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## HUNGARIAN TAX REBATE PROVISION – THE “ONE-PERCENT” RULE<sup>1</sup>

The Act CXVII of 1995 on Personal Income Tax grants private individuals the right to designate, in a statement, the use of a specified portion of their tax paid for the taxable year. For the purpose of the Act CXXVI of 1996, tax paid is the amount which is left after deductions have been taken from the amount due on the consolidated tax base in the individual's tax return or in the employer's account, if made in lieu of a tax return. It is required that the private individual has paid his tax prior to the deadline for submitting tax returns and has not been allowed to defer payment or received a postponement of payment beyond September 30th in the year of the designation statement.

### 1. Extent of the "Specified Amount"

The 1996 version of the Act on the Use of a Specified Portion of Personal Income Tax According to the Designation of the Taxpayer limited the possible designation to one percent of the tax paid. The change in the system for church financing has initiated the 1997 amendment. According to the law in force, private individuals may "offer" one percent of their personal income tax to the civil sector and an additional one percent to churches. Each of the two amounts must be at least HUF 100.

If an individual has designated the above-mentioned specified amount(s), and the transfer has already occurred, the amount cannot be modified later on as a result of either a revision by tax authorities, or a self-revision by the individual. If one of these revisions finds that the tax amount due on the consolidated tax base is lower than the amount on the tax return, the individual must pay the difference between the specified amount and the actual amount which will be designated, only if this amount is at least HUF 1000 and has been transferred to the beneficiary.

### 2. Beneficiaries / Beneficiary Organizations

The Act recognizes two categories of potential beneficiaries. Certain organizations of the civil non-profit sector belong to the first, while churches and advance (earmarked) budgetary purposes belong to the second. The Act determines the requirements of the beneficiary status differently for the two categories. Taxpayers are permitted to designate only one beneficiary for each category for any tax year.

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<sup>1</sup> A summary of the Act CCXVI of 1996 on the use of a specified portion of personal income tax according to the designation of the taxpayer (as amended by the Act CCXIX of 1997).

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## 2.1. Beneficiaries in the first category:

a. Civil society organizations, with the exception of political parties and interest groups for employers and employees, which were established on the basis of the Act II of 1989 on Freedom of Association and foundations fulfilling the following requirements constitute one "component" of this category. They must be registered by the court at least three years prior to the first day of the year in which the designation statement was made and they must effectively pursue a public benefit activity as defined by the Act on Public Benefit Organizations and set forth in their founding documents for at least one year before the first day of the year in which the designation statement was made.

b. Public foundations pursuing public benefit activities also belong to this category.

These organizations have additional criteria with which they must comply. These provisions require that these organizations:

- have their headquarters in Hungary;
- operate for the interests of the domestic population, or of ethnic Hungarians living outside the country;
- declare that they do not pursue direct political activity, their organizations are independent of political parties and do not provide them with financial support (in addition, they must amend their founding documents accordingly; direct political activity includes political party activity and the nomination of candidates for the Parliamentary elections and the elections at county, or Metropolitan level);
- declare that they do not have public debts due and registered by the Customs and Excise Guard, the social security administration, or state tax authorities;
- obtain a certificate, issued within the previous 30 days, from the local government tax authorities confirming that they have no registered public debts due;
- declare that they effectively pursue a public benefit activity as defined by the Act on Public Benefit Organizations, in accordance with their founding documents, uninterruptedly for a period of not less than one year prior to the year of the designation statements, in compliance with all legal provisions relating thereto.

If an organization has registered public debts due, it still can be beneficiary, provided that it complies with all the other requirements. In addition, it must inform the tax authorities to use the amounts transferred by the designation statements to pay its public debts and provide the names of the organizations to whom the debts is owed and the order of paying the debts.

c. Certain national public collections and other cultural institutions (e.g. the Hungarian National Museum, the Hungarian State Opera, the Hungarian

National Gallery, the National Theatre, the National Archives), the Hungarian Academy of Sciences, the Central Fund for Technological Development, the National Scientific Research Fund, the Child and Youth Program, the Higher Education Development Program, the separate state financial fund, theaters, public collections, institutions of public education which had received an individual subsidy from a local government or from the central budget in any of the three years prior to the first day of the year in which the designation statement takes place, the building program of the new National Theatre also belong to the first category.

All the organizations in this category must publish a record detailing the way in which the transferred funds were spent through October 31st of the year following the year of the transfer.

## 2.2. Beneficiaries in the second category:

a. Any church, religious denomination or religious community established under the Act IV of 1990 on Freedom of Conscience, Religion and Churches (hereinafter: churches), belongs to the second category if they were registered by the court before the first day of the year in which the designation statement was. However, an organizational unit or institution of a church cannot be a beneficiary.

b. Any advanced or earmarked purpose defined by Parliament in its chapter in the Act on (State) Budget relating to the year of the designation statement also belongs to this category.

The Office for Taxation and Financial Control provides the beneficiaries in this second category with "so-called" technical numbers. For an advanced budgetary purpose, this is an *ex officio* obligation of the president of the Office. Churches may obtain technical numbers based on their application and the certification of their registration.

## 3. Invalid Designations

The following instances are examples of an invalid designation statement enumerated by the Act:

a. The private individual has designated the one percent of his tax paid to two or more beneficiaries, or the designated one percent is below HUF 100.

b. Both of the two beneficiaries belong either to the first, or to the second category of organizations.

- c. The designation statement contains incorrect or illegible tax (or technical) number, or no number at all, except, if the church or earmarked budgetary purpose can be identified without it.
- d. The designation, the envelope, or their filing/forwarding does not comply with the prescribed rules.
- e. The beneficiary of the first category does not fulfill the requirements as instructed by the Office, or does not fulfill its obligation relating to statements and information.

#### 4. Designation Procedure

An individual taxpayer may make designation statement(s) on a form which can be obtained at the Office for Taxation and Financial Control or on a sheet of paper of the same size and the appropriate information on it. The tax number, or in case of organizations belonging to the second category of beneficiaries, the technical number of the beneficiary must be indicated on the form in every case. The indication of the name of the beneficiary is not mandatory. Taxpayers must put the completed designation form(s) into a postal standard size envelope, seal it and write their name, address and tax identification code on the envelope. They must place the envelope containing the designation statement(s) in their tax return package. In the event that the personal income tax is reported by the employer in stead of an individual tax return, the individual must give the designation statement in the envelope to the employer no later than March 25th of the year following the taxable year. In the latter case, individuals must sign the sealed side of the envelope. The employer gives a receipt about the delivery of the envelope. The employer is not privy to the content of the statement. He must send the intact envelope, together with other information, to the competent tax authority in accordance with the rules governing the employer's tax account in lieu of the individual tax return.

#### 5. Obligations of Tax Authorities

##### 5.1. Data Protection

The information on the envelope and in the designation statement is considered confidential tax information and consequently it is subject to the rules of data protection. Tax authorities may provide private individuals only with information about their own data and designation statements, while beneficiaries may receive information only about the amounts transferred to them. Tax authorities mark the envelope and the designation statement contained therein with an identical identification code. The processing and storing of these documents

take place separately, in such a way, that no person has simultaneous access to both documents. Tax authorities only grant permission to authorized persons, acting in the course of legal proceedings concerning the fulfilment of the designation statements to link these two documents together. The tax authorities must store these documents for five years after the designation statement was filed. If legal proceedings, involving the designation statement, are commenced the documents must be maintained until the proceedings are concluded by a final judgment. After this date, the envelopes and the designation statements must be destroyed.

## 5.2. Transfer

Through September 1st of every year, tax authorities instruct the beneficiary civil society organizations, foundations and public foundations to certify that they have fulfilled the prescribed requirements. Namely, that they have their headquarters in Hungary, they operate in the interests of the domestic population or ethnic Hungarians living abroad, they are not engaged in prohibited political activity, they effectively pursue a public benefit activity and they don't have registered and due public debts, or if they do, the specification of the order of paying these debts. The organizations have 30 days to fulfill their obligations. This deadline is strict, and if neglected, results in the loss of the designated funds. In case the beneficiaries in question certify the fulfillment of requirements unsuccessfully, or fail to fulfill their obligations in this regard, the tax authorities pass a resolution. This resolution can only be altered by the court which has registered the beneficiary organization, if the requirements are actually met, on the basis of the application of the organization, within 15 days through a non-contentious procedure.

The Office for Taxation and Financial Control transfers the funds to the beneficiaries of the first category within 30 days after filing their required statements and certifications, or through October 31st of the year of the designation statement at the latest. If the organization has public debts, the Office deducts these debts from the funds before transfers them to the beneficiaries.

The Office transfers the funds to the beneficiaries of the second category through January 10th of the subsequent year following the designation statement at latest. The reason for the extended time of transfer (in comparison with the first category) is that in 1998 churches will also receive support under the Act on State Budget and the Act on the Financial Conditions of Religious and Public Purpose Activities of Churches in Hungary.

### 5.3. Information

Every year, the President of the Office informs the Office of the Prime Minister and the Ministry of Financial Affairs about the funds transferred to churches or advanced budgetary purposes by designation statements through August 31st. In addition, he reports on the number of designation statements that relate to churches. The Minister of Financial Affairs publishes a report on the second category, detailing the number of designation statements and the amount due to each of the beneficiaries as of September 15th of that year.

### 5.4. Control

The funds transferred to the beneficiaries in the first category are considered budgetary support of such a nature, that tax authorities are entitled to control the appropriate use of such funds for public purpose activities. If the funds are not used for public purposes, tax authorities can adopt a resolution which can require the funds that be repaid.

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