R&D Tax Incentives: Hungary, 2020

Design of R&D tax relief provisions

Hungary provides R&D tax relief through tax allowances (in CIT and innovation contribution), a Development Tax Incentive, and the full exemption of social security (SSC) and vocational training contributions (VTC).

Table 1. Main design features of R&D tax incentives in Hungary, 2020

		R&D related tax base deductibility	SSC and VTC exemption	Development Tax Incentive	R&D tax allowance in innovation contribution**
Tax incentive		Tax allowance	SSC exemption*	Tax credit	Tax allowance
Type of instrument		Volume based	Volume based	Volume based	Volume based
Eligible expenditures†		Current	Labour	Capital, Intangibles	Current
Headline rates (%)		100 (300 R&D collaboration)	100 (SSC rate: 18; 8.25 for PhD students/ doctoral candidates)	0-50 (large), 10-60 (medium-sized), 20-70 (small)***	100 (medium-sized and large firms only)
Refund		No	Redeemable against payroll/ related taxes	No	No
Carry-over (years)		5 (carry-forward)	n.a.	14 (carry-forward)	n.a.
Thresholds	Floor	-	-	HUF 100 million	-
Ceilings	R&D tax relief		SSC liability	80% of the calculated corporate income tax	-
	R&D expenditure		Gross wages per month: HUF 500 000 (HUF 200 000 for PhD students/ doctoral candidates)		-

SSC: Social Security contributions; VTC: Vocational Training Contribution. *In 2019, Hungary introduced three additional R&D tax incentives which are mutually exclusive in their use with the existing SSC exemption and beyond the scope of this note: an SSC credit and KIVA (optional small business tax, replacing SSC and corporate income tax) exemption and credit, both available to small companies. ** Only large and medium sized enterprises pay the innovation contribution of 0.3%. The base of this tax is net sales revenue decreased by the value of the payments to subcontractors and the cost of raw materials. *** The tax credit rate applicable under the Development tax incentive varies by firm size and region of investment. Municipalities in Hungary also provide local business tax (LBT) deductions equivalent to 10% of the direct costs of basic, applied, or experimental research. Hungary also offers income-based tax incentives for outcomes of R&D activities. These are beyond the scope of this note.

Note: For more details, see OECD R&D Tax Incentive Compendium and Eligibility of current and capital expenditure for R&D tax relief

Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Key features:

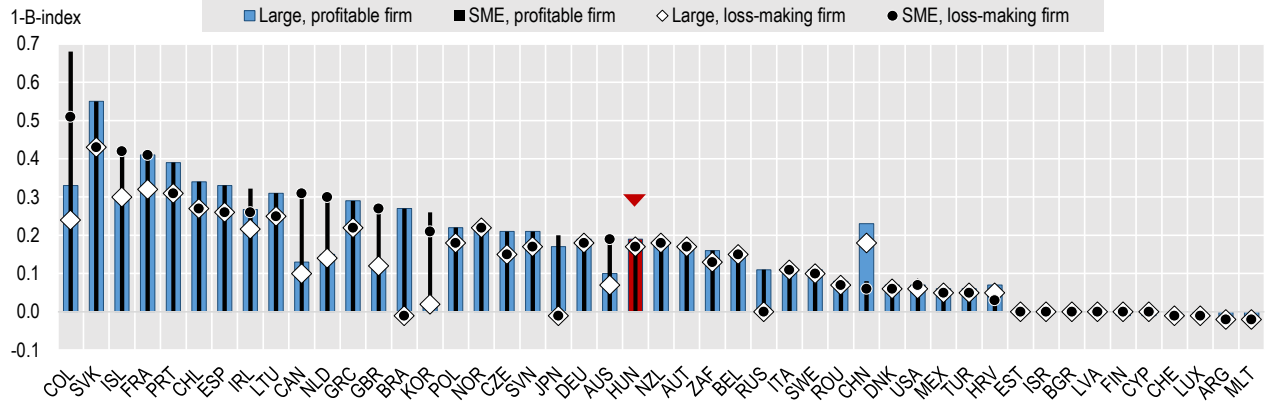
- Under the CIT based R&D tax allowance, a more generous rate applies to collaborative R&D activities (tax benefits capped at HUF 50 million, 100 HUF= 0.283 EUR, Q3 2020). Outstanding credits may be used during the next 5 years to decrease up to 50% of the taxpayer's tax base.
- The Development Tax Incentive provides an investment-based CIT offset and allows for a carry-forward of unused credits up to 14 years. R&D tax benefits are limited to 80% of the firm's CIT liability.
- Ceilings on the amount of eligible R&D expenditure also apply in the case of the SSC exemption.

Generosity of R&D tax support in 2020

Differences in the design of R&D tax incentives drive significant variation in the expected generosity of tax relief per additional unit of R&D investment. In 2020, the marginal tax subsidy rate for profit-making (loss-making) SMEs in **Hungary** is estimated at 0.19 (0.17), slightly smaller than the OECD median of 0.20 (0.18).

Figure 1. Implied tax subsidy rates on R&D expenditures: Hungary, 2020

1-B-Index, by firm size and profit scenario



Note: Implied marginal tax subsidy rates, presented for different firm size and profitability scenarios, are calculated based on headline tax credit/allowance rates (see methodology and country-specific notes), providing an upper bound value of the generosity of R&D tax support, not reflecting the effect of thresholds and ceilings that may limit the amount of qualifying R&D expenditure or value of tax relief.

Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

The tax subsidy rate for large firms is equal to 0.19 (0.17) in the profit (loss)-making scenario, larger than the OECD median of 0.17 (0.15). These estimates, capturing CIT and SSC related incentives, focus on modelling provisions of the R&D related tax base deductibility and the SSC exemption[1].

Recent developments in R&D tax relief provisions

Regular reforms of R&D tax incentives lead to continuous changes in the availability, scope and generosity of R&D tax incentives. Such reforms relate to the launch of new tax incentives, the R&D definition adopted for tax purposes, changes in tax credit and allowance rates, adjustments of thresholds or upper ceilings on qualifying R&D expenditure or tax relief amounts, or changes in the terms and availability of refunds.

In 2020, changes in the availability and scope of R&D tax incentives represented the most frequent type of policy reform (OECD, 2020), along with adjustments to the headline R&D tax credit/allowance rates and adjustments of thresholds or upper ceilings on qualifying R&D expenditure or tax relief amounts. In response to the COVID-19 pandemic, several countries increased the generosity of R&D tax relief or introduced modifications to the administration of R&D tax incentives to facilitate and accelerate R&D funding.

In 2020, **Hungary** did not undertake any **changes** in its R&D tax relief provisions. However, in reaction to the COVID-19 crisis, Hungary lowered the rate for Social Contribution Tax and related tax advances from 17.5% to 15.5% with effect of 1 July 2020, and the rate of the small business tax (KIVA) and related tax advances was reduced from 13% to 12% with effect of 1 January 2020. These tax rate reductions influence the value of social security and KIVA exemptions and credits available to R&D performing firms in Hungary.

Trends in the generosity of R&D tax support

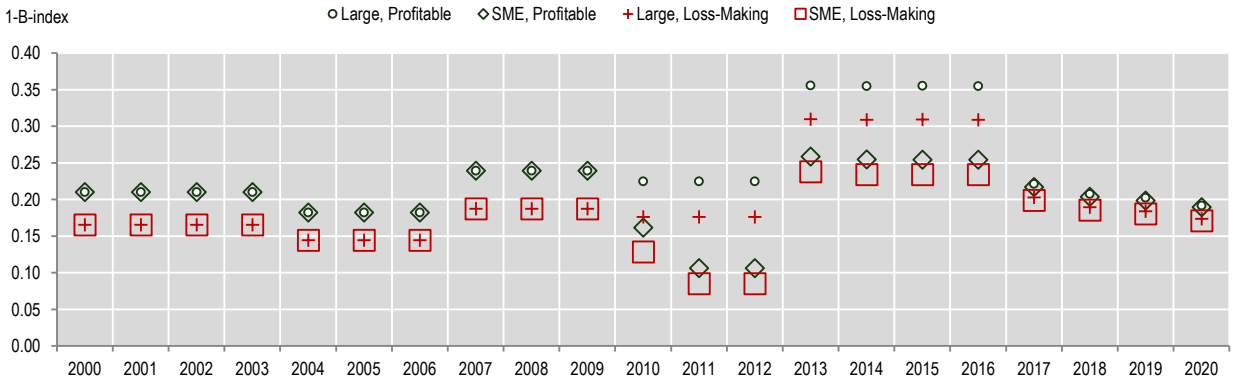
The generosity of R&D tax incentives in **Hungary** has remained overall stable from 2000 to 2020, with some fluctuations arising from changes in corporate income tax rates throughout this period. The value of tax deductions is directly linked to the CIT rate. The lower CIT rates for SMEs vs. large firms are similarly linked to lower implied marginal R&D tax subsidy rates for these firms over the 2010-20 period.

In 2013, **Hungary** introduced a SSC exemption, resulting into a steep increase in the marginal R&D tax subsidy rates. With a reduction and alignment of CIT rates for SMEs and large firms, R&D tax subsidy rates drop in 2017. The stepwise reduction of SSC rates in 2017, 2018, 2019 and 2020 likewise contribute to a drop in implied R&D tax subsidy rates.

If the SSC ceiling is considered in the modelling of R&D tax subsidy rates, the R&D tax subsidy rate for large firms drop from 0.19 (0.17) to 0.15 (0.13) in the profit (loss)-making scenario, and the rates estimated for SMEs drop from 0.19 (0.17) to 0.16 (0.14) in the profit (loss)-making scenario.

Figure 2. Implied tax subsidy rates on R&D expenditures: Hungary, 2000-20

1-B-Index, by firm size and profit scenario



Note: Implied marginal tax subsidy rates, presented for different firm size and profitability scenarios, are calculated based on headline tax credit/allowance rates (see methodology and country-specific notes), providing an upper bound value of the generosity of R&D tax support, not reflecting the effect of thresholds and ceilings that may limit the amount of qualifying R&D expenditure or value of tax relief.

Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

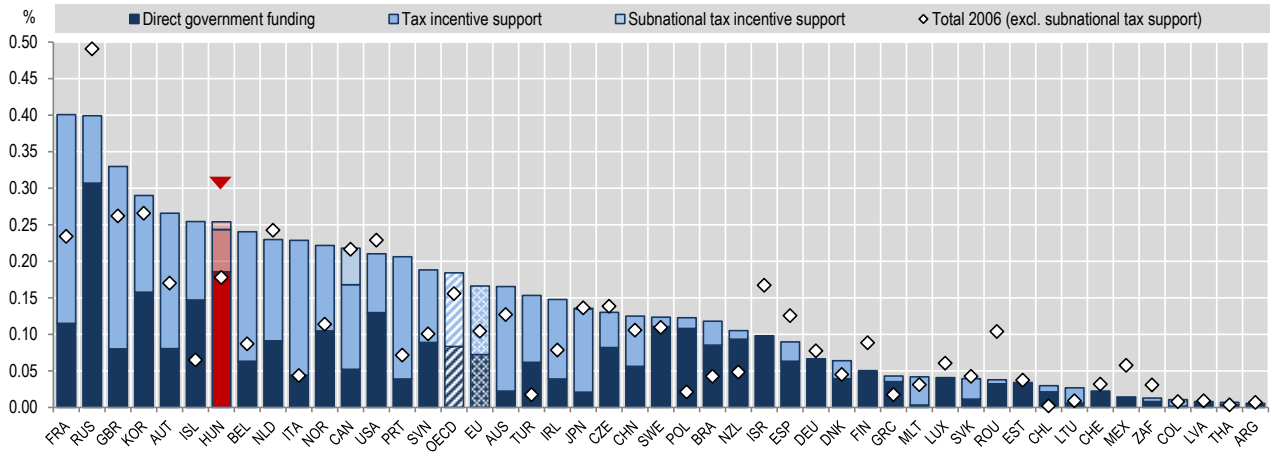
[1] The development tax incentive, used by very few firms, is not modelled.

Policy support for business R&D: the policy mix

In 2018, **Hungary** is positioned above the OECD average in terms of total government support to business R&D as a percentage of GDP, at a rate equivalent to 0.25% of GDP.

Figure 3. Direct government funding of business R&D and tax incentives for R&D, 2018 (nearest year)

As a percentage of GDP



Note: Data on subnational tax support are only available for a group of countries.

Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Key points:

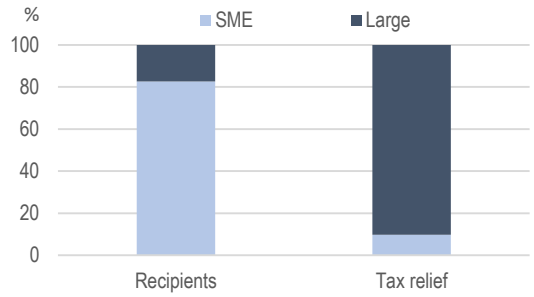
- From 2006 to 2018, total government support for BERD as a percentage of GDP (excl. subnational R&D tax support) increased in **Hungary** by 0.07 percentage point (pp), while the OECD average increased by 0.03 pp.
- During this period, business R&D intensity in **Hungary** increased from 0.47% to 1.14%.
- In 2018, R&D tax incentives accounted for 27% of total government support for BERD in **Hungary**.

Distribution of R&D tax relief recipients and government tax relief for R&D

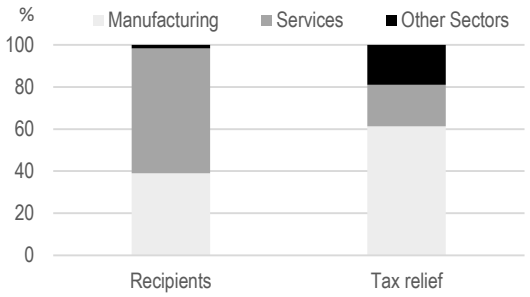
The distribution of R&D tax relief recipients and government tax relief for R&D expenditures (GTARD) provide insights into what types of firms claim and benefit from tax relief.

Figure 4. Number of R&D tax relief recipients and value of government tax relief for R&D, 2018

By firm size*, share in percent



By industry**, share in percent



Note: Figures refer to the R&D tax allowance and the Development tax incentive. *SMEs are defined as firms with less than 250 employees and an annual turnover that does not exceed EUR 50 million or an annual balance sheet that does not exceed EUR 43 million. **Economic activity is classified based on NACE Rev2 (manufacturing: 1011-3320; services 3511-9609; other sectors: remaining classes).

Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

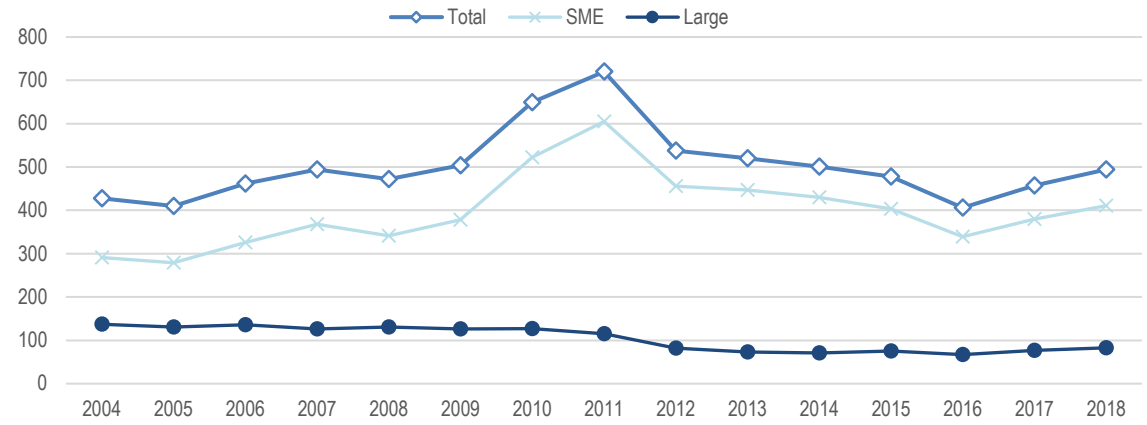
Key points:

- In **Hungary**, SMEs accounted for 83% of R&D tax relief recipients in 2018, while the share of R&D tax support accounted for by SMEs amounted to around 10% in this year. 90% of R&D tax benefits were allocated to large firms, comprising 17% of the population of R&D tax relief recipients in 2018.
- In 2018, firms in services represented around 59% of R&D tax relief recipients in **Hungary**, followed by firms in manufacturing with a share of 39%. The share of R&D tax benefits accounted for by the latter amounted to 61% in that year, while this share amounted to 20% in the case of firms in services.

Trends in the uptake of R&D tax incentives

Over the period 2004-2018, the number of R&D tax relief recipients increased in **Hungary**, reaching close to 500 in 2018. Most of this increase is attributable to SMEs. Throughout these years, the number of SMEs receiving R&D tax support increased from almost 300 to more than 400, while the number of large firms receiving tax support decreased from around 140 to slightly more than 80. Over the 2004-18 period, SMEs accounted for around 65% and 85% of R&D tax relief recipients in **Hungary**.

Figure 5. Number of R&D tax relief recipients, Hungary, 2004-2018



Note: Figures refer to the R&D tax allowance.

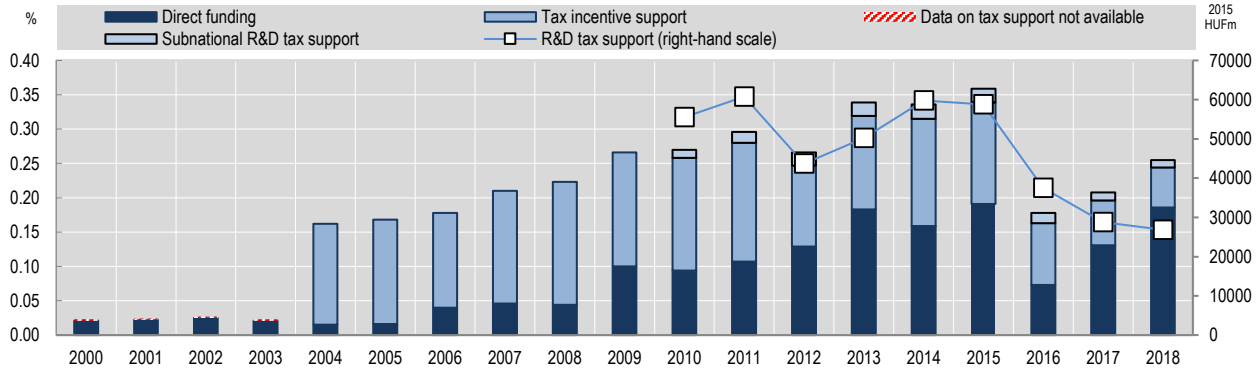
Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Trends in government support for business R&D

Hungary has offered R&D tax incentives since 1996. The importance of this support declined between 2004 and 2018 (when relevant data are available), both in absolute and relative terms.

Figure 6. Direct funding of business R&D and tax incentives for R&D, Hungary, 2000-18

As a percentage of GDP, 2015 prices (right-hand scale)



Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

- The cost of (central and subnational) government tax relief for R&D dropped (in 2015 prices) from HUF 55 513 million in 2010 to HUF 26 846 million in 2018, with a sharp drop in 2012. In this year, the innovation contribution related R&D tax credit expired, and advance assurance provisions for firms applying for R&D tax relief were introduced. The decline from 2016 onwards is attributable to the lower take-up of the R&D tax allowance by business.
- As percentage of GDP, tax support declined from 0.15% in 2004 to 0.07% of GDP in 2018.
- Direct funding of BERD increased over the 2000-18 period, from 0.094% in 2010 to 0.19% of GDP in 2018, with a temporary drop in 2016 (0.073% of GDP).
- The share of R&D tax incentives in total government support dropped significantly over the 2010-18 period, from 65% in 2010 to 27% in 2018. Subnational R&D tax incentives (local business tax deduction) accounted for 16% of total tax support for BERD in 2018, up from 7% in 2010.

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