

Frequently Asked Questions

Effects of the Coronavirus Pandemic on Transfer Pricing Issues

In the following, we examine the effects of the coronavirus pandemic on transfer pricing in light of frequently asked taxpayer questions. As the effects of the pandemic on sectors and companies are not known in detail to us, we can provide general answers to most questions. Our summary is based on information available to us up to the date of publication of this document, which is constantly being updated.

1. Does the organisational unit of NTCA specialised in transfer pricing issues follow international trends related to the epidemiological situation?

NTCA considers measuring the effects of the pandemic as a priority, it follows the international press, participates in the work of international organizations and incorporates the best practices and results into the daily work of the transfer pricing unit. NTCA is present in the OECD working groups, both in those dealing with the pandemic and in other permanent ones, and also participates in the analytical work and discussions of the European Union and of the Intra-European Organization of Tax Administrations (IOTA) in relation to the pandemic.

2. What content should the transfer pricing documentation have for the year affected by the crisis?

The relevant legislation has not changed regarding transfer pricing issues until the publication of this information note, therefore, the transfer pricing documentation, even now, shall be compiled on the basis of Decree No. 32 of 2017 (X.18.) of the Minister for National Economy on the Obligation of Documentation related to Determining Arm's Length Price (hereinafter TPD).

If, there has been a change at the company as a result of the pandemic, this should be detailed in the transfer pricing documentation. For example, if profitability has changed, it is important to present the reasons for this in the sectorial analysis. If, due to the economic effects of the pandemic, the group company carries out a reorganization as defined in Chapter IX of the 2017 OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (hereinafter TPG), the change of functional profile and the business strategy as well as the possible change of the method shall also be justified.

TPG and TPD referred to earlier, both address in several places the importance of documenting changes and the need to justify deviations caused by changes and their consequences.

3. Is the economic recession caused by the current coronavirus pandemic comparable to the 2008 crisis?

The world crisis of 2008–2009 started from the crisis of the financial sector and gradually spread to different geographical regions and economic sectors. In

contrast, the impact of the pandemic on the economy appears in a short period of time and in a concentrated way.

4. What principles should taxpayers follow when comparing data of tax years not affected by the pandemic with data of the tax year of 2020?

The economic effects of the coronavirus pandemic are not yet transparent, so it is not possible to give a complete answer to this question. If these effects have an influence on a given economic sector, a correction may, of course, be necessary, also in view of the characterization.

Adjustments shall be made pursuant to Point k) of Subsection 4 of Section 4 of the TPD which states that the adjustment (s) made shall be justified and should be traceable.

5. During the period of economic recession, is it acceptable for the Hungarian subsidiary to bear a proportionate share of the losses in the entire value chain, and under what conditions can the share of limited risk companies in losses be accepted?

As the onset of the crisis depends on the economic sector and the company, the allocation of losses is generally not acceptable. Adverse economic conditions alone do not justify the allocation of losses, it is also necessary to examine the risks and how they are controlled. Accordingly, in allocating lawful losses, it shall be demonstrated that, in similar circumstances, the reduction of income in question would also be incurred in the case of independent parties.

The functional analysis of a given company and its characterization in this regard – in line with Point D.1.2. of TPG – is of paramount importance, because a firm's ability to generate income is greatly influenced by where it is located in the value chain. The more functions, risks and assets can be linked to a member of the group, the greater may be its ability to generate income, as the expected return also increases in proportion to the risks taken. This, of course, is also true the other way round, from which it follows that limited risk-taking is not only about low, but stable returns, it also means potentially excluding losses or, in exceptional and particularly justified cases, a moderate level of it. Companies characterized as limited risk firms based on the functional analysis can therefore be expected to keep on operating with the stable profitability they have had.

6. In conducting a comparative analysis, do taxpayers have the option not to refuse companies that realize losses?

For reliable database filtering, companies with characteristics such as the party being tested should be included in the sample. A positive, stable level of profitability is expected for companies with limited risks. If database filtering is used to support the profitability level of a limited risk company, permanent loss-making comparable companies should continue to be refused.

If the vast majority of independent players with the same characteristics in the given sector have been loss-making due to the effects of the pandemic, it is not necessary to exclude loss-making companies from the sample.

7. What can taxpayers do if, in terms of time and impact, different economic measures and government subsidies have been introduced in the countries in which the different members of the group operate?

As far as the economic measures and subsidies of the individual states are concerned, the position and practice of NTCA is that the best comparable independent companies can be found on the Hungarian market in order to perform a proper comparative analysis. If the sample from the Hungarian market does not contain a sufficient number of independent companies, then the expansion of the sample to V4 countries and then to EU28 may be justified.

8. In the current epidemiological situation, can taxpayers file applications for the determination of the arm's length price and, if so, are there specific principles for compiling the applications?

During and as a result of the coronavirus pandemic, the legal environment for transfer pricing obligations has not changed. Consequently, it is still necessary to submit applications for the determination of the arm's length price and the annexes to be attached, in accord with the legal requirements. In view of this, the application and its annexes shall be submitted electronically using the form named APIAC. The sectorial analysis also needs to address the impact of the coronavirus pandemic on the industrial sector.

9. Is it possible to initiate a prior consultation?

Yes, NTCA holds online video conferences with taxpayers (it requires a special statement of the taxpayer) and consults with a smaller number of participants (2-3 people) in person again since the end of the emergency situation.

10. How does the tax authority take into account the economic situation caused by the coronavirus pandemic in the ongoing APA proceedings?

Applications are processed in accordance with the standard procedure previously applied.

Of course, as part of the procedure, NTCA also deals with the outlook for the future, as – subject to Point 3.7 of the TPG (extensive analysis) – it is essential to know the business plan for 2020 and the changes that have taken place as a result of the current situation in terms of the examination of the transaction from the angle of transfer pricing. Accordingly, if the pandemic affects the economic sector in which the company operates or is justified in terms of the company characterization, NTCA may ask, inter alia, whether, in view of the emergency situation and the economic crisis, the applicant considers it appropriate to review the 2020 business plan or whether an operating loss is expected for the 2020 business year.

11. What options are there for the taxpayers under an ongoing APA procedure?

Taxpayers may decide to continue the procedure in accordance with the application and information previously submitted, but may also decide to amend or withdraw their request aimed at determining the arm's length price.

12. Do taxpayers have the possibility to amend an APA decision/resolution in force?

Of course, this possibility also exists. If the taxpayer files his/her application for an amendment in view of the economic situation caused by the pandemic, it needs to be substantiated by the taxpayer and examined by NTCA whether the taxpayer, and the industry in which the taxpayer operates, is really affected by the economic impacts, since, in line with the above, an economic sector and company specific assessment is required. In the amendment procedure, the extent to which the taxpayer on the basis of its characterisation can bear the risk associated with the epidemic should be examined.

During the amendment procedure, NTCA will examine whether or not the applicant has acted in accordance with the applicable APA decision in the already closed tax years.

13. Do taxpayers have the option to extend an existing APA decision/resolution?

In this case, too, NTCA is awaiting the taxpayers' application for an extension in accordance with the legislation currently in force. On the basis of the Act on the Rules of Taxation, however, "the effective term of the resolution may not be extended if the facts on which the original resolution is based change to such extent that a new resolution would be necessary to establish the arm's length price". It is the taxpayer's responsibility to prove that the above is not the case. Here again, it is important that the possibility of extension is specific to economic sector, company, and characterization.

During the extension procedure, NTCA will also examine whether or not the applicant has acted in accordance with the applicable APA resolution in the already closed tax years.

14. Can taxpayers depart from the critical conditions set out in the APA decision during the period affected by the coronavirus pandemic?

Even in the current situation, taxpayers are required to comply with each of the critical conditions without exception, but have the opportunity to initiate an amendment to the APA decision.

15. What are the consequences if taxpayers do not meet the critical conditions?

In the event of non-compliance with the critical conditions, the resolution relating to the determination of the arm's length price shall not apply from the very date on. As a result, the decision ceases to be binding.