

SMART TAXATION IN THE HUNGARIAN TAX SYSTEM

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ABSTRACT: *Affected by social and economic processes, tax systems seem to be in a transition all over the world. This transition is not only necessary for ensuring state or public revenues but also for handling certain situations, such as the expansion and escalation of digitalization or the one caused by the covid19 pandemic, which emerged and spread last year. The technologies and business models applied in a variety of economic activities continue to develop, and we get to face new technological advancements, methods of tax evasion and social problems, which all need to be addressed and solved. Tax revenues are primarily used by the state to finance public goods and services. Consequently, it is of essential importance how the state plans and designs their structure and channels of collection. Well-designed taxes support economic growth and investments, they encourage and foster job creation, increase economic competitiveness and improve social fairness and justice.*

This study aims to present the fundamental notions and concepts of smart taxes and taxation through the example of the smart solutions recently introduced in Hungarian tax administration. The reason for this is that ensuring state revenues, stabilizing the economy and the situation of the workers and employees and reducing the administrative burden related to taxation are important priorities even for the Hungarian legislators, which is the reason why quite a few smart solutions have been established here in the past couple of years.

KEYWORDS: *taxes; smart taxation; Hungarian tax system; digitalization; smart solutions*

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1. DEFINITION OF THE CONCEPT OF SMART TAXATION

According to quite a number of sources, smart development policies, which are becoming ever more popular these days, must be backed up by smart tax policies. However, a smart tax policy can be less effective and valuable if it is not possible to implement it efficiently, irrespective of whichever part of the world it may be introduced in. (Bird, 2010) To implement the growing role of the government, it might also be necessary to increase tax revenues, specifically, by introducing new taxes. As regards increasing tax revenues, they require an efficient tax administration: the new taxpayers

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need to be identified and involved in the taxation process, while trying to make sure that the costs on the taxpayers' side should be minimalized. (Mankiw, 2009, 14-23.)

In order to facilitate the implementation of all of the above features, for example, within the European Union, the European Commission analyzes the individual national tax policies and provides advice to the member states in order to help disseminate and exchange good practices and successful policies.¹

First of all, let us clarify what we mean by smart tax and smart taxation. We may recognize it as a trend in recent years that the "smart" concept has been introduced and used in a number of segments of the economy, and it may be related now to whatever kinds of solutions, such as smart phones, smart television sets, smart homes, smart cities, smart public service evaluation, etc. However, the question of what makes any solution smart needs to be addressed. The answer is not always simple. For example, a smart home is basically a building where energy consuming, energy producing and energy storing devices and appliances are aligned and harmonized in a smart way.² (European Commission, 2015)

A smart city is the moniker of settlements developed with the help of state-of-the-art technology covering all the fields of sustainability and well-being.³ At the same time, the common feature in these individual concepts is that they are all about the installment or use of a new technology developed in a different sector, with the overall aim of increasing efficiency.

The adaptation and description of the concept is also problematic in relation to taxation because it seems that the English expression *smart taxation* may comprise both the establishment of a *smart tax system* and the smart solutions connected to the taxation process, as well as the types of *smart tax* and even the related *smart tax policy*.⁴ Thus, different countries have different components in it, and the definitions of smart taxation and smart taxes are not clarified in the relevant literature and publications either in Hungary or abroad.⁵ The video clip "Smart Taxation: A Winning Strategy," posted by the European Commission, emphasizes the importance of designing a proper system of taxation as a priority, which supports economic growth and also creates social fairness; furthermore, it promotes the harmonization of member states' tax policies through an exchange of information in order to fight tax evasion and avoidance. (European Commission, 2015)

By surveying the individual concepts, we can highlight the fact that, within smart taxation, there is a smart taxation process as well as there are smart taxes and other smart solutions. I believe that it includes but is not limited to a tax system that generates an economically efficient and effective way of taxing and taxation for the state, for the

¹ *European Commission: Smart Taxation. A Winning Strategy.* 18 September, 2015. <http://ec.europa.eu/avservices/video/player.cfm?ref=I108968> (Date of access: June 21, 2021)

² Directive 2012/27/EU of the European Parliament and of the Council of 25 October 2012 on energy efficiency, amending Directives 2009/125/EC and 2010/30/EU and repealing Directives 2004/8/EC and 2006/32/EC

³ <http://seap.hu/glossary/smart-city/> (Date of access: June 21, 2021)

⁴ <http://smarntaxpolicy.com/> (Date of access: June 21, 2021)

⁵ Blundell, R. (2016), „Nem egykulcsos, hanem okos adórendszer kell”. Index 2016.12.31, https://index.hu/gazdasag/2016/12/31/richard_blundell_interju/ (Date of access: June 21, 2021). Blundell, R. (2016). *Labor Supply and Taxation*. UK, Oxford University Press.

taxpayers and for the tax authorities, which properly responds to global influences by taking advantage of the smart solutions and technological advancements of our age and expanding them to the entire field of tax legislation and regulations. (Pasquale, 2012) This approach interprets the scope of phenomena under scrutiny in the broadest possible fashion. Accordingly, I intend to divide and separate the following dimensions of a smart system of taxation:

- smart solutions in individual tax laws or acts,
- smart solutions in tax administration, offered by the tax authorities
- and smart solutions providing assistance to taxpayers.

I wish to note at the very beginning that smart taxation is not tantamount to tax evasion or the avoidance of the taxation process, which means that decreasing tax liability in such a way cannot qualify for a smart solution in this sense.

Out of the dimensions listed above, I intend to present in this study the smart solutions related to tax administration in Hungary.

2. SMART SOLUTIONS IN TAX ADMINISTRATION

Operating tax administration is indeed costly, both from the aspect of the state and from the aspects of taxpayers. It is exactly for this reason that the general principles call for the minimization of costs and the maximization of the efficiency of collecting tax. (Högye, 2000) Digitalization and the spread of information technology appliances make it possible that the formerly complicated, time-consuming and costly tasks can be now simplified. (Cowell, 2008) Real-time measurement of tax can now be part of reality as the technical requirements necessary for it are readily available. Thus, for example, the occurrence of tax can be traced and monitored in real time in the case of consumption-type taxes. In what follows, I will highlight some examples in the Hungarian practice where, through some smart solution, either the burdens of the taxpayers are reduced or the efficiency of tax collection is increased.

2.1 Introducing online cash registers

Pioneering in the Central-Eastern European region, Hungary introduced online cash registers (OCRs) in 2014, and the number of taxpaying entities required to use these has steadily increased ever since.⁶ The reason for this reform was that, during the course of a tax audit of previously used cash registers, it had turned out that several ways of abuse had been available in the system, which generated billions in tax losses for the state. Consequently, it was necessary to introduce a system that would be able to provide protection from such abuses and also to forward data related to tax affairs into the system operated by the tax authorities. This was made possible through SIM cards installed into the cash registers that were connected to the server of the tax authorities, maintaining a 24/7 connection via wired or mobile internet. In addition to sales, receipts and invoice data, information on opening and closing the register as well as deleted items could be thus fully monitored and traced.⁷ As a result, the degree of tax evasion could be reduced,

⁶ A system like this is operated in, for example, in Bulgaria and in Croatia, too.

⁷ NGM (Ministry for National Economy) Decree 48/2013. (XI. 15.)

while the efficiency of supervision and control could be improved.⁸ (É. Erdős 2020, 2019) By 2020, more than 213 thousand of such electronic fiscal devices (EFDs) had been hooked up to the server of the national tax authority.

Although it cannot be precisely identified how much exactly the introduction of OCRs has contributed to increasing the revenues in the central budget, it is quite evident from the relevant final accounts and reports on the discharge for the implementation of the budget that, following 2013, the revenues collected just from VAT increased by approximately HUF 200 billion annually.⁹

2.2 Online invoicing

In Hungary, as of July 1, 2018, online invoicing (real-time invoice reporting or RTIR) has been introduced in two phases to apply to almost all economic events. In addition to the collection of digital data, the objective of this was to “whiten” the economy and curb tax fraud. Through this measure, not only receipts from cash registers but also invoices issued could become traceable. From January 4, 2021, all domestic invoices have become subject to real-time electronic reporting obligation, covering all customer groups without exception and irrespective of value extent or other restrictions.¹⁰ For this purpose, the Hungarian National Tax Authority (NAV) operates the system called “Online Invoice 3.0.” As a result, a huge amount of data is fast and easily available to the tax authority for the purposes of implementing risk analyses and audits. At the same time, the system also provides an opportunity for taxpaying entities to become exempt from certain reporting obligations.

2.3 Data reporting from vending machines

In 2017, a decree was issued on the data-providing obligations of food and beverage vending machines through an automatic monitoring unit (named AFE), which aimed at eliminating another possible means of tax evasion.¹¹ AFE devices store, handle and communicate electronic data in a separate, independent and closed unit, on the basis of which taxpayers fulfill the obligation of regular data provision to NAV, the Hungarian National Tax Authority, which then can be used for supervision and audits. The entity that operates the vending machine has to sign a contract with a so-called Supervisor Service Provider, who then implements the technical requirements of the process of recording and transferring data to NAV.¹² The task of supervising and service providing was commissioned to Hungarian Postal Services, and about 30 thousand such supervising units or devices have been registered since. As a result, the turnover of these machines can now also be monitored, like how many sandwiches, coffees or cokes are sold, while the consequent taxpaying obligation and the fact of the related compliance or non-compliance can also be tracked, which had not been possible before.

⁸ see the connection of the digitalisation (advantage) and tax evasion In: ERDŐS Éva: A digitális gazdaság adóztatásának trendjei, *Iustum Aequum Salutare* (IAS) XVI. 2020.4. pp. 9.-10., and Éva ERDŐS: The Tendencies of Direct Tax Harmonization – Tackling the Digital Tax Avoidance, *Curentul Juridic* (Juridical Current), XXII.No.1(76), 2019, pp. 108.-120.

⁹ This increase may also have been partially due to the growth of product consumption but the introduction of online cash registers also played a significant part in it.

¹⁰ Act CXXXVII of 2007 on value added tax (VAT)

¹¹ NGM (Ministry for National Economy) Decree 31/2016. (IX. 2.)

¹² § 107 of Act CL of 2017 on taxation

2.4 EKAER - Electronic Trade and Transport Control System

The system marked by the acronym EKAER was introduced on March 1, 2015, in Hungary.¹³ The purpose of EKAER is to help track the actual route of goods related to intra-Community supplies through purchase and sale as well as intra-Community acquisition, and first taxable domestic sale, with the help of an electronic-toll camera (ETC) network, to check compliance with the tax obligations relating to transportation of goods by road.¹⁴ The scope and the magnitude of the information handled by the system is best illustrated by the fact that the number of those registered in the *EKAER* system had exceeded 150 thousand by 2019.

The objective of the system is to strengthen the market positions of compliant economic operators, to make the circulation of goods more transparent, to eliminate fraud related to food products endangering human health and; last but not least, to eliminate tax evaders. By using EKAER, the actual route of the goods can be tracked because transport related data (such as name and quantity of goods, consignee, consignor, registration number of vehicle, etc.) have to be registered in a central electronic system before starting the transport, which then automatically generates an ID number for the identification of the unit of goods.

The legislators also took into account the practical aspects of the economic event and the transportation, so some of these data (product weight, value, and registration number of vehicle) can be modified up until the arrival of the cargo and can be registered in the system on the first working day after the time of arrival at the address of receipt. Providing the license and registration numbers of the vehicle is not a precondition to determining the EKAER number but they have to be registered before starting the transport.¹⁵ However, unreported goods shall be deemed of unconfirmed origin, upon which a default penalty amounting up to 40% of the value of the unreported goods may be imposed on the taxpaying entity by NAV, the amount of which can act as a significant deterrent.

In the case of the four solutions presented above, it is quite obvious that even state-of-the-art technical solutions get involved and installed for the sake of increasing the efficiency of tax administration. I believe that the smart quality of these measures is present in the aspect that the tax authority gets into an online contact with the taxpayers as it were and, due to the exchange of information, tax obligations can be more easily identified, while the system can provide data in real time. These measures are intended to increase efficiency and revenue; however, they also impose a significant one-off amount of cost on the taxpayer during the course of their introduction. The central government has tried to compensate for this latter feature by making support available through tenders.

¹³ NGM (Ministry for National Economy) Decree 5/2015. (II.27.), NGM (Ministry for National Economy) Decree 51/2014. (XI.31.)

¹⁴ Point 14 of § 7 of Act CL of 2017 on Taxation

¹⁵ The link for registering is <https://ekaer.nav.gov.hu/> (Date of access: June 21, 2021)

3. SMART SOLUTIONS OFFERED BY THE TAX AUTHORITY

3.1 PIT draft tax return

In the case of self-assessment tax returns, filing a tax return is an especially important obligation, which also requires expertise. This activity has been assisted by NAV since 2017 in the case of the personal income tax of private individuals through draft tax returns that are prepared automatically, without the need for a specific application. The basis for this is that, through a variety of data provision services, the tax authority has access to all the information related to personal income tax, such as the tax base, the tax advances deducted by the employer and the various benefits, allowances and disposals, on the basis of which the system can easily prepare the draft by automated means for those concerned. The prepared draft tax returns then are made available to the individual taxpayers through the single digital gateway. This is a user-friendly surface, where the draft can be accessed, approved and accepted with a few clicks of the mouse.

If a private individual is not registered and does not have access to the single digital gateway, a request may be submitted either through SMS (IM) or telephone to NAV, asking for the draft to be mailed in a hard copy. If the individual does not approve, supplement or correct the draft tax return by the deadline of filing it, the draft tax return will become a final tax return.¹⁶

By 2021, NAV will essentially prepare a draft tax return for all private individuals, irrespective of what sources of income they have had, and it may be necessary for the individuals to prepare a self-assessment or supplement the draft only in a couple of special cases. Thus, the draft makes the life of private individuals easier, replaces the previous paper-based administration and saves time and money for the taxpayers, which makes it a truly smart solution indeed.

3.2 Draft VAT return

As of 2021, NAV will prepare draft VAT returns¹⁷ for those concerned, which might affect approximately half a million businesses a year in a positive way. This opportunity will be available starting with the monthly VAT return to be filed for July 2021. Hungary will be one of the first countries in the European Union to provide a draft VAT return service to businesses. This can be regarded an extremely huge step in the process of simplifying and reducing tax administration, with the introduction of which businesses and firms can save time and money. In addition, this measure is also expected to improve competitiveness. NAV will offer electronic access to data received from the real-time invoice data service and the data provided by the online cash registers, available in its own registries and databases. The system will show the invoice data by item lines, in addition to which it will provide an aggregation of exemption or obligation and even the data of invoices subject to reverse charge.

3.3 NAV application

Since 2014, it has been possible to download an application of NAV to (Android and iOS) smart phones, the purpose of which is to assist taxpayers in all stages of tax administration. Through this, one can find up-to-date opening hours for customer service at border crossings and the tax authority, as well as the latest tax and customs news. Moreover, if taxpayers consider it necessary, a map navigation system helps them locate

¹⁶ <https://www.nav.gov.hu/nav/szja/szja> (Date of access: June 21, 2021)

¹⁷ § 346 of Act CXXXVII of 2007 on value added tax (VAT)

the destination they wish to reach. In addition, the system also provides them with direct access to making telephone calls and sending e-mail messages. However, it can be used for a lot more specific tax acts, too. For example, in the case of a transfer of assets, the program simply calculates whether and to what extent tax would be payable on real estate property sold. There is also a tax calendar feature, which can be equally practical if the taxpayer wishes to be alerted about tax return deadlines and due dates. It can also facilitate making the right decisions in business life when it is necessary to find out if another taxpayer, for example, a partner company, has any public debt or is in the process of enforcement by simply entering the relevant name or tax number.¹⁸ Taxpayers thus can save time and money, while making the operation and management of their enterprises more practical and rational.

3.4 EFO - Simplified Employment [Egyszerűsített foglalkoztatás] notification mobile app

In a way similar to the one mentioned above but designed specifically to meet a tax liability, the so-called *EFO* application can be helpful, which has been developed in cooperation with a university. The app can be used to support sending electronic notification about simplified temporary employment¹⁹ (for example, in the case of seasonal agricultural work, when the employment lasts for a few days only). In addition to downloading the application, the taxpayer also needs to have a single digital entry gateway registration.

This application is faster and less stationary than the traditional methods; moreover, it also offers individual and multiple notification modes, according to or depending on the IT skills of the taxpayer. For example, the employer can report simultaneously the number of employees that have showed up for work on a specific day. The data submitted and the confirmation of receipt are stored by the application, and the taxpayer is then notified of their acceptance or rejection.²⁰ Thus, this is not only a faster but also a more cost-effective form than the traditional phone calls, since it is no longer necessary to wait too long for a connection at the end of the phone line.²¹

As we have seen, there is a number of solutions now offered for meeting tax obligations, the significance of which is that there is less paper-based administration, which is also important in terms of its environmental impact, not to mention the faster administration, the elimination of the possible mailing costs and the cost of working hours and travel related to personal errands. That is to say, in addition to cost-effectiveness and reducing administrative burdens, the aspect of environmental protection also appears. Yet, in my opinion, this is just the beginning, as the number of such or similar programs and applications can be expected to increase. By building on the already existing systems and using state-of-the-art technology, they can be instrumental in creating truly intelligent taxation systems.

¹⁸ <http://www.euconto.hu/19-erdekes/76-nav-os-applikacio-az-okostelefonokra> (Date of access: June 21, 2021)

¹⁹ Act LXXXV of 2010 on Simplified employment

²⁰ <https://ugyintezes.magyarorszag.hu/szolgaltatasok/efo.html> (Date of access: June 21, 2021)

²¹ <http://www.nisz.hu/efo2015/> (Date of access: June 21, 2021)

4. CONCLUSION

So, is there a smart component in the Hungarian system of taxation? This seems like a legitimate question to ask on the basis of what has been described above. I believe that, even if they are rather rudimentary, the spread of digital systems bring along quite a number of smart solutions even in tax administration. In other words, the basis for a smart tax system lies in the development and introduction of individual smart solutions. Legislation needs to keep abreast of the opportunities offered by technology, including those available in the regulation of taxes and tax administration. This is important in particular because taxation imposes significant costs on the taxpayer, which can have negative economic, social and environmental impacts. It is also the task of the state to minimize the latter. This may comprise supporting smart taxation and building a smart tax system. There may be little information available on how exactly to do this, but it is already certain that there are quite a few options and alternatives that need to be implemented. The influence of digitalization has intensified recently as a result of the pandemic. As a consequence, the existence of smart solutions is currently unquestionable, and we will probably encounter more and more solutions in connection with taxes and procedures similar to the ones presented above, which might prove to produce a substantial increase of convenience and support in the long run for both the state and the taxpayers.²²

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²² The paper was prepared in the framework of Project no. 134499 titled 'Increasing government intervention in market regulation' has been implemented with the support from the National Research, Development and Innovation Fund of Hungary, financed under the K_20 „OTKA” funding scheme.

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