e.g. meal vouchers, vacation and recreation, local travel passes, etc.).

These benefits are taxed at preferential rates compared with the taxation of employment income. Benefits available to all employees of the employer can also be provided at preferential tax rates.

Although there is no special expatriate tax regime in Hungary for assignees, they can be provided with certain tax-free benefits.

The social security coverage of international assignees from EEA countries is governed by EC Regulation 883/2004 or 1408/71. Third-country nationals assigned to Hungary become subject to Hungarian social security if the length of their assignment exceeds two years, unless a bilateral social security agreement stipulates otherwise.

Personal income tax and social security rates applicable to employment income

2014	Employee	
	Personal income tax	16%
	Pension contribution	10%
	Health insurance and unemployment contribution	8.5%
	Employer	
	Social tax	27%
	Training fund contribution	1.5%

Source: PwC

Job protection action plan

To improve the situation of unqualified/unskilled employees, jobseekers, youth (under the age of 25 years) and senior (above the age of 55 years) employees, and mothers with young children, the Government set a 10-point job protection action plan, effective as of 1 January 2013. With these steps the Government intended to reduce costs of employing such people. When employing young or old people, unskilled or long-term unemployed people, or mothers with



young children, the employer can apply social tax and training fund contribution allowances. The eligibility period of the allowances and their exact proportion (50% or 100%) depends on the employee groups to which the allowances can be applied. The allowances could be applied on the gross wage to a maximum of the first HUF 100,000 of the gross wage.

As a part of the job protection action plan, the Government introduced two new taxes for small and medium-sized enterprises (SMEs): a fixed-rate tax of low tax-bracket enterprises ("KATA"), and a small business tax ("KIVA"). By choosing these methods of taxation, SMEs can reduce their administration costs.

R&D-related allowance

An employer that qualifies as a research facility can apply social tax and training fund contribution allowances (100%) on the gross wage to a maximum of the first HUF 500,000 of the gross wage, in the case of researchers with at least a Phd. As of 2014, such an employer can apply social tax and training fund contribution allowance (50%) on the gross wage to a maximum of the first HUF 200,000 of the gross wage in the case of doctoral candidates and employees enrolled in a doctoral programme.

Free enterprise region

Employers operating in a free enterprise zone can apply social tax and training fund contribution allowance (100% in the first two years, 50% in the third year), per employee, if certain conditions are met. The allowances can be applied on the gross wage to a maximum of the first HUF 100,000 of the gross wage.



4. KEY TAX RELATED ISSUES

Corporate Income Tax

Resident taxpayers are subject to unlimited tax liability. Non-residents are subject to corporate income taxation on the income from their Hungarian branch's business activities.

In general, Hungarian companies are subject to corporate income tax ("CIT"), which is based on profit before tax and is subject to certain modifications.

The most common **deductions from the tax base** include:

- Losses carried forward (see details below);
- Reversal of provisions;
- Deductions relating to research and development ("R&D") activity (see details below);
- Depreciation based on rates prescribed in the CDTA;
- Reversal of impairment losses;
- Capital gains from the alienation of registered shares;
- 50% of royalties received by Hungarian entities.

The most common **additions to the tax base** include:

- Provisions for prospective obligations and for future expenses;
- Depreciation based on the accounting rules;
- Penalties and fines levied by the Hungarian Tax Authorities;
- Costs and expenses not incurred in the interest of the company's business activity;
- Interest expenses in excess of the allowable amount under the thin capitalization rules (see details below).

The CIT rate is 10% on the first HUF 500 million (cca. EUR 1.66 million) of the positive CIT base without any further preconditions and 19% on the CIT base above this limit. If a company's CIT base or the pre-tax profit (whichever is higher) is less than 2% of its total revenues reduced by the cost of goods sold, the value of mediated services and the income of the foreign permanent establishments ("minimum tax

base"), the company can choose to file a declaration presenting its cost settlement and pay CIT in accordance with the general provisions or pay CIT on its minimum tax base.

A special regime applies to income from royalties, under which half of the general tax rate may be applicable on royalties. Thin capitalisation rules may apply to interest on any non-banking debt and noninterest-bearing loans received from related parties in excess of three times the equity. Tax losses can be carried forward indefinitely and their use is no longer subject to the Tax Authority's approval. As of 2012, tax losses are deductible up to 50% of the positive tax base.

Hungary has concluded double tax treaties with 73 countries, including all EU member states, Canada, China, Hong Kong, South-Korea, Brazil, Mexico, India, and others. Double tax treaties are currently under renewal with the USA, Switzerland, Japan, Moldova, Serbia and the United Arab Emirates.

Dividends, interest and royalties are exempt from withholding tax under the domestic rules.

Capital gains realized by foreign persons are exempt from CIT in Hungary. However, this exemption does not apply to capital gains related to stakes in Hungarian real estate companies; in these cases, transfer tax may also apply.

From 1 January 2012, there are further incentives available for holding intellectual properties. Any gains on the sale (or a capital increase that is not in cash) for qualifying intellectual property would be exempt from corporate income tax if the seller reported the acquisition to the Tax Authority and held the property for at least one year. Alternatively, if such reporting was not made, gains realized on a sale would still be exempt if the taxable gain is used to purchase qualifying intellectual property within three years of the sale.

Local Business Tax

Entrepreneurs must pay the local business tax ("LBT") in the municipalities where their activities are located.

LBT must be paid on the amount of adjusted annual turnover determined by law. When calculating the LBT base, the annual turnover can be reduced by the cost of goods sold, the costs of mediated services and subcontractors' activities, the costs of materials and the direct costs of R&D. However, as of 2013 only the base part of the cost of goods sold and part of the value of mediated services as calculated based on brackets determined in relation to their annual sales revenues may be deducted from this tax. Royalty and interest income are exempt from LBT.

The tax rate is determined by the local government within whose jurisdiction the company carries out its business activities, but cannot exceed the maximum determined in the Local Tax Act (2%). If a company carries out its business activities within the jurisdiction of more than one Hungarian local municipality, its LBT base has to be allocated amongst the different municipalities.

LBT has to be paid even if the company had a tax loss for CIT purposes.

The LBT base of a foreign permanent establishment of a Hungarian company is exempted from the Hungarian LBT.

Innovation Contribution

Companies fitting the definition in the Accounting Act are subject to this contribution, except for small and medium-sized enterprises. The innovation contribution is calculated on the LBT base, furthermore, no innovation contribution is payable, with retroactive effect from 2012, on that part of the tax base allocated to foreign permanent establishments. The tax rate is 0.3%.

Transfer Pricing

In Hungary transfer pricing rules apply. Accordingly, if the prices applied in related-party transactions are not arm's-length prices, the Tax Authority is entitled to modify a company's CIT and special tax base by the difference between the prices applied and the arm's-length prices.

Taxpayers are obliged to prepare transfer pricing documentation on intragroup transactions and also on transactions carried out between Hungarian companies and their foreign branches. The documentation has to be prepared for every contract (transaction) between related parties (including in-kind contributions made at the time entities are established).

TP rules do not apply to transactions between a resident taxpayer's permanent establishment and related company if the resident taxpayer under the provisions of an international treaty adjusts the corporate tax base, ensuring that it

does not include the foreign taxable income.

Rulings

The Tax Authority and the Ministry for National Economy provide the following types of ruling upon submission of a formal request:

- Non-binding rulings on the interpretation of regulations, provided free of charge.
- Binding rulings may be requested by taxpayers and foreign entities regarding any type of tax, provided the ruling has bearing on the tax consequences of a future contract, transaction or chain of transactions, and a detailed description is provided.
- Binding rulings may be requested regarding CIT, PIT, LBT and SME tax, provided the ruling has bearing on the tax consequences of past and ongoing transactions.
- Super rulings (binding for



three years, even if there are subsequent changes to the CIT law) are also available.

- Advance Pricing Agreements are available for the purpose of setting a transfer price or price range with the Tax Authority.
- As of 2012, the Hungarian IP office is authorised to classify whether a specific future project can be treated as an R&D project. This classification is binding for any other authorities.

Value Added Tax

As a general rule, Value Added Tax (“VAT”) should be charged on the following transactions:

- Supplies of goods and services provided for consideration in Hungary;
- Intra-Community acquisitions of goods in Hungary;
- Imports of goods.

Certain services are exempt from VAT, including but not limited to medical, cultural, sporting, and educational services provided as public services; and financial and insurance services. Intra-Community supplies of goods and services and exports are also treated as exempt transactions.

The supply of a building or parts of a building and the land on which it

stands and the rental of real estate are VAT exempted in general, but taxpayers might opt to treat these transactions as VATable. The supply of building plots is, however, not VAT exempt.

There are some special transactions that may be out of scope of Hungarian VAT, provided that special conditions are met. These are the acquisition of any contributions in kind, the acquisition of any assets by way of succession and the transfer of business as a going concern.

Based on the general rule to be applied in the case of business-to-business services, the place of supply is where the customer has established its business.

The standard VAT rate in Hungary is 27%. There are also two reduced rates: 18% and 5%. The 18% VAT rate is applicable to certain dairy products and products made from cereals, flour, starch and milk. The 18% VAT rate should also be applied to commercial accommodation services and to services that grant admission to musical and dancing events. The 5% VAT rate is applicable to certain pharmaceutical products, audio books, printed books, newspapers, district heating services, certain live performance activities, and the supply of certain goods in the pork sector.

Related companies that have established business presences in Hungary are entitled to form a VAT

group. The essence of a VAT group is that its members act under a single VAT number in their transactions (i.e. they issue invoices under a shared VAT number and submit a single, joint tax return), and product and service supplies between the members do not qualify as business transactions for VAT purposes.

The VAT act allows Hungarian taxpayers to apply the domestic reverse-charge mechanism to the following transactions:

- Services related to immovable property (e.g. construction, maintenance);
- Sales of waste materials;
- Sales of carbon quotas;
- Sales of real estate and land if the application of VAT was chosen;
- Sales of certain agricultural products (e.g. maize, wheat, barley, rye, etc.);
- Sales of pigs (e.g. pork, pork side).

Under the general rule, VAT returns have to be submitted quarterly. However, under some circumstances monthly or annual VAT returns have to be prepared.

In the case of intra-Community transactions, the taxable person has to submit recapitulative statements (monthly or quarterly). These statements can only be submitted to the Hungarian Tax Authority electronically.

From 1 January 2013 taxpayers registered in Hungary have to submit a domestic recapitulative statement about those transactions, the VAT amount of which reaches or exceeds HUF 2 million (cca. EUR 6,667) together with the basic data of the related business partner. In respect of the incoming invoices, those cases also have to be considered and reported in which the sum of the VAT on all transactions carried out by the same partner in a given VAT period reaches or exceeds HUF 2 million. If a domestic recapitulative statement has to be prepared (i.e. there are transactions with a VAT amount higher than the threshold), the VAT return can only be submitted electronically.

If a taxpayer has a negative VAT balance in a return period, this



amount can be recovered, provided that the tax balance reaches or exceeds an absolute value of HUF 1 million (cca. EUR 3,330) for monthly filers, HUF 250,000 (cca. EUR 833) for quarterly filers or HUF 50,000 (cca. EUR 167) for annual filers.

Environmental Protection Product Fee

Businesses engaged in manufacturing, importing and intra-Community purchases of certain products must pay an environmental protection product fee (“product fee”). The following products are subject to the product fee in 2014:

- Certain petroleum products;
- Tyres;
- Packaging materials (included as part of the packaging);
- Batteries;
- Commercial printing paper; and
- Electrical and electronic products.

The parties liable to pay the product fee are the first domestic distributor or the user for own purposes; in the case of domestically manufactured petroleum products, the first buyer from

the domestic distributor or the user for own purposes; and in the case of toll manufacturing, the party that orders the toll manufacturing. The product fee is calculated on the basis of the weight of the product multiplied by the fee rate.

The tax returns have to be filed quarterly, and an advance payment has to be made for the fourth quarter of the year. The National Tax- and Customs Authority’s tax body is responsible for tasks related to the product fee.

In certain cases the product fee can be reclaimed if the taxpayer meets the requirements.

In addition to the above listed main taxes, Hungarian taxpayer entities are subject to several smaller taxes, e.g. excise tax, customs duties, stamp duties, registration tax, community tax, tourism tax, sector-specific taxes (energy tax, pharma taxes), accident tax, etc., which are not covered in this booklet.

Other Taxes

Several new taxes have come into effect in the last few years. The **bank tax** is levied on financial

institutions. The rates, among others, are 0.15% on balance sheet totals of up to HUF 50 billion, and 0.53% on balance sheet totals of HUF 50 billion and above.

Telecommunication service providers are subject to a special tax with rates of HUF 2 per minute for calls made and HUF 2 per message sent for private individuals, and HUF 3 per minute for calls made and HUF 3 per message sent for entities other than private individuals. The monthly ceiling of the tax payable is HUF 700 per phone number for private individuals and HUF 5000 per phone number for entities other than private individuals.

In addition to corporate income tax, energy suppliers and public utility service providers are subject to another income tax, popularly known as the “**Robin Hood tax**”. As of 2013, the government increased its rate from 8% to 31%, although, it is possible to claim development tax incentive up to 50% of the tax liability.

Insurance tax is levied on insurance companies. The rates are 15% on insurance premiums for casco insurance services provided and 10% on property and accident insurance services provided.

The buyer and first domestic distributor of certain products are liable to pay **public health product tax**. The products which fall under this tax are beverages, energy drinks, cocoa powder with added sugar, other pre-packed products with sugar, salty snacks, seasonings, flavoured beer and alcoholic beverages, and fruit jam. The rates vary depending on tariff number and salt, sugar, cocoa, methyl-xanthine, or taurine content.

Payment service providers, credit institutions and special services intermediaries are subject to the **financial transaction tax** levied on payment services, e.g. bank transfers and direct debits. The amount payable in general is 0.3% of the amount of transaction but may not be more than HUF 6,000 per transaction (except for cash withdrawal).



Moving in a new direction

