

2007

Yearbook

Information about
the activity of the
Hungarian Tax
and Financial Control
Administration

YEARBOOK

A REVIEW OF APEH ACTIVITIES IN 2007

A Publication of the Hungarian Tax and Financial Control Administration for the 17th Year



BUDAPEST, 2008

CONTENTS

FOREWORD OF THE PRESIDENT	5
INTRODUCING APEH – IN BRIEF	7
TAX ADMINISTRATION ACTIVITIES IN FIGURES	8
Revenues and Refunds	8
MAJOR REVENUE ITEMS OF THE GENERAL GOVERNMENT	10
Personal Income Tax	10
Value Added Tax	11
Corporate Income Tax	12
Simplified Entrepreneurial Tax	13
Social Security Contributions and Health Insurance Contributions	13
Revenues Collected from Duties	13
SERVICES PROVIDED BY APEH	14
Registration of taxpayers	14
Providing information and electronic services (Customer service)	14
Integration of duties	16
The changes in connection with tax returns and electronic filing (Processing tax returns)	16
Account statements	17
Provision of information for external organisations	18
ACTIVITIES OF APEH AS AN AUTHORITY	19
Tax audit	19
Debt recovery, enforced collection and liquidation	21
General legal cases	22
Administrative decisions, appeals and legal remedies	23
Criminal charges	24
Gambling supervisory activities	24
Operation	24
International relations	25
Organisational Structure of the Head Office as of 1 st June, 2007	27
Organisational Structure of the Central Hungarian Regional Directorate 2007	28
Organisational Structure of the Large Taxpayers Directorate 2007	29
Organisational Structure of a typical Regional Directorate 2007	30
Contact details of the Regional Directorates	31

FOREWORD OF THE PRESIDENT

On behalf of the Management of the Hungarian Tax and Financial Control Administration (APEH), it is my pleasure to greet the readers who are holding our annual booklet published for the 17th time now.

Year 2007 was a special period in the history of APEH, marking the 20th anniversary of its establishment. We began the year by changing the hierarchy of the organisation from the traditional county level to regional level, and had the task of setting up the Directorates to operate in their new respective areas of competence. Simultaneously, the integration of the Supervisory Agency for Gambling (dissolved as of 31 December 2006), as well as of the metropolitan and county level duty agencies into our organization, were completed.

In addition to organizational restructuring, the scope of APEH activities was extended by numerous new tasks. These included particular focus on audits conducted into the growth of net worth of "ten thousand" private individuals; a series of actions aimed at whitening the black economy; managing employers' declarations; the operations of the Contact Center, which has been reorganized at regional level, and making electronic filing of tax returns universal; as well as the launching the Centralized Audit Directorate empowered with national scope of competence.

However overwhelmed we were with work, we had to remember our most important duty, i.e. ensuring the revenues for the General Government.

During last year, almost all estimates regarding the planned revenues were overperformed. On APEH accounts HUF 8,654 billion (EUR 33.3 billion) were realized, which was HUF 1,490 billion (EUR 5.7 billion) more than the previous year's receipts. In order to reach it, we paid special attention to fulfill effectively our duties both as a service provider and as an authority. We conducted audits focusing on scrutinizing the high-risk taxpayer groups or economic processes and schemes. In order to enhance the taxpayers' sense of being controlled, we increased our presence as an authority, and the broad application of targeted selection for audit contributed to significant improvement of our audit results. Translated all this into the language of figures it meant that the net tax difference (change) found in the framework of subsequent tax auditing amounted to HUF 356.5 billion, (EUR 1.4 billion) exceeding the previous year's result by HUF 54 billion (EUR 208 million).



János Szikora
President



Lászlóné Varga
Vice President



Péter Polgár
Vice President



Ferenc Kiss
*Finance and Logistics
Manager*

As a result of the numerous measures to collect tax and contribution arrears in the shortest possible time, the results of our enforcement activity were better than in the previous year, producing over 17 percent more receipts than in 2006.

Slowly it has become usual that we face extended requirements year by year, as has also the fact that our organisation - making use of the available resources - wishes and is capable to meet decently these requirements.

We can proudly say that in 2007, APEH succeeded again in effectively carrying out an extremely complex set of requirements as a tax administration.

This year also a summary of the most important information regarding these results are in our Yearbook, which will continue to be published as a tool providing authentic information about our activities to everybody who might be interested in our multifaceted work.

Introducing APEH – In Brief

The largest part of taxes and social security contributions indispensable for fulfillment of public tasks are collected by APEH. The national tax authority was established as part of rolling out the new taxation system in Hungary in 1988. While its responsibilities have been almost continuously extended since, the organization was subject to restructuring several times. Only one of its numerous features has remained stable, that it has always managed to fulfill its statutory obligations and satisfied expectations raised by the Government. Flexibility and capability of adjusting to frequent changes have become part of its daily work. It has been facilitated by the fact that the staff can rely upon an IT background that has been continuously upgraded and without which overall operation would be unthinkable today.

In order to collect General Government revenues, APEH operates a taxation system based on self-assessment; consequently, it has to ensure the conditions that help taxpayers fulfill their obligations. These conditions include: supplying taxpayers with Tax Identification Numbers; keeping up-to-date records of personal data they provide, including the changes (e.g. moving of registered seats); designing tax return forms and making them available for the taxpayers; processing the completed and filed returns in order to post them to the taxpayers' accounts and aggregating information on the national economy. As the other side of the account reflects whether the fulfillment of the financial obligation has taken place, therefore, the invoices and postal orders needed for payment will continue to be provided and the paid amounts identified, so that they can be posted on the accounts.

APEH, as an authority, is also responsible for revealing the cases of tax evasion and collecting overdue taxes to the largest possible extent. To do that, it conducts audits and recovers debts. Achieving improvement in compliance is also an expectation, the statutory provisions however, offer only rather indirect ways to make it prevail (e.g. closure of outlets, making VIR lists*, and publishing the list of defaulting taxpayers). In addition, the statutory provisions entail tasks for the organization concerning other revenues as well (for example withholding public dues, membership fees collected and other dues recovered for private pension funds). As of 2003, the national tax authority has carried out these functions acting in accordance with its medium term strategy, taking into account the interests of both the state and the customers (a "service-provider tax administration"). While adhering to these two main strategic directions, a significant extension of responsibilities has taken place in 2007 (dealing with employees' and social security insurance holders' announcements, assumption of the functions of the duty agencies, as well as the Supervisory Agency for Gambling) and organizational restructuring (organizing the Large Taxpayers' Unit/Directorate of nation-wide competence and the seven regional directorates). All these issues raised the need for developing strategic objectives for the next medium term period.

* A list of privileged taxpayers paying the largest amounts of taxes

It was ten years ago (in 1998) when the tax administration began to set up the conditions for electronic taxation, in an environment that offered more opportunities year by year, as its conditions improved. In accordance with Government efforts, in 2007 new and remarkable steps were taken in the area of improving the practices applied in electronic public administration, and in the ongoing improvement of customer-friendly taxpayer services. As of that year, the obligation to file tax returns electronically has become universal, with the exception of private individuals. That was possible through carrying out a broad information campaign for masses of taxpayers, while APEH faced the challenge of designing and operating IT applications capable of smoothly receiving and processing returns filed electronically on a larger scale than ever before. The bulk of documents arriving and moved electronically has brought changes in thinking in the area of authority procedures (audits, debt recovery, etc.) and needs an IT background implying new dimensions (e.g. in identification of high-risk taxpayers). Compliant taxpayer activities are supported by significant extension of the various information databases published on APEH's home page on the internet (e.g. suspended and terminated tax numbers, the list of VAT-subjects). All these things could contribute to "whitening" the black economy, i.e. compliance should become universal rather than non-compliance.

TAX ADMINISTRATION ACTIVITIES IN FIGURES

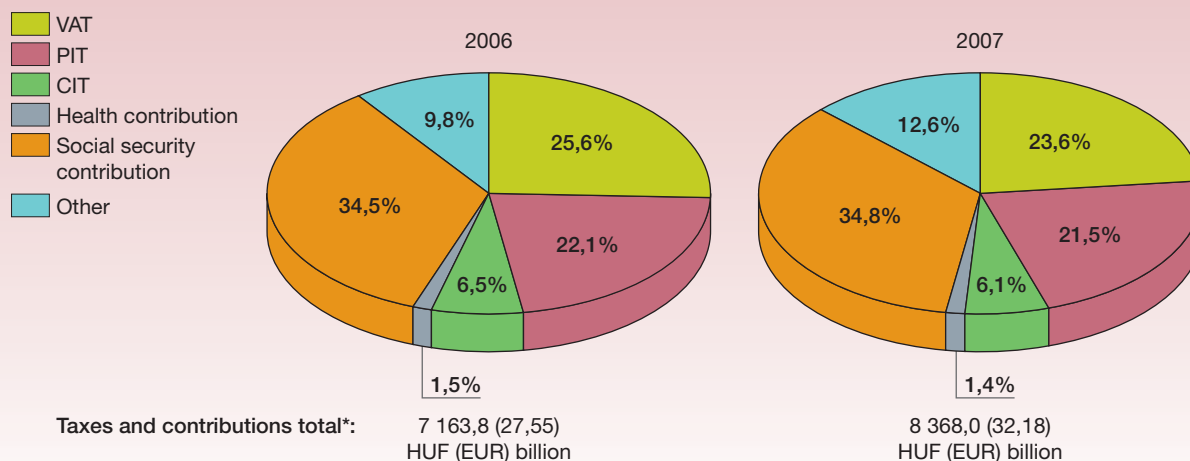
Revenues and Refunds

In 2007 the amount collected by APEH from taxes and social security contributions rose to HUF 8,654 billion (EUR 33.3 billion*), exceeding by 20.8 percent, i.e. HUF 1,490 billion (EUR 5.7 billion) the revenues in 2006. The total sum of revenues also included those types of revenues that arose from the new activities assumed by APEH as of 1st January 2007. Such receipts were generated from various duties and settlement of accounts in relation to private pension funds. The related money flow amounted to HUF 286 billion (EUR 1.1 billion), which was not part of the General Government revenues. 82.4 percent of the combined revenues of the central budget and various funds, were collected by APEH, amounting to HUF 8,368 billion (EUR 32.2 billion). The substantial majority of surplus revenues in 2007 were attributed to income type taxes (e.g. social security contributions, personal income tax, and corporate income tax). The increase within these tax types amounted to HUF 848 billion (EUR 3.26 billion), resulting from realized wage increases as well as changes in statutory provisions involving taxation conditions and contribution rates. In addition, the achieved results were increased by the fact that supplementary taxes levied on private individuals and corporations were taken into account among the revenues in their full amount in 2007. As to value added tax, the positive balance of payments was somewhat lower due to the refunds claimed by

* For every amount referred to in the present document: 1 EUR = HUF 260.

enterprises, owing substantially to their exports and investments. Nevertheless, from this tax type HUF 147.4 billion more revenues (EUR 566.92 million) were realized, than in the previous year.

Distribution Ratio of Revenues from Taxes and Contributions



* / Receipts in 2007 without receipts of Private Pension Funds

Refunds of Taxes and Tax-like Revenues

Items	2006 in million forints (in million euros)	2007 in million forints (in million euros)
Total refunds	1 503 830,7	1 770 818,4
	5 784,0	6 810,8
of which:		
VAT	1 264 364,7	1 480 106,7
	4 862,9	5 692,7
CIT	72 450,3	93 497,9
	278,7	359,6
PIT*/	97 201,4	122 421,3
	373,9	470,9
Social Security, Health Contribution	41 751,7	13 401,9
	160,6	51,6
Tax differences revealed voluntarily	8 555,9	25 080,8
	32,9	96,5
Surtax on Larger companies		7 786,5
		30,0
Surtax on Financial institutions and entrepreneurship		3 604,3
		13,9
Duties (without tax procedures duties)		4 730,7
		18,2
Surtax on overdue payment	2 027,2	2 518,0
	7,8	9,7
other	17 479,5	17 670,3
	67,2	68,0

Note: */ the 2006 PIT outflow data was corrected by 16497 million forints (63,45 million euros), due to misreporting of net accounting organisations in May

As a result of APEH's audits, enforced collection and sanctioning activities, the position of the General Government improved by nearly HUF 326 billion (1.25 billion EUR), exceeding by HUF 40 billion HUF (EUR 153.85 million) the revenues in the previous year. Enforced collection of taxes and contributions was 241 billion HUF (926.92 million EUR), 25.6 billion HUF (98.46 million EUR) more than in the previous year. In addition, as a result of one of APEH's new assignments, the tax administration managed to cut down the delinquent duties by HUF 14.7 billion (EUR 56.54 million). Collection conducted on referrals of external agencies produced additional HUF 4.3 billion (EUR 16.54 million) receipts. Pre-refund audits prevented unlawful refund of HUF 30.6 billion (EUR 117.69 million), HUF 2.9 billion (EUR 11.15 million) less than one year before. Sixteen percent of the rejected claims occurred in audits conducted on foreign taxpayers.

In 2007, APEH paid HUF 348 billion (EUR 1.34 billions) subsidies to applicants, exceeding by 24 percent the disbursements in the previous year. From resources provided by the Ministry of Agriculture and Rural Development, the Tax Administration disbursed nearly 32 billion HUF (EUR 123.08 million) for farming subsidies. The normative farming subsidies as an incentive for employing people with impaired work abilities were somewhat higher than expected, whereas disbursements declined nearly by half. Such decline came about as that kind of support was terminated as of end of June 2007.

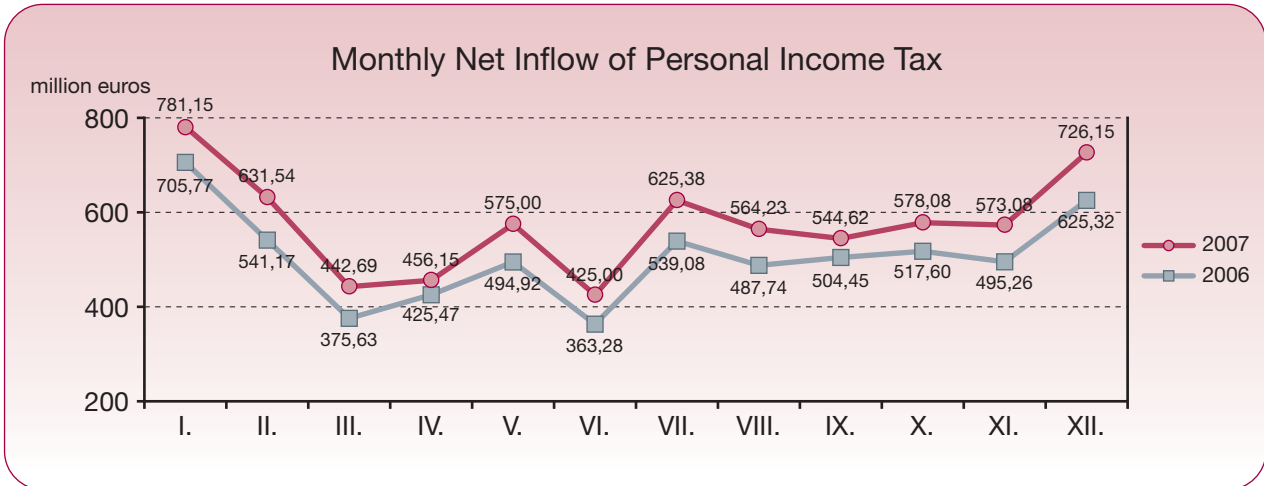
MAJOR REVENUE ITEMS OF THE GENERAL GOVERNMENT

Personal Income Tax (PIT)

The net personal income tax revenues amounted to HUF 1,800 billion (EUR 6.92 billion) in 2007, exceeding the figure in the previous year by HUF 220 billion (EUR 846.15 million). The changes in relation to these two years were - in addition to increased wage levels - substantially influenced by the modifications in the tax regulations. One of the most remarkable changes was related to the aggregated income level, as from 2007, leaving the actual rates unchanged, the yearly income level for the upper tax rate of 36 percent was increased from 1 million 550 thousand HUF (EUR 5961.54) to 1 million 700 thousand HUF (EUR 6,538.46). Under another new provision, pensions will be included in the aggregated income of individuals as of 2007 and that had to be taken into account for the first time when the amount of tax advances payable for year 2007 were calculated.

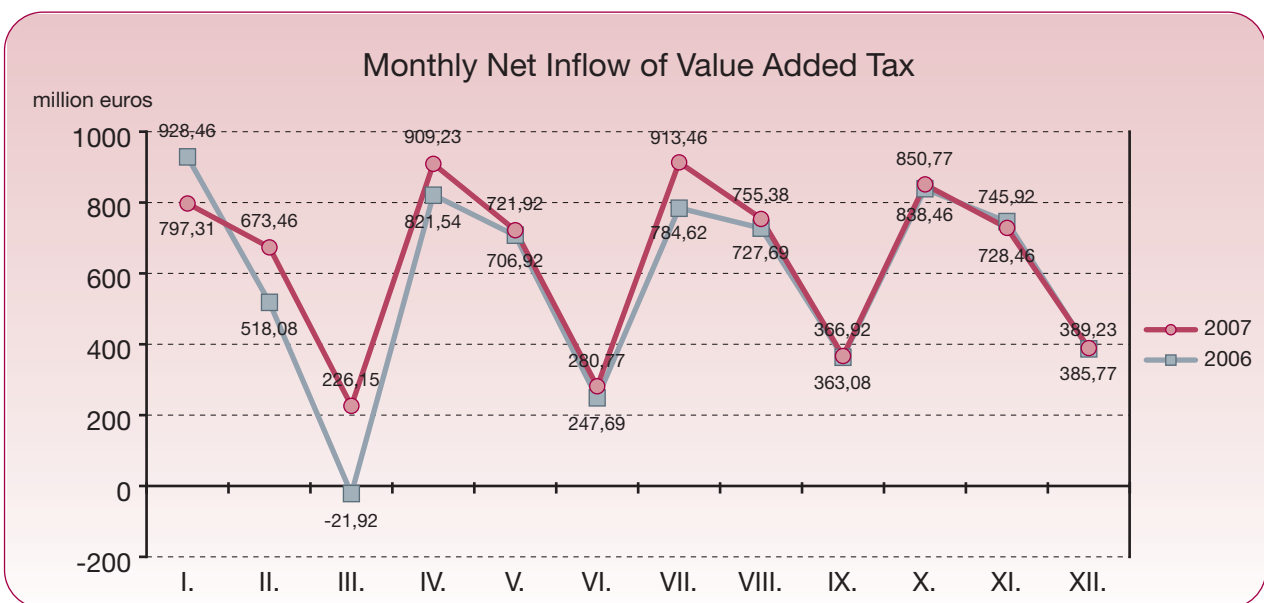
The net tax revenues resulted from HUF 1,922 billion (EUR 7.39 billion) payments and 122 billion (EUR 469.23 million) reimbursements made during 2007. The volume of payments and reimbursements exceeded considerably the amount in 2006, which is - in addition to the factors mentioned in the context of net revenues - attributed to the fact that in 2007 the way of filing personal

income tax returns had changed considerably. From the previous year's 55 percent, the number of taxpayers filing their tax returns based on self-assessment rose to 76 percent, while the number of taxpayers that settled accounts with their employer dropped simultaneously.



Value Added Tax (VAT)

Last year the amount of value added tax revenues were defined by the termination of the reduced tax rate of 15 percent from 1st September, 2006. After that date, the products and services that were earlier subject to the reduced 15 percent VAT rate became subjects to the universal 20 percent rate of VAT. An additional significant change took effect with the accession of Romania and Bulgaria to the European Union on 1st January, 2007, as the goods coming from and directed to these countries, qualify as intra-Community trade in the VAT system.



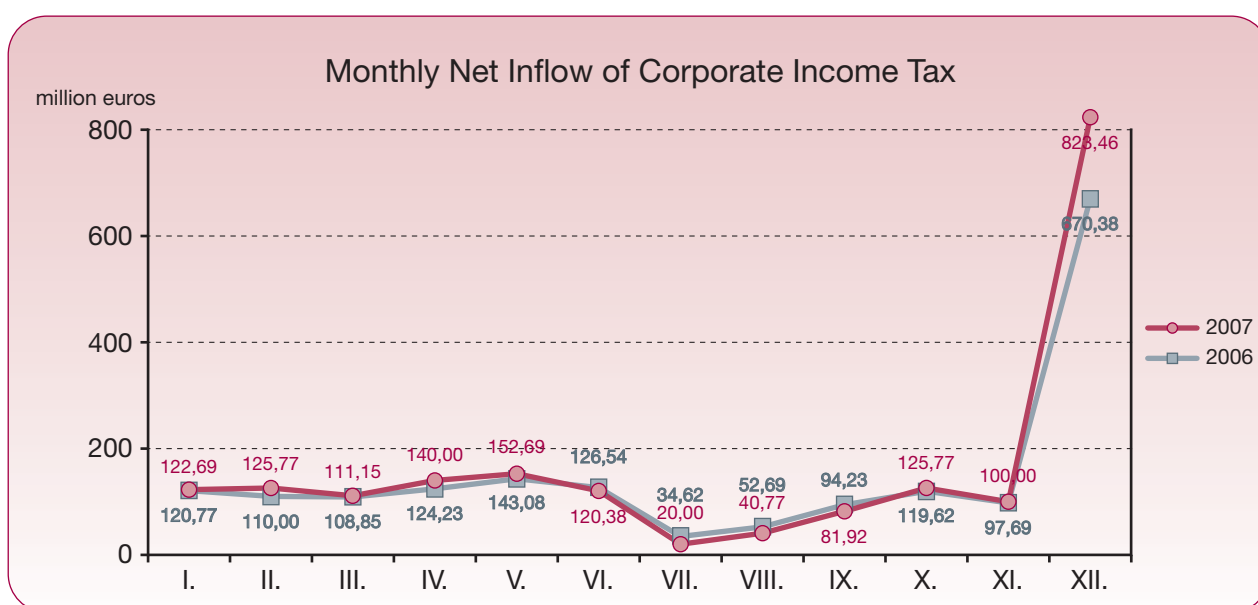
In 2007, the revenues from value added tax - substantially as an effect of termination of the 15 percent rate in September 2006 - were considerably, by 8 percent higher than that of 2006. These amounted to HUF 1,979.4 billion (EUR 7.61 billion) net revenues for the central budget, exceeding by HUF 147.4 billion (EUR 566.92 million) the receipts in the previous year. The considerable increase in net revenues took place along with a nearly 12 percent increase of payments and 17 percent increase of reimbursements.

Corporate Income Tax (CIT)

The changes in legislation on corporate income tax and dividend tax in 2007 were motivated by considerations such as improving competitiveness, encouraging employment, ensuring application of the European Union legislation and improving the contribution of businesses to public expenditures by taking their fair share in paying tax.

The change in corporate income tax legislation influencing the volume of net revenues took effect on 1st July 2007, and relates to the tax payment obligation on minimum incomes (profits), applied to those undertakings whose profits before tax or corporate income tax base are lower than a minimum amount of income (profit). These enterprises have two choices. They shall either make a declaration, or pay a tax using the minimum income (profit) as their tax base.

At national level, companies paid HUF 604.3 billion (EUR 2.32 billion) corporate income tax in 2007, representing an increase of 12 percent, i.e. HUF 63.2 billion (EUR 243.08 million) as compared to the gross revenues in 2006; while the net corporate income tax revenues to central budget were HUF 510.8 billion (EUR 1.96 billion). Because of a moderate increase in payments versus refunds, the net revenues in 2007 exceeded those of 2006 by 9 percent.



Simplified Entrepreneurial Tax (SET)

In Hungary this type of tax has been an option for entities to choose since 1st January 2003 provided their annual earnings remain under a certain income limit; typically for individual entrepreneurs (= self-employed individuals), partnerships, limited partnerships, lawyer firms, patent and trademark firms. The SET is - as suggested by its name - a combined tax type, replacing corporate income tax, VAT, entrepreneurial personal income tax, entrepreneurial dividend tax, and company car tax. The growth of SET payments continued in 2007, although somewhat less dynamically. The net revenue was almost HUF 10 billion (EUR 38.46 million) higher, that is 6.8 percent more than in the previous year. The increase came primarily as an effect of the tax rate increase.

Social Security Contributions and Health Insurance Contributions

The social security payments to Social Security Funds were substantially modified by the changes in legislation implemented in 2006 and 2007. The amount of individual health insurance contribution increased and the employers' payments were rearranged between Health Insurance and Pension Funds. The overall 29 percent contribution rate did not change, but the contributions paid to the Health Insurance Fund dropped from 11 percent to 8 percent.

The changes in liabilities to Pension Funds were substantially effected by the rearrangement of employers' payments, from which source the Funds collected 84.6 percent of their total receipts. The introduction of the 8.5 percent contribution payment liability by persons continuing work after retirement also had an impact toward increasing the receipts. The upper limit of daily pension contribution increased from HUF 17,330 (EUR 66.65) to HUF 18,490 (EUR 71.12), and its annual amount rose to HUF 6,748,850 (EUR 25,957.12). The budget law contained HUF 2,760.9 billion (EUR 10.62 billion) estimates from social security contributions for 2007. The actual revenues were HUF 2,893.3 billion (EUR 11.13 billion), exceeding the estimates by 4.8 percent, and the revenues in 2006 by 17.6 percent.

Revenues Collected from Duties

A fundamental change took place as of 1st January, 2007, as the duty agencies merged into the organization of the tax administration. Such merger rendered the collection of duties to be paid in the form of money (overwhelmingly levied on acquisition of property) under the competence of APEH, while the procedural duties mostly taking the form of stamps remained the competence of other agencies. The revenues collected by the duty agencies or, from 2007 by APEH, are to be reallocated between the central budget and the local governments of counties and cities of county rank.

APEH collected and allocated HUF 136 billion (EUR 523.08 million) from duties in the year 2007.

SERVICES PROVIDED BY APEH

Registration of taxpayers

The number of operating taxpayers, minus private individuals increased by 3.6 percent in 2007. The number economic organizations with legal entity status continued to grow gradually, the growth this time was 7 percent. Nearly 29 thousand newly established businesses began their operation as opposed to somewhat more than 13 thousand businesses ceasing activities. The share of economic organizations with no legal entity slightly, by the 2.5 percent decreased. Now nearly 128 thousand corporations have a community tax number, they grew by 23 thousand in 2007, by 3 thousand more than in the remarkable boom in the previous year.

The number of individual entrepreneurs, though moderately, continued to decline. Behind the balance of minus 10 thousand, there is still significant trade. More than 37 thousand people applied for new individual entrepreneurship passes. Nearly 47 thousand, however, exited from this taxpayer group.

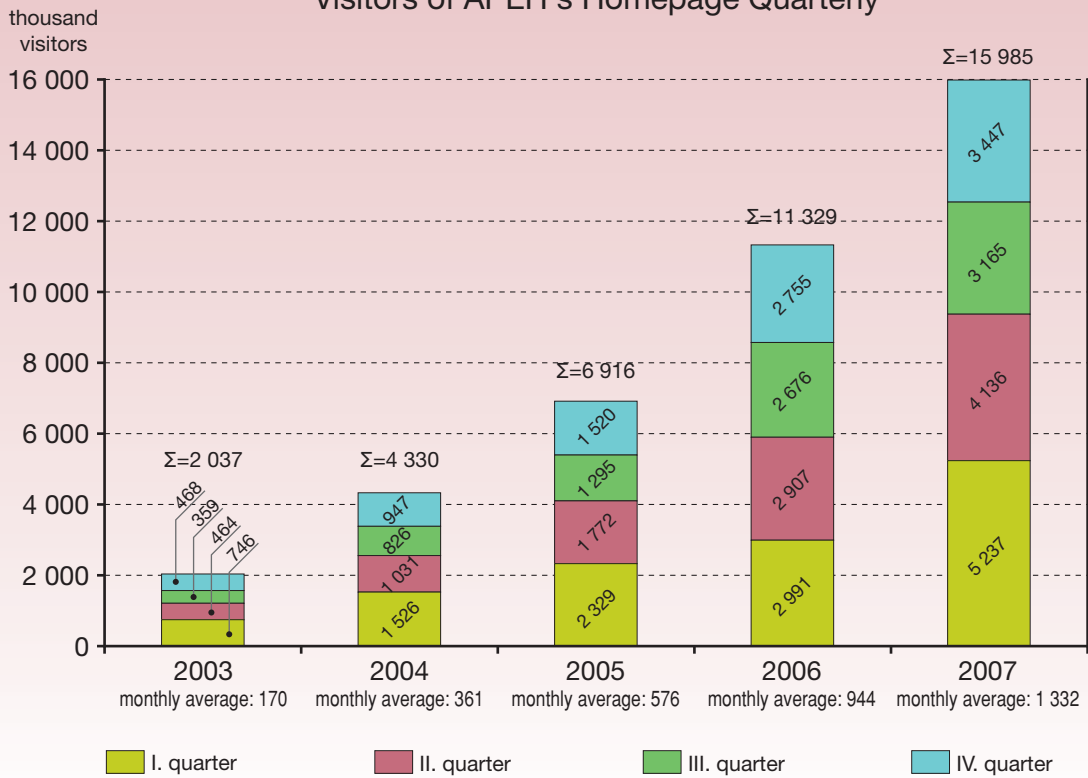
Remarkably, the number of private individuals carrying out independent activities with a tax identification number grew by nearly 18 percent, reaching 41 thousand people. The underlying reasons are in the law. The agricultural primary producers are required to have tax ID numbers with effect of 1st January, 2008, which explains the huge tide of applications.

Providing information and electronic services (Customer service)

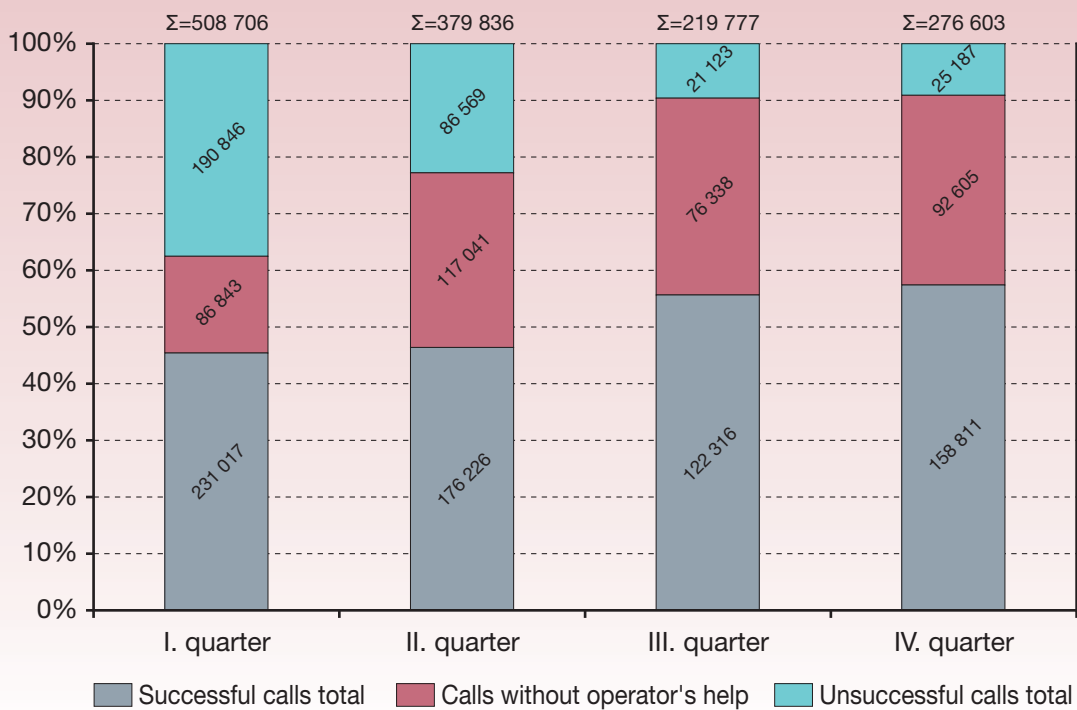
The frequent changes of legislation became more intensive in the latest couple of years, in which context the Tax Administration considers as its priority task to provide appropriate information and support for taxpayers in order to help them comply with their obligations. To circulate information APEH made use of many communication opportunities this year. Among these APEH home page has priority. Interested taxpayers made nearly 16 million visits at this forum and completed more than 20 million downloads, indicating dynamic extension of customer contacts. The Hungarian Tax and Financial Control Administration plays a key role in the Hungarian public administration providing electronic services, and maintaining accessibility of its home page for public interest. The services were used and the various queries made quasi irrespective of time, most frequently in relation to submitting tax returns, queries for tax accounts, contributions and tax returns data.

Due to taxpayers habits for obtaining information there were constant demand for verbal and personal contact, despite opportunities offered by the home page. To satisfy such demand, the taxpayer service and the information organization were rearranged and in every directorate unified business hours schedule was implemented (receiving customers on every weekday) involving

Visitors of APEH's Homepage Quarterly



Telephone Statistics of APEH's Contact Center in 2007



substantial staff rearrangement. In the course of the year the telephonic information system, the so-called Contact Center (CC) was refurbished, which made way for receiving and handling incoming calls as well as obtaining basic information automatically.

Integration of duties

The process of taxation was significantly affected by the implementation of duties' integration effective as of 1st January, 2007. The merger of duty agencies into the national Tax Authority required tremendous efforts as there were connected procedures regulated in a different manner and therefore had an impact on every area of APEH. The integration proceeded gradually, aimed at creating harmony between taxation and the responsibilities with respect to duties, in other words setting up a method allowing the management of taxes and duties in a unified manner. The priority was to keep the workflow uninterrupted in a way that customers should not be bothered by the difficulties of APEH. To that end, taxpayers were informed adequately and timely.

In order to co-ordinate the extremely complex process of integration, a working group was set up. With its help, sample documents were unified and an internal regulation was published directed to levying, accounting for and bookkeeping the duties as well as assessing the market value of properties. In (cash) payments of duties at post offices the use of postal payment vouchers represent a considerable part; therefore, the tax administration continued to provide these order forms to the taxpayers.

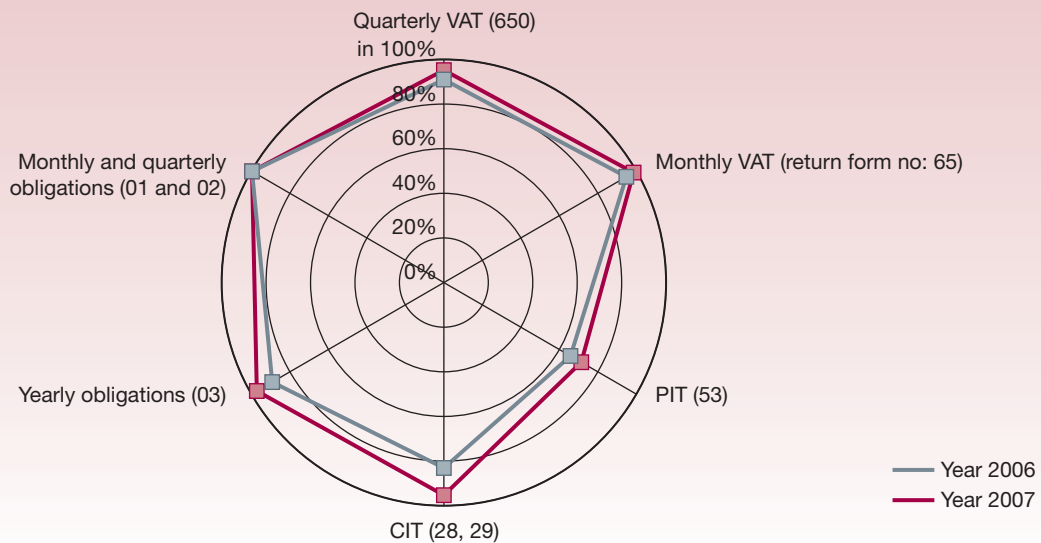
The changes in connection with tax returns and electronic filing (Processing tax returns)

The taxpayers are responsible for fulfillment of their obligations using various tax return forms. By year-end 19.1 million returns and 7.7 million control-information provisions were filed. The majority of returns were filed electronically.

The processing of returns arriving electronically became easier and faster, however, electronic filing did not result in lowering taxpayers' errors automatically. During the year, the tax administration's eBEV system received 24.8 million returns and documents providing information, from these 34 percent were social security contribution returns, 11 percent VAT returns and self-made revisions, 34 percent employers' tax assessment and control data, 21 percent PIT returns and other information.

In 2007 private individuals had the opportunity to offer one percent of their personal income tax for the eleventh time to an NGO and another 1 percent to a church or an earmarked important item within the central budget. 1,688 thousand private individuals donated one percent of their tax on 2.7 million declarations. Nearly HUF 15 billion (EUR 57.69 million) were offered for 27,800

Ratio of Tax Returns Filed in Paper Form or Electronically, Prepared with Assistance of Internet Programme



beneficiaries, 56.5 percent of the theoretic maximum amount. From that HUF 8.8 billion (EUR 33.85 million) were allocated to 27,600 NGOs, 143 churches received HUF 4.3 billion (EUR 16.54 million), and to the earmarked appropriations of the central budget (their number has grown to six by this year) HUF 1.9 billion (EUR 7.31 million) were offered. Some beneficiary civil organizations - 2.5 percent - did not wish to collect the amount offered, and the Tax Authority rejected 1.8 percent of the requests for disbursement by beneficiaries. In connection with "personal income tax 1-1 percent" for public good, the Tax Administration also fulfilled its publishing obligation.

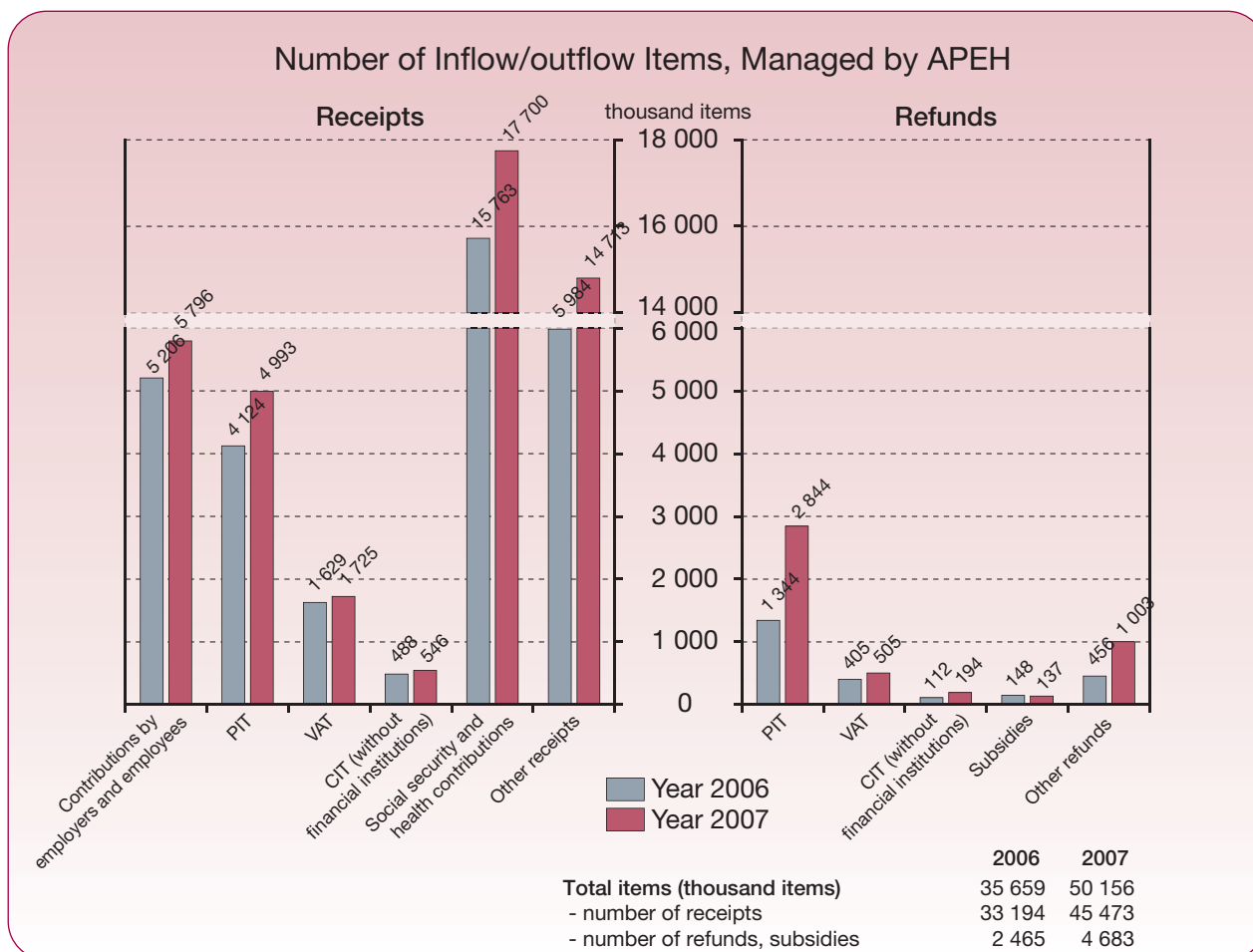
With support from the Ministry of Finance, the Tax Administration launched a tax returns modernization programme aimed at creating user-friendly return forms that are modern both in their look and in content. In order to make the new tax returns acceptable by the widest possible scope of people, the Tax Administration organized a Returns Modernization Forum for professionals representing the MoF, the Chambers, the IT Businesses' Association, and the Central Statistical Office, where the professional representative bodies participated and had an opportunity for exchanges.

Account statements

In the money flow system for handling the different payments and disbursements, more than 50 million entries were processed, being mostly bank transfers, exceeding by 41 percent those of the previous year. Due to the flows on new accounts opened at the start of the year, the number of both bank and postal payment entries increased, in total by 37 percent. The reimbursements and subsidy disbursements almost doubled, reaching 4.7 million. Nearly two-fifth of disbursements was related to social security contributions and health contributions, while 60 percent of

reimbursements involved personal income tax. As an effect of growth in money flows, the number of unidentified entries increased considerably.

Provision of information for external organisations



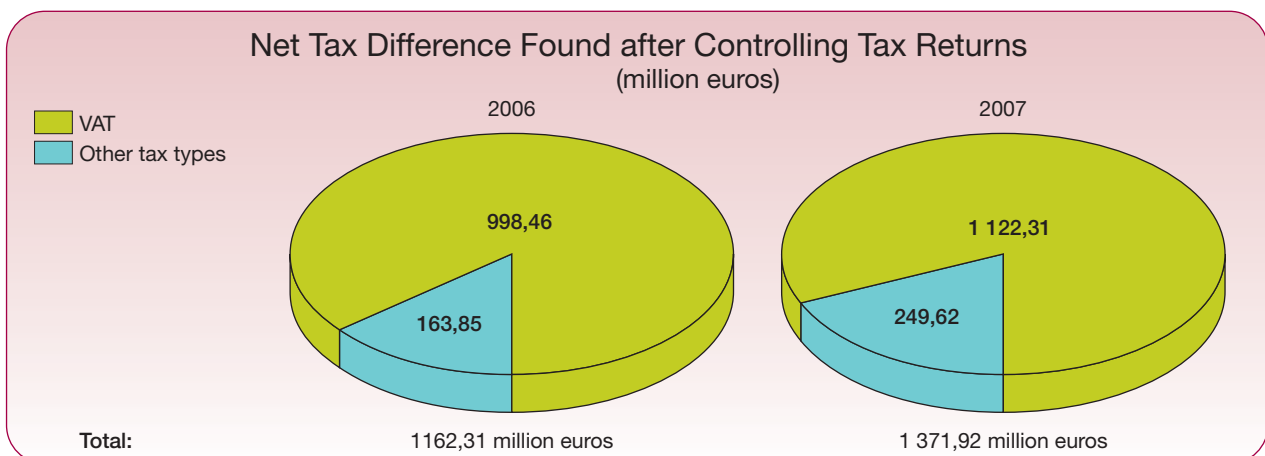
The demand for provision of information by APEH and its frequency continued to grow on grounds of statutory provisions, co-operation agreements and on ad hoc referrals. One of the reasons is that the tax authority receives employees' and social security insurance holders' announcements, and as of the start of the year, the membership fees payments made to private pension funds, then the required information is forwarded to the adequate public organizations, health funds and pension funds. The Tax Authority provides information in accordance with its international obligations, required for settlement of VAT-based payments within the EU, about public enterprises, and for intra-Community trade statistics from VAT returns.

ACTIVITIES OF APEH AS AN AUTHORITY

Tax audit

The important audit tasks and objectives in 2007 - such as auditing assets (property) growth, high-risk taxpayer groups and economic processes, fulfillment of social security contribution obligations, the audit of announcements in connection with the minimum contribution base, natural gas price subsidy audits, declaring "zero tolerance" against evasion - were implemented in a different organizational structure and through applying numerous new audit methods by the Directorates.

The managers of the APEH, the Hungarian Customs and Finance Guard Headquarters, the Hungarian Labour Inspectorate and the National Consumer Protection Authority developed an overall strategy in the framework of the so-called "four-agency co-operation", in order to improve efficiency in the fight against black economy as well as react in a unified and rapid way to serious infringements experienced in other areas.



While the number of audits decreased as compared to the previous year but their effectiveness and efficiency improved. The net tax owed of HUF 357 billion (EUR 1.37 billion) revealed as a result of completed audits, was about one-fifth more than in the previous year. The majority of findings were realized again in value added tax despite its decreasing proportion. The distribution of the net tax owed assessed among the taxpayer categories changed substantially, because of a shift in the focal points determined at the start of the year, as compared to the previous year. The share of individual entrepreneurs and private individuals rose to more than twofold, whereas the weight of organizations with legal entity and of those with no legal entity declined by 8-10 percent.

Owing to the organizational restructuring, changes in legislation, as well as the experiences gained during audits, a need was identified for unifying the applied systems, and thinking over the IT support behind the work processes. Therefore, from the start of the year, the Centralized Audit

Directorate (KESZ) started its operation; a unit with national scope of competence, also reaching across boundaries, established with a view to auditing fraudulent schemes, such as "invoicing round", involving complete business groups and supply chains. The activities of "Rapid" teams are closely connected with the preparations for audits, and the mapping of the ever-renewing techniques of tax avoidance. The importance of audits carried out by auditors working in teams grew in order to increase the control by the Tax Authority. Supported by EU, projects were launched designed to increase the efficiency of selection for audit based on risk assessment in the framework of international co-operation, as well as projects aiming at improving the audit of supply chains.

The number of audits completed at some level was more than 246 thousand.

Utilisation of audit capacities by type in 2007 (in %)		
Audit types	Utilisation of yearly auditing capacity (%)	
	planned	fact
Audits aiming at ex post control of tax returns, including simplified control	66,4	65,1
of which:		
– Auditing the largest taxpayers	9,6	13,2
– Net wealth growth audits	22,6	28,3
– Audits following amendment of tax returns	0,1	0,1
– Prompt audits	–	0,2
– Audit of transforming, dissolving entities and undertakings ceasing operations	13,5	13,4
– Audits before allocation of funds	10,0	10,2
Audits on redemption of government guarantees	0,1	0,1
Audits to control fulfillment of certain tax obligations	25,2	25,7
Audits to collect data	8,0	8,8
Repeated audit on periods already closed by earlier audits	0,3	0,2
Other audits, outside the scope of the Act on rules of Taxation	–	0,1

Responding to Government expectations published at the start of the year, the Directorates carried out a large number of audits concerning coherence between the private individuals' incomes and their worth growth. The audits were conducted based on unified principles, applying IT support. More than two-third of the audits closed with a change (new amount assessed), the average net tax owed per audits was HUF 4 million. However, the delaying and thwarting tactics used by the taxpayers seriously hindered the rapid completion of audits. As a result of 77.6 thousand completed audits carried out in order to tackle taxpayers' evasion tactics posing the worst threat to the social security funds' revenues, the amount of the owed contributions exceeded HUF 12.6 billion (EUR 48.46 million). According to experiences, in areas typically requiring a lot of work force, the fictitious subcontractors' chains and unregistered employment of workers continue to be common.

In order to fight black economy APEH paid special attention to frequent changes in registered seats and owners, newly established enterprises, recurrent non-filers as well as to enterprises

steadily reporting deficits. Furthermore, in the course of conducting value added tax type audits, auditing of the schemes causing tremendous losses, such as invoicing in a circle, the supply chains, the lawfulness of intra-Community transactions, and those who minimize their obligations where the actual profits are gained from fictitious or only partially real activity was an important task.

During the year, the Directorates habitually controlled fictitious enterprises, mostly found in trading with computer parts, cellular phones, and automobile parts. These audits continued to reveal considerable infringements; therefore, both the ratio of audits closed with a change (new amount assessed) and the tax difference revealed continue to be high. In the business of trading wastes however, the reverse tax charge mechanism was implemented, resulting in considerable decline in the number of changes (new amount assessed).

Based on conventions concluded on avoiding double taxation from within the member states of the European Union, as well as from countries outside the Community, 55 referrals were received. The total number of referrals launched by APEH during the year was 186.

Debt recovery, enforced collection and liquidation

The effectiveness of enforced collection increased, as 18 percent more delinquent taxes were collected in 2007, compared to the previous year's increase of 3 and a half percent. Such substantial growth was possible primarily - in addition to the efficient IT support - because of applying flexible work organization adjusted to the circumstances and the considerably enhanced intensity of the arrears management activity. The Directorates launched enforced collection action in 415 thousand cases during the year to collect the amount of HUF 653 billion (EUR 2.51 billion) owed. Compared to 2006, the number of cases referred to enforced collection grew by 71 percent and its amount increased by 41 percent.

The total receipts from enforced collection were HUF 260 billion (1 billion EUR) in 2007, involving HUF 241 billion (EUR 926.92 million) taxes and contributions, nearly HUF 15 billion (EUR 57.69 million) duties, and more than HUF 4 billion (EUR 15.38 million) receipts from enforced collection based on requests of external institutions. Two-third of the receipts via enforced collection were realized from the delinquent taxes in value added tax and social security contributions.

The largest part of the amount collected by enforced collection continued to result from direct (electronic) collection from taxpayer bank accounts (57 percent), and was prompted by the threat of enforced collection action. In 2007 the Tax Authority seized assets in total value of HUF 82 billion (EUR 315.38 million) but the composition of such amount changed substantially compared to the previous year. Resulting from the option of simplified final settlement available for the taxpayers 7,862 final settlement were initiated in 2007, which exceeded by 40 percent the volume of cases one year before. The number of proceedings completed was 6,326, twenty six percent of which continued as liquidation.

Main indicators of enforcement measures (Pieces)

Name	2006	2007
Enforcement		
Started processes	243 446	415 312
Pending processes (at the end of the year)	191 658	214 059
Processes started by external stakeholders	172 632	162 236
Liquidation		
Initiated processes	5 589	4 644
Started processes	8 809	9 147
Finished processes	6 794	6 525
Pending processes (at the end of the year)	17 800	19 500
Foreclosure		
Started processes	5 593	7 862
Finished processes	4 715	6 326
Pending processes (at the end of the year)	12 000	13 500

Like in the previous years, the collection of public dues to be collected as taxes increased the workload appreciably in 2007. During the year APEH received external requests for assistance involving 162 thousand cases, upon 82 different grounds, and all of the requests were satisfied. The Customs authority and the private pension funds submitted the largest volume of requests for collection of receivables.

General legal cases

The tax administration helped the application of tax laws changing every year by providing information in various forms. The taxpayers turned to APEH primarily in writing - on complex legal tax law subjects, 30 thousand such questions were answered, more than half of them via e-mail. The unified interpretation of laws was supported by nearly 150 opinions from tax professionals published in the Tax and Audit journal, the 21 external actions, initiated by the President of APEH and, in 178 instances, information provision also published on the internet.

The processing of law changes was supported by a complex legal co-ordinatory activity. It took considerable efforts to prepare in a legally adequate way, the various methodological guides, information brochures, model decisions, tax return forms and the instructions for completing tax returns needed for the fulfillment of tax obligations. In establishing a unified adaptation of the legislation, discussions organized on their interpretation at overall APEH level, as well as publishing the guidelines on the Intranet, all played an important role.

Administrative decisions, appeals and legal remedies

As a result of the substantial growth in workload, the number of first instance decisions and rulings issued grew to threefold, and by the end of the year 83 percent of almost two million decisions became definitive. The Directorates issued decisions/rulings/orders of payment in the largest number (1,630 thousand) in matters involving taxes and duties, two-third of which were related to duty issues.

Within the legal remedy system, the performance of new tasks of APEH as an authority in connection with duty and gambling supervisory issues was satisfactory. Nearly 14 thousand cases were completed at the second instance level. This year fewer taxpayers used the tool of extraordinary legal remedy, 421 cases becoming definitive by first instance and 266 cases becoming definitive by second instance decisions were contested in requests for supervisory action.

The tax administration attaches great importance to lawsuit representation activity, for the adequacy and legitimacy of its work is measured in front of the courts. The quality of lawsuit representation is indicated by the fact that the rate of won lawsuits improved substantially, and largely the courts found the decisions made by APEH legitimate and substantiated.

The tax administration won a lawsuit that may become precedent in the subject of what is called "VAT chain audits". The rulings - considering that these audits pose serious problems not only within Hungary but also outside its borders for the tax authorities - meant a major breakthrough, as a considerable part of VAT frauds are built upon the scheme of invoicing round.

Administrative causes and their verdicts

Data on legal cases */	Units	2006	2007	2007/2006
Causes started in earlier years	pieces	1 267	1 521	120,0
Causes started in the given year	pieces	1 257	2 134	169,8
Causes pending total	pieces	2 524	3 655	144,8
Causes finished in the year	pieces	1 281	1 660	129,6
of which:				
– causes closed by verdict	pieces	922	1 288	139,7
proportion	%	72,0	77,6	107,8
= approval	pieces	670	1 010	150,7
proportion	%	72,7	78,4	107,9
= changed	pieces	36	46	127,8
proportion	%	3,9	3,6	91,5
= invalidated	pieces	216	232	107,4
proportion	%	23,4	18,0	76,9
– annulment	pieces	359	372	103,6
proportion	%	28,0	22,4	80,0

Criminal Charges

Resulting from audit and enforced collection activities, the tax administration detected 1,747 crime cases, the Directorates submitted criminal reports on 1050 cases, and the Gambling Supervisory Department on 21 cases. The detected crimes were perpetrated for the value of HUF 31.7 billion (EUR 121.92 million), and the average amount per criminal report was nearly HUF 30 million (EUR 115,384.61). 91 percent of the detected amount was connected with tax frauds, which are committed with the highest frequency. The average value was remarkably high in respect to tax frauds (HUF 44 million (EUR 169,230.76)), and tax frauds in the context of employing workers, which amounted to more than HUF 20 million (76,923.08 EUR). One quarter of the 1,168 perpetrators reported remained unidentified, and 70 percent of those identified were representatives or members of business associations, 15 percent individual entrepreneurs, and 14 percent of them private individuals.

Gambling supervisory activities

APEH scope of activities was extended as of 1 January 2007, to include supervision of gambling. The tasks of the Department include, among other things, authorization for games, auditing the games' operators and organizers, the relevant record keeping duties. One of its responsibilities is to apply sanctions in cases of failure to comply with the rules; moreover, it plays an important role in fighting illegal gambling and the related advertising activity, and in the battle against money laundering.

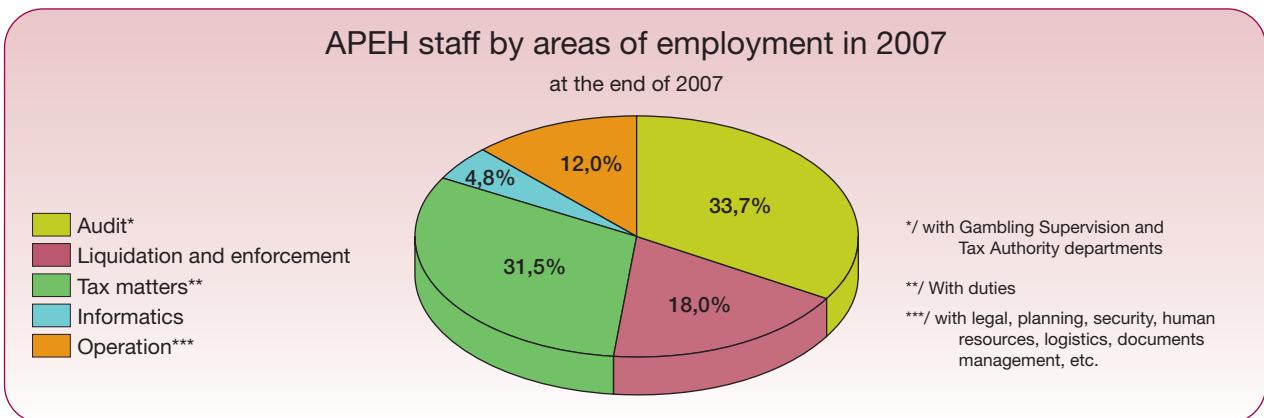
In addition to the supervisory function, another priority was the participation in preparations in connection with concession procedures. The tax authority achieved success by contributing to an expert team set up because of the European Commission proceedings on breach of obligation - launched because of national rules of sports wagering in 2006 - as well as in preparations for creating a work group to take action against illegal on-line gambling.

Operation

Due to organizational restructuring and further extension of responsibilities, changes were carried out within the tax administration, which were greater than ever seen by the staff in the previous years, affecting the overall scope of activities and the whole organization. These things required substantial amount of extra work and continuous control by management. The organizational management tools of the Directorates and the Headquarters, the controlling systems supporting management decisions also had to be adjusted to the new organizational structures, modified functions as well as to changing Government requirements. Almost every internal instruction had to be re-shaped, presidential and management meetings had to be carried out every week, where management bodies were continuously informed on the completion of current tasks, and decisions made with respect to additional work to be done.

Despite the large-scale changes during the year, operation of the performance evaluation system, which had been applied and annually updated in tax administration for several years, was secured and fulfillment of the performance requirements therefore could be monitored.

APEH approved number of staff as of 1 August 2007, increased to 15,635. In the course of the year substantial changes took place concerning the organizational structure, number and position of managers, also including individual changes, ranging from the vice president levels to the section heads. As a result, the number of management positions in the tax administration dropped by 76 people. The 1,717 new positions, which are largely to enhance audit and enforced collection workforce capacity, will be gradually filled in by the end of March 2008. At the same time, the new and vacant positions are increasingly difficult to fill with adequately qualified and experienced professionals, as the labor market positions of the Public Service and therefore of the Tax Administration have been weakening due to less certainty in job stability and a relative lag of wages.



International Relations

As a follow-up to intensive international relations work pursued in the previous years, during the year APEH participated in numerous events involving international and EU tax administrations, and took part actively in international co-operation. We hosted the delegation of the International Monetary Fund (IMF), which had discussions in our country about a possible tax reform. At the end of September - on the request of the President of the Tax Administration - the IMF delegates analyzed the situation taking shape since a similar organizational review conducted in Hungary back in October 2005, the main economic and legislative environment, the functions to be carried out by APEH, as well as the changes affecting the organization. An additional objective of the delegation's visit was to lend a hand in determining the potential directions of future development aimed at creating an organizational strategy on the medium term.

The eleventh General Assembly of IOTA, composed of 40 states' tax administration organizations took place in the middle of June 2007 in Varna, Bulgaria, where the member states elected the Hungarian national Tax Authority into the executive body of the international organization.

Last autumn the European Union tax administrations managers forum (G27) took place in Budapest organized by the Hungarian Tax Authority in the House of Parliament, aimed to discuss the latest strategic issues concerning tax administration. The Budapest talks were the first among such meetings of IOTA held elsewhere than in the capital of the country delegating the President, and its major subject was "The need for efficient external communication as an indispensable tool for encouraging voluntary compliance by taxpayers". In middle-October, APEH took part in the II. ITD World Conference organized in Buenos Aires jointly by the Tax Administration of Argentina, the International Development Bank, the IMF, the World Bank and the OECD. With nearly 220 high-ranking delegates from 72 countries participating in the forum, the main subject was dealing with small and medium sized enterprises from tax policy and tax administration perspective.

In the framework of the FISCALIS Community programme APEH organized a professional seminar titled "How to carry out a Transfer Price audit" in November 2007. At the event of 80 participants, every EU Member State participated.

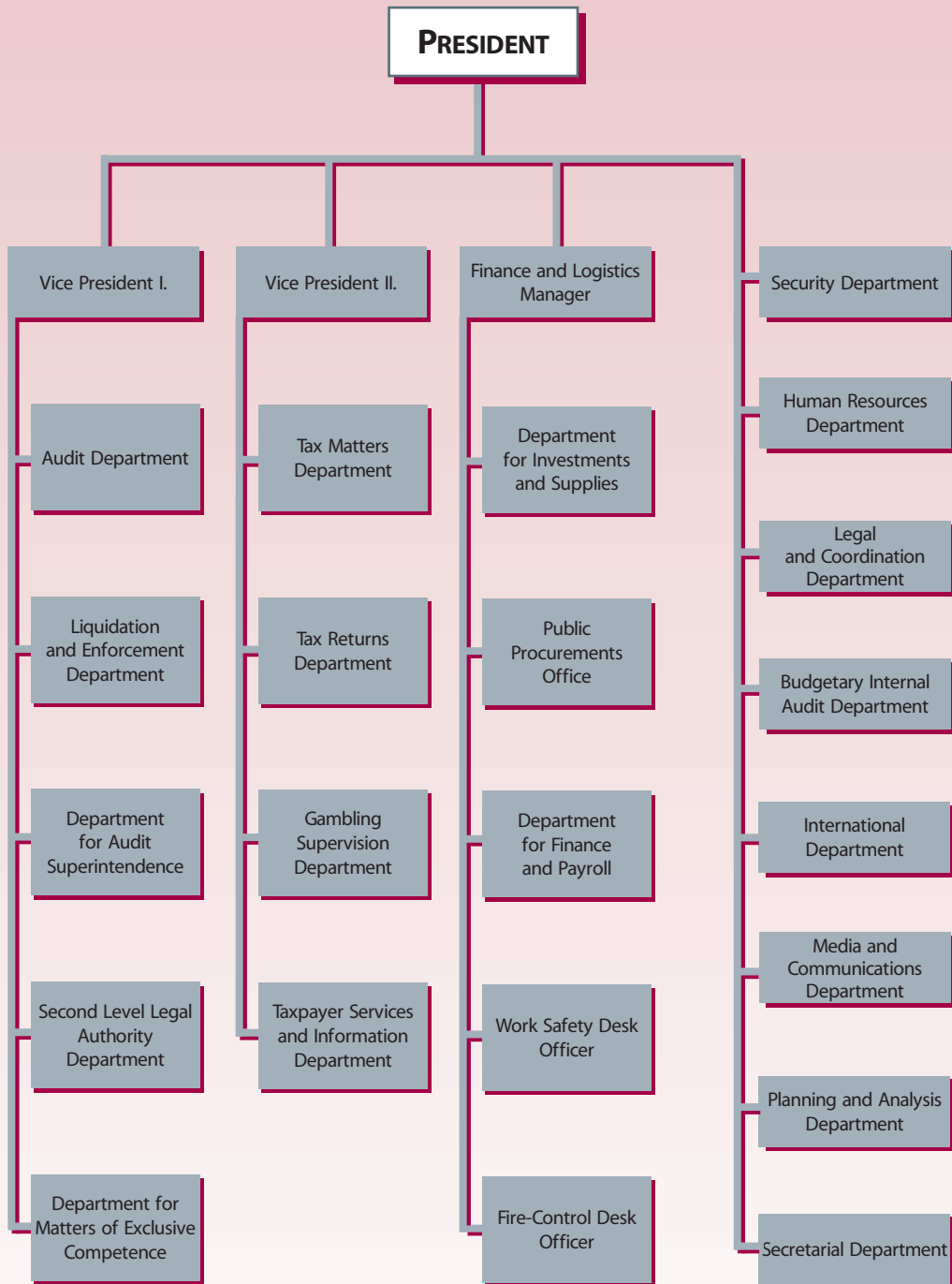
Last year several bilateral meetings took place with the EU Member States' tax authorities and those of other countries outside the Union.

In November APEH concluded a co-operation agreement with the Czech State Tax Authority. We also signed a declaration of intent with respect to strengthening co-operation between the Romanian and Hungarian tax administrations.

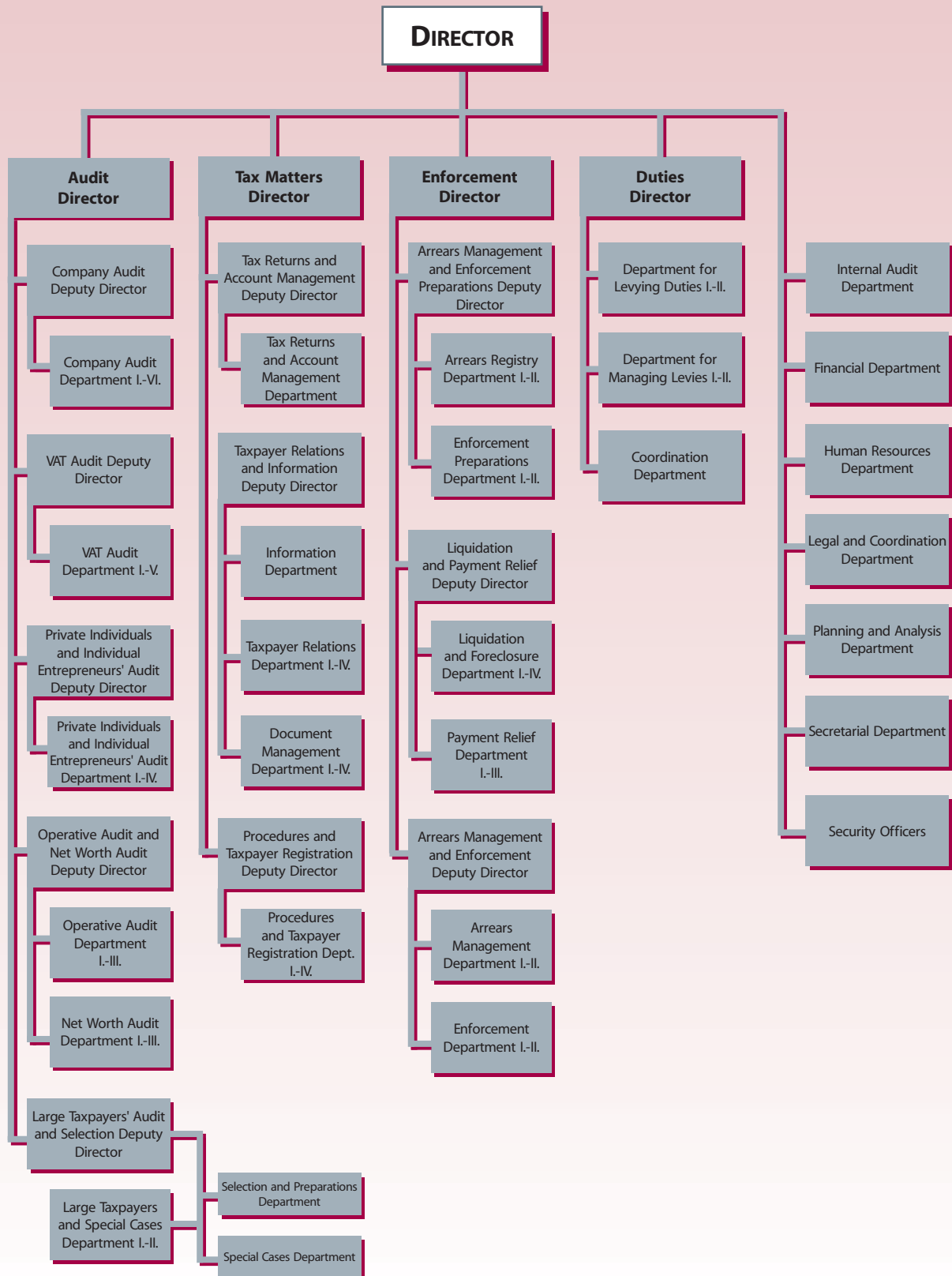
APEH joined to several international projects. In connection with the closing session of the project - concerning transactions of issuing invoices round - held in the middle of December, the methodological aid considered as the main product of the project, which is meant to facilitate the auditors' work and presenting in specific details the audit practices of trading chains, was finalized. The objective of the project is to develop further the software already applied in Hungary for selection for audit based on risk assessment involving external resources. In November within the framework of the project, the specification containing the professional and technical requirements of the software, supporting risk assessment was completed, based on which the public procurement competition can be launched in 2008.

APEH Training Institution, as a member of the TRIAS international consortium, developed the communications module of the EU Leonardo project, accepted by the international partners with acknowledgement.

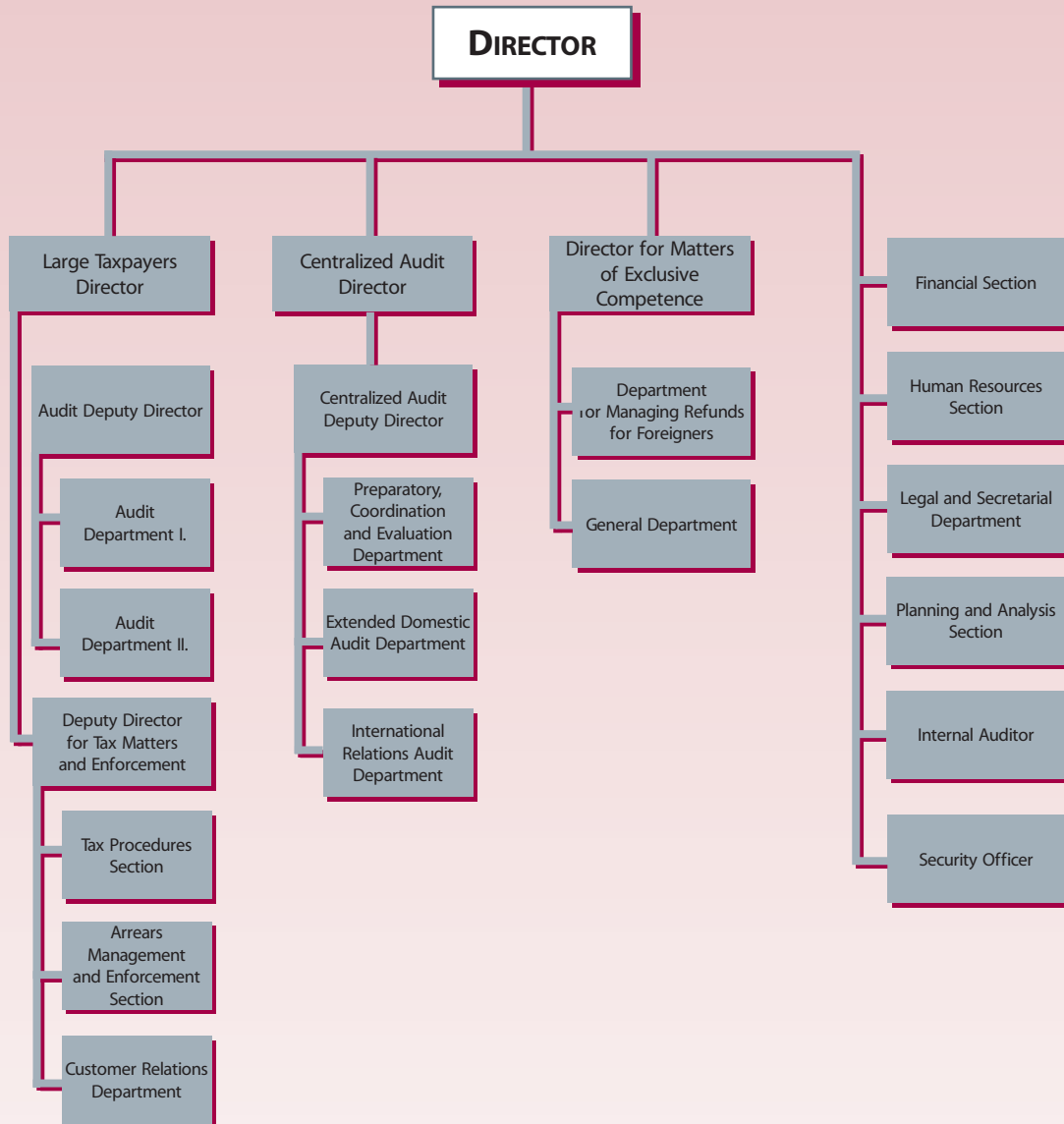
Organizational Structure of the Head Office as of 1st June, 2007



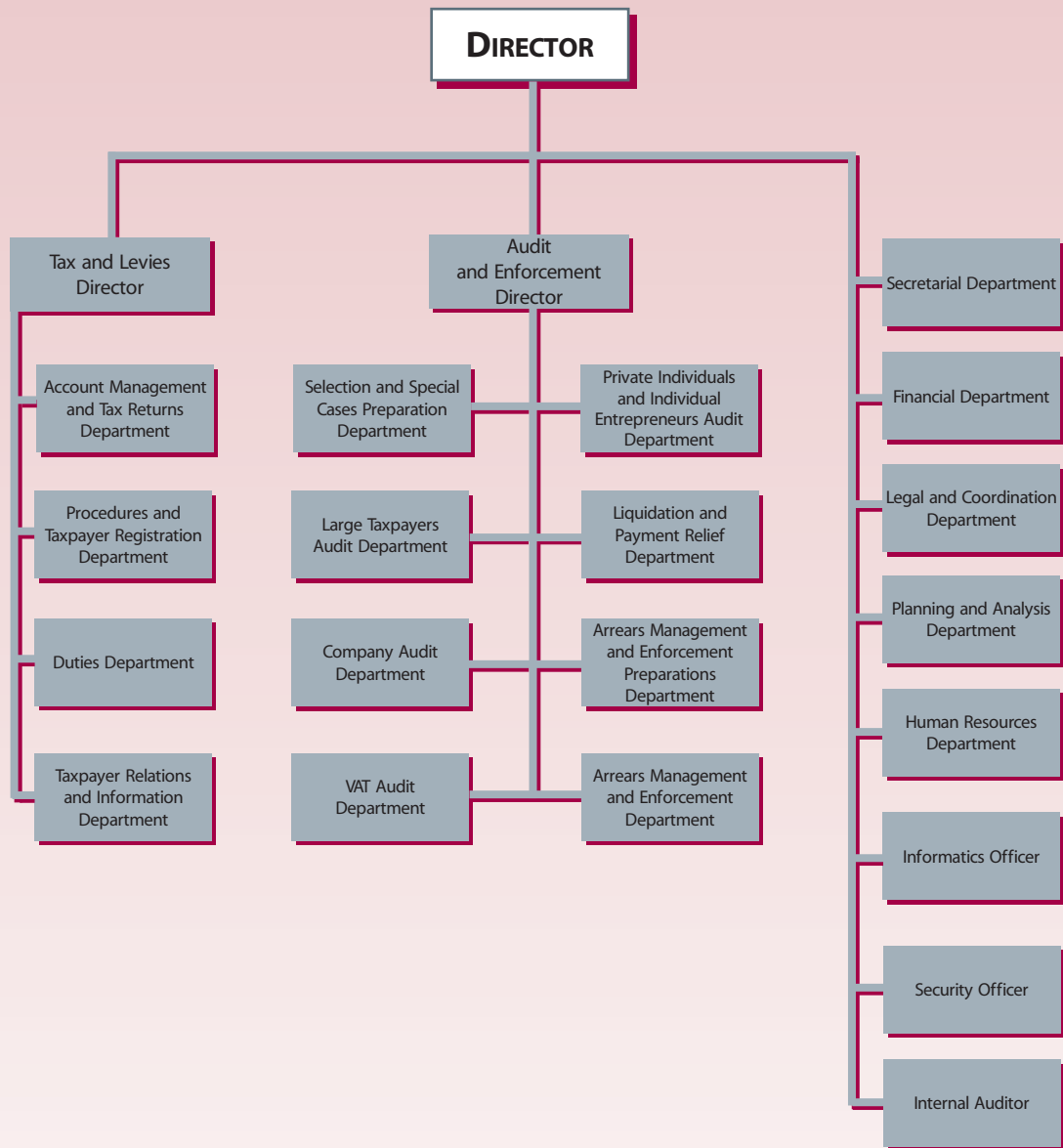
Organisational Structure of the Central Hungarian Regional Directorate, 2007



Organizational Structure of the Large Taxpayers Directorate in 2007



Typical Organizational Structure of a Regional Directorate, 2007



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