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EU Direct Tax Newsalert

CJEU Issues Judgments in Hungarian Turnover Tax Cases

On 3 March 2020, the Court of Justice of the European Union (CJEU) handed down judgment in two related cases regarding the progressive rates applied under the special turnover tax regime in Hungary (C-75/18 and C-323/18).

Background

The preamble of the Hungarian legislation sets forth that special taxes may be imposed on taxpayers whose ability to contribute to the costs of public expenditure exceeds the general level of tax liability. Specifically, the special tax regime lays down that telecommunication operations and retail trading activities are, amongst others, subject to special tax, which has a steeply progressive rate ranging between 0% and 2.5% for retail traders, and between 0% and 6.5% in the case of telecommunication service providers. The tax is levied on the gross turnover arising from the respective activities.

The companies litigating filed for judicial review against the assessments of the Hungarian Tax Authority (HTA) in respect of the special tax.

The companies held the view that the special tax is contrary to the provisions of the Treaty on the Functioning of the European Union (TFEU) with respect to, amongst other matters, State aid and the freedom of establishment, and contrary to the EU's VAT Directive.

It was claimed as regards the freedom of establishment that the companies that fall within the highest band are typically undertakings of foreign tax resident companies. Accordingly, the companies owned by foreign natural or legal persons bear a disproportionate share of the burden of the special tax.

During the lawsuit against the HTA, the Hungarian Court submitted a preliminary ruling request to the CJEU, inquiring whether the special tax regime is in breach of the respective provisions of the TFEU.

The CJEU's Judgments

The CJEU concluded that neither of the litigating companies can rely on the alleged prohibited State aid nature of the special tax regime in order to avoid the payment of such special taxes and the question (whether the tax was unlawful aid) was therefore inadmissible.

In connection with the potentially restrictive nature of the special tax regime, the CJEU highlighted that Member States are generally free to establish progressive tax systems, also on turnover, as it may be a relevant indicator of a taxable person's ability to pay taxes. In this regard, it was established that the respective markets are generally dominated by persons realizing the highest turnover who in this case simply happen to be foreign owned. The fact that they pay a higher amount of tax under a turnover-based progressive tax reflects the economic reality of such markets and does not constitute discrimination against the parties concerned.

Lastly, the CJEU also established that the special tax does not have all the essential characteristics of VAT, and therefore cannot be treated as comparable to VAT, concluding that the tax does not jeopardise the functioning of the VAT system.

Separate CJEU Judgment on penalties for non-registration under the Hungarian turnover tax regime

On the same day, the CJEU handed down a judgment in another case concerning the Hungarian turnover tax regime, this time dealing with penalties for non-registration (C-482/18). Whilst the CJEU found that applying penalties for non-registration was not per se a breach of the TFEU, it concluded that where those penalties applied disproportionately to foreign businesses, it was a restriction on the freedom to provide services.

