

Hungary

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I. Summary

A. Types of Organizations

Hungary is a civil law country, and as such it recognizes two traditional civil law forms of nongovernmental, not-for-profit organizations (NPOs) – the association and the foundation.

Hungary recognizes additional organizational forms, including civil groups, nonprofit companies and public chambers. The civil group is an unincorporated legal form which does not have legal personality. The nonprofit company is the non-profit distributing version of a for-profit company form (e.g., general partnership, limited partnership, limited liability company, or shareholder company). [\[1\]](#) Public chambers are rare, as they are formed by an Act of Parliament.

From 1994 to 2006, Hungarian legislation permitted the establishment of a public foundation (a foundation created by the Parliament, the Government, or the municipal council of a local government or a minority government in order to ensure the continuous performance of public duties). However, this form was discontinued on August 24, 2006 [Act LXV/2006 §1 (1)], and new public foundations may not be established after this date.

In addition, Hungarian legislation enables associations, foundations and nonprofit companies to qualify as "Public Benefit Organizations," or PBOs. PBO status is currently regulated in Chapter VII of Act CLXXV/2011. Since public benefit status brings the organization closer to being an IRC section 501(c)(3) equivalent, grantmakers should inquire as to whether an NPO is a PBO. According to the data of the Central Statistical Office from 2012, 53% of NPOs have public benefit status in Hungary. [\[2\]](#)

For practical purposes, then, a potential grantee will likely be organized as:

1. an association,
2. a foundation, or
3. a nonprofit company.

As noted above, these organizations may also have PBO status under Act CLXXV/2011, as amended.

B. Tax Laws

An association or foundation's income from any type of support, allowance, or membership fees is exempt from corporate income tax if it is allocated either to public benefit activities or other mission-related activities of the organization as indicated in its statute or bylaws.

Hungary also exempts from corporate income tax an association or foundation's income derived from public benefit or mission-related economic activities, with unrelated economic income subject to tax under certain circumstances. Such a distinction does not apply to nonprofit companies; thus, their economic activities are generally taxable. However, income of a public benefit nonprofit company is not taxed if it is generated from public benefit activities provided under contract with a local government or other institution, where such activities have a separate line in the annual state budget.

Hungary also subjects certain sales of goods and services to VAT, with a limited list of exempt activities.

The corporate income tax law provides tax benefits for donors. Hungary and the United States have entered into a double taxation treaty.

II. Applicable Laws

- [Act IV/1959](#) on the Civil Code [\[3\]](#)
- Act CLXXV/2011 on the Freedom of Association, Public Benefit Status and the Operation and Support of CSOs
- [Act CXXVI/1996](#) on the Use of Specified Amount of Personal Income Tax in Accordance with the Taxpayer's Instruction

- [Act LXXXI/1996](#) on Corporate Tax and Dividend Tax
- Act LXXXVIII/2005 on Public Interest Volunteer Activities
- [Act CXXVII/2007](#) on Value Added Tax
- Act CXXV/2003 on Equal Treatment and Promotion of Equal Opportunities
- Act IV/2006 on Business Companies
- [Act CLXXXI of 2007](#) on Transparency of Subsidies Provided from Public Funds
- Act CLXXXI/2011 on the Court Registration of CSOs and the Relative Procedural Rules
- Government Decree 350/2011 (XII.30.) on Certain Issues of CSO Financial Management, Fundraising and Public Benefit Status

III. Relevant Legal Forms

A. General Legal Forms

Association

An association is a self-governed, voluntarily established organization which is formed for a purpose defined by its articles of association and which organizes its members' activities in order to achieve its aim. An association has members – called its "registered membership" under local law [Act IV/1959 §61 (1)]. At least ten natural persons, legal persons, and/or organizations without legal personality are required to form an association [Act IV/1959 §61 (3)]. An association cannot be formed for the primary purpose of performing business (entrepreneurial) activities; such activities may only be ancillary, and carried out in order to further the purpose of the organization [Act IV/1959 §61 (2)]. In addition, an association cannot be formed for criminal, military, or unlawful purposes or to undertake a public task which is reserved for state bodies [Act CLXXV/2011 §3 (3)-(5)]. [\[4\]](#)

The special forms of associations are: alliances, political parties and trade unions. Alliances can only have foundation and association members, and may be established and operated by two legal entities.

Foundation

A foundation is an organization established through a statute by any natural or legal person or by a business partnership without legal personality. A foundation must be established for long-term, public interest purposes [Act IV/1959 §74/A (1)]. A foundation must have and disclose sufficient assets to achieve its purposes – or at least to begin operations – and an administering organ (i.e., a board) must be appointed [Act IV/1959 §74/A (1), §74/B (1)(c),(4), 74/C]. After establishing a foundation, founders may not maintain controlling influence over the foundation's assets [Act IV/1959 §74/C (3)].

Civil Group

The civil group is a new, unincorporated legal form which does not have legal personality. Natural persons may set up a civil group without financial contribution to further their common, non-economic purpose and to harmonize their community-oriented activities [Act IV/1959 §578/J]. A civil group may be established by the adoption of a statute and shall not

be registered by any authority. Civil groups do not have any assets and may not undertake economic activity.

Nonprofit Company

A nonprofit company is the non-profit distributing version of an otherwise for-profit company form (e.g., partnership, limited partnership, limited liability company, or shareholder company). In other words, all company forms can operate in a nonprofit manner. A nonprofit company may conduct ancillary business (entrepreneurial) activities, but its profit may not be distributed among its members [Act IV/2006 §4 (3)].

Public Chamber (Public Body)

A public chamber is a self-governed organization with a registered membership, which is established by an act of Parliament. A public chamber fulfills a public task connected to its members or the activity performed by its members [Act IV/1959 §65 (1)]. Legislation may delegate certain public tasks to public chambers (such as certifying professional qualifications) and may prohibit non-members from engaging in those activities [Act IV/1959 §65 (3), (4)]. Where not stated otherwise, the rules for associations apply to public chambers [Act IV/1959 §65 (6)].

B. Public Benefit Status

Public Benefit Organization (PBO)

Associations and foundations may register as PBOs. In addition, other organizations (such as nonprofit companies) may be authorized by law to acquire PBO status [Act CLXXV/2011 §32 (1)]. [5] There are a number of requirements for PBO status. As a precondition of the status, the organization shall undertake public benefit activity. Public benefit activity is defined as an activity that directly or indirectly serves the completion of public (governmental, including at the local government level) tasks, and thereby contributes to the satisfaction of the common needs of society and individuals [Act CLXXV/2011 §2 (20)].

Qualifying organizations shall meet one condition from each of the following two groups of criteria [Act CLXXV/2011, §32§ (4) and (5)]:

- *Having “appropriate resources”*
Based on the previous two completed fiscal years, one of the following conditions must be met:
 1. the average annual income exceeds HUF 1,000,000 (approximately \$4,400), or
 2. the after-tax result of the two years counted together is not negative, or
 3. personnel expenditures – except for the compensation of executive officers – account for 1/4 of the total expenditures.

- *Having “appropriate social support”*
Based on the previous two completed fiscal years, one of the following conditions must be met:
 1. the amount of 1% tax designations (*see Section V.B*) transferred to the organization reaches 2% of the total income, or
 2. the costs and expenditures arising in the interest of the public benefit activity reach 50% of the total costs and expenditures in the average of the two years, or
 3. at least 10 volunteers are permanently (in the average of two years) supporting the

public benefit activity of the organization in accordance with the Act on Public Interest Volunteer Activities [Act LXXXVIII/2005].

Furthermore, the organization's statute shall determine the following [Act CLXXV/2011 §34]:

- a) the public benefit activity or activities that it undertakes; the public tasks that these activities further; and exact references to the legislative provisions that prescribe those public tasks to the state;
- b) the organization does not exclude non-members from benefiting from its services;
- c) business (entrepreneurial) activities may be undertaken only without jeopardizing the implementation of the public benefit and other mission-related activities determined in the statute;
- d) the organization is not entitled to distribute its profit and shall spend it on its public benefit activity;
- e) the organization does not undertake direct political activity, shall be independent from any parties, and shall not provide financial support to them.

By introducing the above criteria, Act CLXXV of 2011 substantially reformed the concept and the preconditions of the public benefit status. Those organizations which gained their public benefit status on the basis of the previous Act (Act CLVI/1997) may remain PBOs until May 31, 2014. Should they seek to retain their status, they must reapply and will need to meet the above criteria with regards to their prior two fiscal years.

IV. Specific Questions Regarding Local Law

A. Inurement

In order to qualify as a PBO, an organization's statute must state that "the organization does not distribute profits, but spends the profits on the public benefit activity defined in its statute" [Act CLXXV/2011 §34 (1)(c)]. However, this requirement is not broad enough to encompass all inurement possibilities. Situations may occur where inurement issues arise, most notably upon dissolution of certain kinds of organizations (*see Section C, infra*).

B. Proprietary Interest

Foundations and nonprofit companies can be formed such that founders retain a proprietary interest in the organizations. This is true even for organizations registered as PBOs because Act CLXXV/2011 does not preclude such interests. The founders of both foundations and nonprofit companies are entitled to reacquire their contributed assets upon dissolution as long as the statutes contain such a provision (*see C.2. and C.3., infra*).

Founders do not retain proprietary interests in associations, but members may have reversionary interests in non-public benefit associations. Public chambers and public foundations, which have state bodies or the Parliament as a founder, permit reversion of assets to the founder.

C. Dissolution

1. Associations

The general assembly has ultimate decision-making power over the dissolution or merger of an association [Act IV/1959 §63 (4)]. If the articles of association or a law do not regulate this, any assets remaining after payments made to creditors are due to the National Cooperation Fund [Act CLXXV/2011 §6, Act IV/1959 §64 (4)]. The law does not impose further limitations on how the founder can regulate the distribution of the assets in the articles of association. Consequently, the association may provide that membership contributions are reacquired by the members both in case of public benefit and non-public benefit associations. Moreover, the law does not prohibit non-public benefit associations from distributing remaining assets to members upon dissolution. In the case of PBOs, the restriction to distribute the remaining assets is also not regulated explicitly; however, it is derived from the spirit of the law and other regulations.

2. Foundations

If the statute does not regulate dissolution, the assets of a foundation upon its dissolution are due to the National Cooperation Fund [Act IV/1959 §74/E (5)]. However, it is not clearly determined by law how the founder can regulate the distribution of the assets within its statute. Based on court practice, the statute may provide that the founder is entitled to reacquire its contributed assets upon dissolution.

3. Nonprofit Company

A nonprofit company can only transform, merge or split into a nonprofit company [Act IV/2006 §4 (4)]. If a nonprofit company terminates without a successor, the debts of the organization shall be settled first. In case of public benefit nonprofit companies the statute may stipulate that the members of the company are entitled to receive the equity capital of the organization at the time of termination but not more than the amount of the nominal capital they contributed. Any remaining assets will be expended by the court of registration for public benefit purposes in conformity with the provisions of the statute. In the absence of such regulations the court of registration will assign the remaining assets of the company to support the National Cooperation Fund [Act IV/2006 §4 (6)].

4. Public Chambers

The rules on dissolution of associations apply to public chambers [Act IV/1959 §65 (6)].

5. Public Benefit Organizations

The law requires that when an organization loses its PBO status it must pay taxes and other debts owed to the state and fulfill its duties under contracts for the performance of public services [Act CLXXV/2011 §50]. If the PBO itself dissolves, the rules governing the specific legal form (as described above) shall be considered.

D. Activities

1. General

NPOs in Hungary are generally permitted to engage in all activities which are not prohibited by an act and correspond with the Basic Act of Hungary (i.e., the Constitution) [Act CLXXV/2011 §3 (4)]. Foundations must serve long-term public interest purposes; associations are not restricted in such a way.

2. Public Benefit Activities

Public benefit activity is defined as an activity that directly or indirectly serves the completion of public tasks and thereby contributes to the satisfaction of the common needs of society and individuals. A public task is defined as a governmental or local governmental duty set forth in a legal regulation which is undertaken by the legally obliged (assigned) provider in the interest of the public, without the aim of profit-making and in conformity with the requirements and conditions set by the law. Such tasks include the provision of public services to citizens and the provision of the necessary infrastructure to implement such services.

3. Economic Activities

NPOs are generally allowed to engage in any economic activities that do not jeopardize the mission-related activity of the organization. Thus, NPOs in Hungary may pursue any sort of income-generating activity (investment, trade, etc.) to help finance their operations. However, associations and foundations must not be established for primarily business (entrepreneurial) activity [Act CLXXV/2011 §17]. An NPO is deemed an organization established for primarily business (entrepreneurial) activity if its income from such activity is equal or higher than 60% of the total income of the NPO [Act CLXXV/2011 §2 point 7]. In addition, none of the not-for-profit legal forms may distribute profits to any person; all profits must be used to carry out the purposes of the organization. This is required by law in the case of PBOs [Act CLXXV/2011 §34 (1)(c)], and by judicial practice in the case of other NPOs. A nonprofit company may conduct ancillary business (entrepreneurial) activities, but its profits may not be distributed among its members [Act IV/2006 §4 (3)].

For PBOs, an exhaustive list of preferred fields of activity no longer exists, but §2 point 20 of Act CLXXV/2011 gives a definition of public benefit activity (*see supra D(2)*). Business (entrepreneurial) activities may be undertaken by the NPO only without jeopardizing the implementation of the public benefit and other mission-related activities determined in the statute [Act CLXXV/2011 §34 (1) (b)].

Under the corporate tax law, Hungary generally taxes an organization's "entrepreneurial activities," defined as "economic activities aimed at or resulting in the acquisition of income or property" [Act LXXXI/1996 §1 (1)]. In theory, the income of associations and foundations from economic activities is not taxed, and not deemed "entrepreneurial," if the activities are related to the organization's public benefit or mission-related activities. The consideration of or revenues from the sale of intangible assets, tangible assets, or inventories serving solely the

public benefit or mission-related activities shall also not be taxed. Furthermore, there is a tax exempt threshold on income arising from business activity.

Such a distinction does not apply to nonprofit companies; thus, their economic activities are generally taxable. However, income of a public benefit nonprofit company is not taxed if it is generated from public benefit activities provided under contract with a local government or other institution which have a separate line in the annual state budget for continuous service provision, including the fee and the conditions of amending the fee. In addition, the support and allowance provided to such activity are also not taxed [Act LXXXI/1996 §1 (1) Annex 6. E].

E. Political Activities

Act IV/1959, as amended, places no restrictions on legislative or political activities of NPOs. Foundations and associations may nominate and support candidates and legislation freely.

However, if the organization is registered as a PBO under Chapter VII of Act CLXXV/2011, its statute must state that it does not pursue direct political activity, it is independent of political parties, and it does not provide financial support to political parties [Act CLXXI/2011 §34 (1)(d)]. [\[6\]](#) The prohibition does not apply to the nomination of candidates for local government councils at the municipal level (including districts of the capital). Similarly, although PBOs cannot support political parties, political parties may support PBOs.

F. Discrimination

Act CXXV/2003 bars racial discrimination by any school that uses a state-accredited curriculum or that receives direct or indirect financial support from the government, which accounts for the vast majority of Hungarian schools.

G. Control of Organization

In general, no restriction exists on the control of not-for-profit organizations by other organizations or persons. It is possible that a Hungarian NPO may be controlled by a for-profit entity or by an American grantor charity (which requires that the charity specifically so provide in the affidavit).

V. Tax Laws

A. Tax Exemptions

Hungary generally taxes an organization's "entrepreneurial activities," defined as "economic activities aimed at or resulting in the acquisition of income or property" [Act LXXXI/1996 §1 (1)].

All income related to the public benefit or mission-related activities of associations and foundations are deemed non-entrepreneurial and therefore exempt from corporate tax. This exemption includes any support, allowance or membership fee received in connection with such activity. The consideration of or revenues from the sale of intangible assets, tangible assets or inventories serving solely the public benefit or mission-related activities shall also not be taxed. Only income from unrelated economic activities is subject to taxation as entrepreneurial [Act LXXXI/1996 Schedule No. 6].

B. Tax Deductions, Credits, and Rebates for Charitable Contributions

Tax deductions and credits

Individuals are not entitled to any tax benefits for charitable donations. For companies, donations to Hungarian NPOs with PBO status are tax-deductible under limited conditions. Companies may also enjoy tax benefits for donations to the National Cultural Fund and the National Relief Fund. To claim the deduction, the company has to be in possession of a certificate for tax purposes provided by the beneficiary organization [Act LXXXI/1996 §7 (1)(z), §7 (7)].

The pre-tax profit may be reduced:

1. by 20% of the donation if the donation supports the public benefit activity of a public benefit organization or 50% if the donation supports the Hungarian Relief Fund or National Cultural Fund; and
2. by an additional 20% of the donation if provided under a long-term donation contract (i.e., a monetary contribution provided on the basis of an agreement between a public benefit organization and its donor wherein the donor undertakes to provide the donation in the subject year and in at least three forthcoming years at least once each year, in the same or larger amount, without any consideration)

up to the amount of the pre-tax profit on the aggregate.

Rebate of individual taxes to charity

Individuals living in Hungary who pay income tax are also entitled to designate 1% of their income taxes to specific NPOs that carry on public benefit activities and some other institutions [Act No. CXXVI/1996]. [\[7\]](#)

C. Value Added Tax

Generally, all organizations engaged in economic activities are subject to the VAT. The standard rate is 27%, with some goods and services taxed at 18% and 5%.

There is a list of public interest activities which are exempt from VAT if they are provided by public service providers. The following organizations may be public service providers:

budgetary organs, associations, federations of associations, civil groups, public bodies, national professional sports federations, foundations, public foundations, churches, nonprofit companies, and other organizations which have obtained PBO status or perform their activities within the framework of a social security or other obligatory insurance relationship for the benefit of insured or other beneficiaries.

Furthermore, organizations may also be considered as public service providers if the following conditions are met: 1) they do not systematically aim to make a profit and they use the profit to maintain and extend their public interest activities; 2) their executive officers (including the board) are volunteers; and 3) they charge prices for the supply of goods or services in compliance with the Act on Price Control Regulations or the prices are lower than those charged on the market for similar goods or services. The exempt services include, among others: health, social services, public education, child and youth protection, day care, psychological assistance, folk art, and sports-related services [Act CXXVII/2007 §85 (1) and (4)].

The sale of assets is also exempt from VAT if the asset was previously used for the above activities [Act CXXVII/2007 §87].

Moreover, the donation supporting the public benefit activity of the public benefit organization is also exempt from VAT so far as the donor disposes of the certificate of the beneficiary [Act CXXVII/2007 §259 9/A].

Finally, the sale of assets beyond the EU for humanitarian, educational and charitable causes for an organization undertaking public benefit activity is also exempt from paying VAT [Act CXXVII/2007 §100].

D. Double Tax Treaty

Hungary has entered into double tax treaties with a number of countries, including the United States. When such a treaty is in existence, dividends, interest, and royalties arising in one country and paid in another are subject to tax only in the country where paid.

VI. Knowledgeable Contact

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Footnotes

[1] The nonprofit company replaces the former category of public benefit companies, which ceased to exist as of July 1, 2009.

[2] PBOs acquired their status based on the previous law on PBOs, Act CLVI/1997, which was repealed in 2011. They will have to re-apply for this status before May 2014 and qualify based on new criteria in order to retain this status. (*See Section III.B*)

[3] The new Civil Code (Act V of 2013 on the Civil Code) was adopted in 2013 and will come into effect on March 15, 2014.

[4] The exact formulation of the provision is: An association may not undertake activities that are aimed at realizing a public task that is assigned by law in the exclusive competence of a state body (i.e. the state body cannot delegate or outsource this task) [Act CLXXV/2011 §3 (5)].

[5] Pertinent regulations were set forth in a separate Act [Act CLVI/1997], which was repealed by the adoption of the new “CSO Law” [Act CLXXV/2011], and are now found in Chapter VII of the CSO Law.

[6] Under Act CLXXI/2011 §2, point 22, "direct political activity" includes "political activity undertaken for the benefit of a political party, nomination of candidates during the Parliamentary election or to the county or metropolitan local government council (including the capital Budapest), nomination of a member of the European Parliament, nomination to the council of a city with county rights, and nomination of a mayor.”

[7] For a discussion of the requirements of this legislation, see ECNL’s paper "[About Miracles and Misperceptions - Lessons from the "percentage mechanism" in Hungary.](#)"