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Conference Proceedings

**Nemzetközi tudományos konferencia
a Magyar Tudomány Ünnepe alkalmából**

International Scientific Conference
on the Occasion of the Hungarian Science Festival

Sopron, 2024. november 7.

7 November 2024, Sopron

**FENNTARTHATÓSÁGI ÁTMENET – INNOVÁCIÓS
ÖKOSZISZTÉMÁK – DIGITÁLIS MEGOLDÁSOK**

SUSTAINABILITY TRANSITIONS – INNOVATION ECOSYSTEMS – DIGITAL SOLUTIONS

Szerkesztők / Editors:

RESPERGER Richárd, SZÉLES Zsuzsanna, TÓTH Balázs István

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Financial and Accounting Issues in Sustainable Economic Decisions – Direct Tax Law Comparison Between Hungary and Germany

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Abstract:

Taxes are used to finance the state budget. Subjects in the legal framework obliged to pay taxes and are entitled to a proportionate, fair and coherent legal system. The tax liability relationship are subject to various problems, such as the scope of the law, interpretation of content, bureaucracy e.t.c. When taxpayers act across borders, these areas of tension multiply. The first section of this document outlines the challenges facing taxpayers in Hungary and Germany. Based on this, the income and corporate tax systems are compared. The comparison of the tax systems makes it clear that the tax systems are not coordinated with one another, meaning that taxpayers who operate internationally must carefully analyze each national legal system and possible double taxation risks. The article also addresses the OECD's double taxation agreements (DTAs), which attempt to mitigate the double taxation situation. However, DTAs assign the right to tax to only one state and do not resolve the inconsistencies of the bilateral systems. This leaves double taxation risks that influence sustainable, financial and economic decisions. The paper ultimately proposes a different approach to a solution that would need to be further scientifically researched: Instead of adding additional standards to the existing, problematic tax systems, an understanding, respectful and communicative approach between the tax jurisdictions could be a better solution. This could create trust in the rule of law and contribute to more sustainable decisions.

Keywords: International economic order, Efficiency Taxation, personal income tax, OECD Convention for the avoidance of double taxation, International Fiscal Issues

JEL Codes: F02, H21, H24, H87, K34

1. Introduction

1.1. Topic introduction and relevance

A business requires planning security for both national and international transactions to ensure efficient and successful management of its business processes (Burger & Kälberer, 2020). A legal system should not act as an obstructive element but instead facilitate the efficient and seamless execution of business processes, intervening only in cases of market failure (Baumann, 2007). This approach enhances overall economic welfare and facilitates the exchange of goods and services.

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However, economic reality is often different: In particular, unsystematic tax norms in one's own country of residence, differences in the legal and tax framework regarding the classification of a tax subject in different countries and different government requirements hinder such transactions (Van Lishaut, 2024).

This conference paper examines the specific challenges faced by internationally operating taxpayers, including both (regular) natural persons (n.p.) and legal entities (l.p.), such as corporations in Germany (D) and Hungary (HU). The analysis focuses on selected differences between the tax systems of these two countries and how these disparities create obstacles in international business transactions.

Through the use of international agreements – specifically, double taxation agreements (DTA), the global community seeks to eliminate tax-related barriers in cross-border processes. This paper also addresses the extent to which such agreements succeed and highlights their limitations.

Finally, the paper concludes by summarizing the key findings and insights gained.

1.2. Research question

The central research questions of this study are:

1. What are the differences between the Hungarian and German tax systems?
2. What tax-financial and accounting challenges do international taxpayers face when operating in these countries?

This article aims to identify the challenges in income taxation in both countries (chapter 2), show why people act cross-border (chapter 3), and what they have to know if they get into the tax systems of Hungary and Germany (chapters 4 to 6). The analysis highlights the differences between the two tax systems. With any inconsistencies in the tax systems, the risk of (international) double taxation rises.

DTAs try to avoid double taxation but can't change with the basic inconsistencies of the tax systems (chapter 7). For well-functioning financial sustainability, proposing new potential solutions is necessary (chapter 8).

1.3. Methodology

To address the research question, a comparative legal approach was employed (Hepting, 2018). This method seeks to evaluate the functioning of different (tax) legal systems, identify areas for improvement, and, if applicable, derive actionable recommendations. Both systematic and structural differences between the two systems were examined in this context.

In addition, content analysis (Mayring & Fenzl, 2019) was applied to systematically and clearly present the various types of taxes.

2. A look at domestic tax law and its challenges

Before addressing international tax systems, taxpayers must understand the domestic tax systems and their influence on economic decision-making.

2.1. Challenges of German tax law

To gain an initial understanding of the challenges posed by the German tax system, general media reports can serve as useful indicators. Selected headlines include: Tax competition is weakening, but bureaucracy is increasing ["Steuerwettbewerb schwächt sich ab, aber die Bürokratie nimmt zu"] (Stiftung Familienunternehmen, 2024), Germany's paralyzing bureaucracy ["Deutschlands lähmende Bürokratie"] (Beeger et al., 2023), or German tax law is the most complicated in the world ["Das deutsche Steuerrecht ist das komplizierteste der Welt"]

(Schmidt, 2015). The tax declaration system is similarly described as overly extensive, prompting statements like Merz [a German politician of the Christlich Demokratischen Union (CDU)] calls for corporate tax on a beer mat (Spiegel, 2020) to illustrate the demand for simplification.

These sources highlight widespread perceptions of high bureaucratic burdens and the overall complexity of the German tax system. Scholars have also identified and attempted to measure this complexity, for instance, by evaluating the volume of tax legislation, accompanying guidelines, notices, and technical literature. They also examine the workload for taxpayers, tax consultants, and authorities during assessment, appeals, and litigation processes (Borne-mann et al., 2019; Wölfl & Wiedenmann, 2023), as well as the uncertainties in the interpretation of abstract legal terms (Fischer, 1998).

As a result, there is little public interest in engaging deeply with tax policy (Statista, 2024), despite its significant impact on economic and sustainable financial decisions.

2.2. Challenges of the Hungarian tax system

Similar perceptions are reflected in Hungarian news: an imbalance in tax policy is accompanied by a high level of bureaucracy (Irány, 2024). For Hungarian taxpayers, preparing tax declarations also poses significant challenges. In response, the National Tax and Customs Administration of Hungary ["Nemzeti Adó- és Vámhivatal" (NAV)] has made efforts to provide citizens with tax-related information in a simple and accessible manner (NAV, 2021).

At the same time, tax professionals repeatedly highlight various systemic issues within the Hungarian tax framework (Ferencz, 2024). These challenges underline the need for reforms to alleviate bureaucratic burdens and improve the clarity and functionality of the system.

2.3. Comparative analysis of domestic tax systems

Both the D and HU tax systems exhibit both homogeneous and heterogeneous national challenges. Common to both systems are inconsistencies and high administrative burdens. Taxpayers must thoroughly acquaint themselves with these discrepancies, as well as the formal and substantive tax regulations in each country, before pursuing international investments. This includes, but is not limited to:

Institutions: Knowledge of the respective institutions in each country is essential. In D, tax declarations must be made to the local tax office or the German Federal Central Tax Office [Bundeszentralamt für Steuern (BZSt)]. In Hungary, the NAV is the most important tax authority to which tax data must be reported. Submitting the data to the wrong place will result in disadvantages for the taxpayers (e.g. a late payment surcharge (§ 152 Abgabenordnung (AO) [The Fiscal Code of Germany]) or legal deadlines may expire (§ 355 AO)).

Tax obligations and types: Taxpayers must understand their specific obligations (§ 38 AO) under each system. For example (e.g.), HU has unique levies such as the retail tax (Felkai, 2022) or the simplified small business tax ["kisvállalati adó" (KIVA)] (Juhász, 2022), which are unfamiliar to German.

Filing and reporting requirements: The differences in declaration and accounting methods must be noted, like the German § 140-153, § 164, § 167 AO, while Hungarian taxpayers follow provisions in the Act CL of 2017 on the Rules of Taxation and must meet distinct accounting requirements (Felkai, 2022).

These variations necessitate comprehensive preparation and understanding to ensure compliance and efficiency in cross-border economic activities.

3. Tax rates in the European Union, with special focus on Hungary and Germany

When a taxpayer accepts the complexities of international tax systems and decides to invest in another jurisdiction, the focus often shifts to the applicable tax rates. The European Union (EU) comprises 27 member states, each determining its own entry-level and top income tax rates as well as its corporate tax rates (*Figure 1*).

Income tax and corporate tax rates in Europe

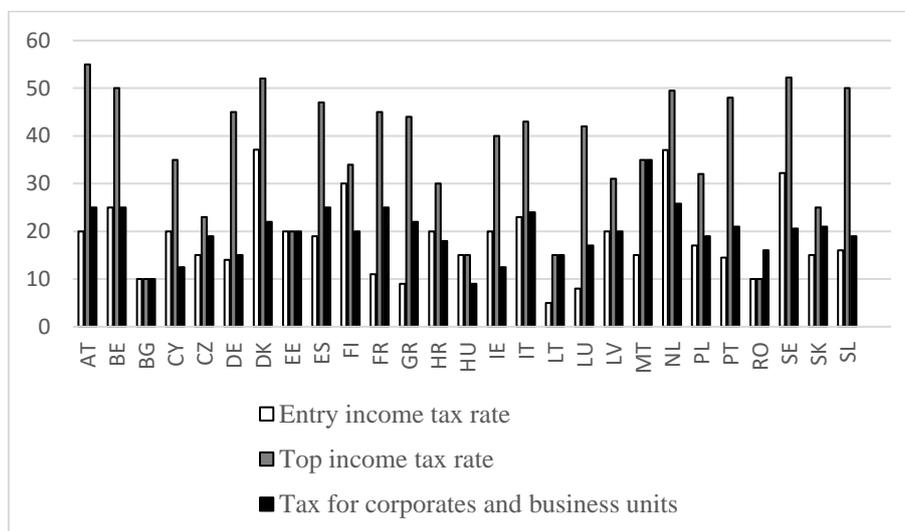


Figure 1: EU tax burden comparison

Source: Own presentation, data source Sprengel (2023)

HU stands out with particularly low income tax and corporate tax rates, while D ranks among the EU countries with higher tax rates.

From the perspective of the D-tax system, high tax rates are justified and constitutionally compliant, as the system adheres to the principle of ability to pay, which is a manifestation of the equality principle (art. 3 I Basic Law [Grundgesetz (GG)]). Accordingly, taxpayers with differing income levels are taxed differently, while those with comparable income are taxed equally (König, 2024), in German also referred to as the "objektiven Nettoprinzip" (Klein & Orlopp, 2024). This principle is similarly recognized at the EU level under article 20 of the Charter of Fundamental Rights of the EU (Kokott, 2018).

Despite this justification, the attractiveness of low-tax jurisdictions cannot be denied, as tax payments are a significant cost factor for businesses (Birkemeyer et al., 2019). Relocating to a low-tax country often results in the reallocation of production resources (e.g., financial or human capital) and increased tax revenues for the host country, placing tax jurisdictions in direct competition with one another (Haase, 2017). In recent years, this "race to the bottom" has intensified (Grotherr, 2023).

The existing international double taxation agreements (DTA) often fail to allocate tax bases effectively. This failure stems from various issues, such as being designed in eras of limited economic mobility and less easily transferable (digital) intangible assets, as well as differing linguistic and cultural interpretations (Haase, 2023). To address these challenges, the Organisation for Economic Cooperation and Development (OECD) has been working for years to establish new global tax norms. An example is the 15 Base Erosion and Profit Shifting (BEPS) actions proposed by the Organisation for Economic Co-operation and Development (OECD, 2024).

However, tax savings are usually just one of several reasons for foreign investments (Vig, 2003; Lieb & Yalcin, 2015; Dörr et al., 2024; Stahlschmidt, 2024;). Other factors, such as lower

wage levels, reduced production costs, or additional economic considerations (Berlemann & Tilgner, 2006), also drive cross-border activities (Magyarország Kormánya, 2021; Borstell & Riesselmann, 2024). HU offers several favorable location factors (Grieß, 2024), making it more than just a low-tax country or a tax haven within the EU (Federal Ministry of Finance [Bundesministerium der Finanzen (BMF)]) (BMF, 2024; European Council, 2024).

4. Comparative legal analysis of income tax systems in Germany and Hungary for persons

4.1. German income tax – “Einkommensteuer (ESt)”

The first legal provisions of the German income tax [Einkommensteuergesetz (EStG)] date back to 1871 (Spilker & Stöber, 2024; Rauch, 2024), which initially established the concept of personal tax liability. The EStG applies to all n.p. (§ 1 I Bürgerliches Gesetzbuch (BGB) [Civil Code]), who have their domicile (§ 8 AO) or habitual residence (§ 9 AO) in Germany.

All income of the n.p. individuals (so-called “Welteinkommen“ (Bott et al., 2024) is subject to the EStG. The taxable income is determined by deducting expenses from revenues for each category of income (§ 2 I, § 2 II EStG). A distinction is made between two primary income determination methods:

- Business income types (German: “Gewinneinkunftsart“): Business revenues (similar § 8 I EStG) are offset against related business expenses (§ 4 IV EStG). This calculation is conducted through either cash accounting (§ 4 III EStG) or accrual accounting (§ 1, 2, 238 Handelsgesetzbuch (HGB) [Commercial Code]; § 140, § 141 AO; § 4 I, § 5 I EStG) (Hey, 2024).
- Non-business income types (German: “Überschusseinkunftsart“): Income is calculated on a cash basis by deducting associated expenses (§ 8 I EStG) from revenues, using the principle of inflow and outflow (§ 9 I ff. EStG) (Seiler, 2024, p. 1192).

This dual approach is crucial because:

- Depending on the type of income, capital gains from asset disposal (rather than just ongoing income generation) may be included (e.g., § 22, § 23 EStG; Boelsen, 2025).
 - Losses arising from personal hobbies or preferences (e.g., loss from a farm in Paraguay) (Bundesfinanzhof (BFH) [Federal Fiscal Court], 1999), cannot offset positive income to reduce an individual’s tax liability (German term “Liebhaberei”) (Nacke, 2024).

This distinction supports the implementation of the “objektiven Nettoprinzip” (Schaumburg, 2024) and is referred to as the “Dualismus der Einkünfte” (Grashoff & Mach, 2023, p. 66.). The resulting surplus (for non-business income) or profit (for profit income) is taxed. In D, seven categories of income are recognized and subject to tax:

- Income from agriculture, forestry, § 13 EStG (profit-income),
- Income from trade or business, § 15 EStG (profit-income),
- Income from self-employment, § 18 EStG (profit-income),
- Income from employment, § 19 EStG (non-business income),
- Income from capital investments, § 20 EStG (non-business income),
- Income from rental and leasing, § 21 EStG (non-business income),
- Other income, § 22, 23 EStG (non-business income).

The total of all profits or surpluses (or losses) constitutes the total income (§ 2 III EStG). From this total, additional deductions can be made:

- *Basic tax-free allowance*: In order to art. 6 I GG, the fundamental rights protection for marriage, family and children, the legislator provides a tax-free allowance of approximately €11,604 per individual (§ 32a I EStG; Mandler, 2024). So a person’s minimum subsistence level is not taxed. Special provisions exist for married couples (§ 1353, § 1567 BGB, § 26,

§ 26b, § 32a V EStG; Münch, 2020) or for children (§ 31, 32 EStG; Bundesverfassungsgericht (BVerfG) [Federal Constitutional Court] 1998; Loschelder, 2024) (*child allowance*).

- *Extraordinary expenses*: Private expenses (e.g., for personal clothing) are generally non-deductible (§ 12 No. 1 EStG). However, unavoidable and extraordinary expenses that affect only certain n.p. (e.g., due to illness or increased care needs) can reduce taxable income (§ 33 EStG; Unger, 2024; § 33b EStG; R 33.1–33.4 ESt directive). Such deductions are permissible as they reduce the taxpayer's ability to pay and align with social welfare principles.

After considering these and other deductions (§ 2 IV, V EStG), the taxable income referred to as the "Gesamtsumme der Einkünfte" (§ 2 V EStG) is determined. This income is multiplied by a progressive tax rate, resulting in the income tax liability.

The higher the taxable income, the higher the applicable tax rate (BVerfG, 2006; Loschelder, 2024). This progressive tariff ensures adherence to the principle of ability to pay (see Section 3).

Certain types of income are exempt from taxation, often for social reasons, such as publicly funded scholarships (§ 3c No. 44 EStG) or payment from health and care insurance (§ 3c No. 1a EStG) (Nußbaum & Jungblut, 2024).

Income tax is assessed on an annual basis (§ 25 I EStG, § 37 I, § 38 AO). N.p. are required to file their tax returns using an official form (§ 25 IV EStG) with the competent local tax authority (§ 16 ff AO). The tax authority then determines the tax liability (§ 155 I AO) and issues a formal tax assessment notice (§ 157, § 118 AO), specifying the amount of tax payable. Tax declarations must generally be submitted by the end of July of the year following the tax year (§ 149 I, II AO).

4.2. Hungarian personal income tax – “Személyi jövedelemadó (Szja)”

The foundational principles of the Hungarian personal income tax ["Személyi jövedelemadó" (SZJA)] were established at the Diet of Ónod in 1707, aiming to create equal tax burdens for all Hungarian n.p. Before this, the nobility and clergy enjoyed significant tax privileges, and taxation was opaque in both scope and amount (Juhász, 2015). Similar to D, individuals in HU are subject to Act CXVII of 1995 on Personal Income Tax ("Szja tv.", hereinafter: SZJA) if they reside in the country for more than 183 days (§ 3 IIb SZJA) or establish domicile there (§ 3 IIc SZJA).

HU follows the worldwide income principle (§ 3 I “A magánszemély minden jövedelme adóköteles...”) (Felkai, 2024), meaning all income and financial benefits (§ 4 I, II SZJA), denominated in Hungarian forints (HUF), are subject to taxation. Income is categorized into three main sources:

- Income from self-employment (e.g. freelancers), § 16 SZJA,
- Income from employment (e.g. employees), § 24 I SZJA,
- Other income, § 28 I SZJA.

When comparing these three categories of income under the SZJA with the seven income types of the D EStG, the HU system may appear to have a broader regulatory scope. However, this is not entirely accurate, as § 28 SZJA serves as a residual clause for all income not explicitly listed under other categories: “Egyéb jövedelem [other income] 28. § (1)”. This provision ensures that all income is accounted for taxation (Reith, 2024).

The total income in HU is taxed at a flat rate of 15% on the taxable base (§ 8 I, § 3 ff. SZJA). Certain exceptions are outlined within the SZJA itself, such as in Part III, chapter X, § 49a VIba SZJA.

Some income is taxed under a schedular system, meaning only gross revenues are considered without accounting for related expenses. For instance, self-employed individuals can opt to either:

- Tax their gross revenues at a flat rate of 10% (§ 17 IIIb SZJA), or

- Deduct expenses (up to 50% of revenues) and calculate the taxable base as the difference between revenues and expenses, which is then taxed at the 15% rate (§ 17 IIIa SZJA).

Deductions are allowed only as stipulated by law. Examples include:

- Family tax allowances (§ 29a I SZJA) or
- Discounts for newlywed couples (§ 29c SZJA) (Rádi, 2023).

Certain types of income are exempt from taxation, similar to the D system. These include scholarships (annex 1 of Act CXVII of 1995, Nos. 1.1 and 3.2.6) and benefits for foster parents or childcare subsidies (annex 1 of Act CXVII of 1995, No. 1.3) (NAV, 2024).

In HU, tax liability arises at the commencement of an activity or the establishment of a legal relationship (§ 9 I SZJA). Depending on the type of income, taxpayers must report their taxable revenues in a tax return (§ 13 SZJA), typically due by May 20 of the following year (§ 44f, § 11 I SZJA). The tax authority (NAV, before "Adó- és Pénzügyi Ellenőrzési Hivatal" (APEH)) prepares a preliminary tax draft (§ 12b SZJA) and determines the final tax liability.

5. Comparative legal analysis of corporate tax systems in Germany and Hungary for legal entities and selected commercial entities

5.1. German corporate tax – “Körperschaftsteuer (KSt)”

The corporate tax in D [Körperschaftsteuer (KSt)] and an independent type of tax distinct from income tax (ESt) and applies to legal entities (l.p.) or corporations. L.p. are legal constructs capable of holding rights and obligations in their own name (§ 14 II and § 21 ff. BGB, granting full legal capacity). Representative examples include the German Limited liability company [Gesellschaft mit beschränkter Haftung (GmbH)], § 1 ff. Limited Liability Company Act [Gesetz betreffend die Gesellschaften mit beschränkter Haftung (GmbHG)] or the European Societas Europaea (SE), which resembles the stock corporation [Aktiengesellschaft (AG)], pursuant to § 1 I S. 1 Stock Corporation Act [Aktiengesetz (AktG)].

Corporations that establish either their registered office or management in D (§ 10, § 11 AO) are subject to unlimited corporate tax liability, encompassing their domestic and foreign income (§ 1 I, Körperschaftsteuergesetz (KStG) [Corporation Tax Act]).

On the other hand, Partnership, are only granted limited legal capacity and are not subject to the KStG. Instead, the partners behind the partnership are considered taxpayers and are subject to income tax, adhering to the principle of transparency ("Transparenzprinzip") (Beuthien, 2011; Vogl, 2024; Sagasser, 2024).

By law, l.p. are deemed to generate business income (§ 1 I No. 1, § 8 I, II KStG, § 15 I No. 1, § 15 II, § 2 I No. 2, § 2 II No. 1 EStG). They are subject to the net worth comparison method or accrual accounting (§ 1, § 6, § 238 ff. HGB; § 7 IV KStG; § 140 AO; § 4 I, § 5 I EStG). This method involves offsetting all operating revenues against operating expenses to calculate either profit or loss.

A positive (KStG-) base is further adjusted according to specific provisions under the KStG (§ 7 II KStG). These include corrections for unreasonable benefits provided to shareholders (referred to as hidden profit distributions, § 8 III S. 2 KStG) or e.g. half of the remuneration paid to members with oversight functions (supervisory boards under § 111 AktG) is added back to prevent undue enrichment (Gosch, 2020).

The resulting taxable income is subject to a flat corporate tax rate of 15% (§ 7 I, § 23 KStG).

Certain entities are granted exemptions from KStG, such as the "Deutsche Bundesbank" (§ 5 I No. 2 KStG) or state organizations like pension, death, and health insurance funds (§ 5 I No. 3 KStG). These exemptions are generally granted for charitable or public welfare purposes (Märtens, 2020, pp. 258–259).

5.2. Hungarian corporate tax – “Vállalati nyereségadó - társasági adó (tao)”

The corporate tax in HU ["társasági adó" (tao)] is, as an independent type of tax and partly similar to the German KSt, because the tao is designed as a profit tax. So it include l.p., such as the joint stock company ["részvénytársaság" (rt)], a stock corporation ["korlátolt felelősségű társaság" (kft), an equivalent to a limited liability company]. Over all it includes HU (single) businesses and partnerships, such as the limited liability company ["közkereseti társaság" (kkt)], general partnership or limited partnership ["betéti társaság" (bt)]. If all these units have registered office or management in HU (§ 1 I, § 2 II, § 2 IIj, § 4 II, Act LXXXI of 1996 on Corporate Tax and Dividend Tax ["Tao tv.", hereinafter: TAO]), the HU administration can tax the income they earn.

The inclusion of partnerships and sole proprietorships in a corporate tax-like system represents a Hungarian tax perspective (detached from the civil or corporate law). It also deviates from the D system, where such entities are typically subject to income tax under the EStG framework in order to maintain the German "Transparenzprinzip" (BMF, 2009).

In the case of sole proprietorships, HU tax law differentiates between commercial and professional self-employment activities. The TAO primarily applies to commercial activities, while taxation under the SZJA is more likely for other self-employment activities, such as primary agricultural production or the work of auditors (§ 16, § 17 IIIa SZJA; Felkai, 2024).

The different tax classification of business units is generally unproblematic within the respective national frameworks but can lead to taxation conflicts in cross-border activities.

Similar to the German KStG, the HU corporations must include all domestic and foreign income in their taxable base ("teljes körű adókötelezettség", § 3 I TAO). However, unlike in D, the determination of profit or loss in HU is based on accounting standards ("Számviteli törvény"), such as IFRS (§ 1 V, VI, § 4 IVa TAO), for a tax year/calendar year (§ 5 Ia TAO). Entities can file simplified annual reports, simplified balance sheets (§ 5 III TAO), or cash accounting statements (§ 6 II TAO).

The TAO also includes specific modifications to the taxable base, regulated under § 6 I, 7, 18, 28, and 29 TAO. After these adjustments are applied, the remaining positive taxable base (§ 4 XXI: "jövedelem: az e törvényben az adó alapjaként meghatározott összeg...", § 5 TAO) is subject to a flat tax rate of 9% (§ 5 I, § 19 TAO). The result of this calculation constitutes the corporate tax liability for the legal entity.

Tax exemptions are granted by statutory provision and are listed in § 2 IV TAO in conjunction with annex 5d of act LXXXI of 1996. These exemptions include, among others, the Central Bank of Hungary ["Magyar Nemzeti Bank" (MNB)] (No. 1), charitable organizations (No. 4 and 5), and foundations (§ 20 I TAO).

6. Summary of the income tax systems in Germany and Hungary

A summary of Sections 4 and 5 can be found in the *Table 1* and *Table 2*.

Direct income tax for private individuals in Germany and Hungary

Table 1: Summary of the tax system comparison EStG and SZJA (chapter 4)

Direct/ income tax	Taxes a „regular people“	
Law	Einkommensteuergesetz (EStG)	"Személyi jövedelemadó" (SZJA)
Tax subject	Person who lives in the country for a certain period of time (6 month)	Person who lives in the country for a certain period of time (min. 183 days)
Basis of assessment tax object	Revenue minus all costs determined per type of income, 7 areas	Revenue minus all costs determined per type of income and partially tax schedule system: Revenue per type of income, only 3 areas
Tax exemption	Example: Supplementary insurance	Example: Maternity allowances
Reduce tax	Example: discount for childs or married couples	
Tax rate, allowance	Progressive tariff with 14% to 45%; Basic allowance of € 10.908 € (2024)	Flat Rate 15 %; No basic tax allowance, all income is taxed

Source: Own presentation

Direct income tax for corporates or business companies in Germany and Hungary**Table 2: Summary of the tax system comparison KStG and TAO (chapter 5)**

Direct/ income tax	Tax for coporates / taxes on profit	
Law	Körperschaftsteuergesetz (KStG)	"Vállalati nyereségadó - társasági adó" (TAO)
Tax subject	Business companies, Example: "Aktiengesellschaft" (AG); Not Partnerships, Headquarters or business management in Germany	Business companies, Example: "részvénytársaság" (rt) and partnerships like "betéti társaság" (bt), Headquarters or business management in Hungary
Basis of assessment tax object	All income less operating expenses based on accounting, with special tax law modifications Headquarters or its management in Germany. All income less operating expenses, based on accounting	All income less operating expenses based on accounting or income-expenditure-determination, with special tax law modifications Revenue minus all costs determined per type of income and partially tax schedule system: Revenue per type of income, only 3 areas
Tax exemption	Example: non-profit organizacions	
Reduce tax	Unavailable	
Tax rate, allowance	Single rate of 15%, No basic tax allowance	Single rate of 9%, No basic tax allowance

Source: Own presentation

At a fundamental level, the income tax systems in HU and D share similarities. Both systems classify n.p. and l.p under either income tax (ESt in D, Szja in HU) or corporate tax (KSt in D, tao in HU).

However, a critical legal comparison reveals significant differences in the detailed provisions of the two systems:

Income of commercial entrepreneurs: In D, such income is subject to ESt with a progressive tax rate ranging from 14% to 45%. In HU, these entities may be subject to tao, allowing flexibility in the choice of profit determination method (accrual accounting or cash accounting), with a flat tax rate of only 9%.

A comparison of the parameters of profit determination and the applicable tax rates also shows differences between countries. Many accounting terms are written in the HU tax law itself. In D taxpayers must refer to multiple legal sources. For Examples:

Investment incentives in Hungary: In HU, various tax incentives are available for investments, such as for research and development (R&D) activities (§ 22 ff. TAO) and are explicitly outlined in the tao itself. These incentives are optionally distributed over several years. Taxpayers in D, however, must refer to a separate legal framework, the Research Allowance Act [Forschungszulagengesetz (FZulG)], established in 2020 (BMF, 2023)), which regulates such incentives with its own parameters

Tax reserve provisions under TAO: The tao contains specific rules for calculating tax reserves (§ 24a, § 7 Ib TAO). In D, similar principles for reserve calculations can be derived from the interpretation of the German § 7 I, 8 I KStG; §15 I, 4 I, 5 I, § 6 IIIa EStG; § 249 HGB as well as from R. 7.1 I S. 1, 2 No. 1 KStG directive and R. 5.7 EStG directive.

Depreciation of assets: In HU, § 7 Id tao in conjunction with Annexes 1 and 2 tao governs the depreciation of assets. For instance, buildings are depreciated at rates ranging from 2% to 6%. In D, asset depreciation is primarily regulated by § 252 I No. 3, 4, § 253 III HGB and § 5 I S. 1, § 7 IV S. No. 1 EStG. Operational buildings are typically depreciated at a rate of 3%, depending on the year of construction.

When different states apply varying laws and tax parameters, achieving consistent taxation (§ 88 II AO) of income or equitable tax credits (§ 34c I S. 1 EStG) or exemptions (§ 32b I No. 2, 3 EStG) for foreign income under double taxation agreements (DTAs) becomes problematic. This disparity arises because the two states base their calculations on different tax bases.

(Furthermore, divergent interpretations of other tax parameters – such as those regulated under § 2 and § 7 of the German Foreign Tax Act [Außensteuergesetz], § 50d IX, or § 2a EStG – can exacerbate these differences. However, these aspects are not explored further due to the scope of this paper.)

7. Insights into international taxation and double taxation systems

Each state has the right to regulate its internal and external legal relations independently (in German called "Staatssoveränität" (Schallmoser, 2024)) and to determine its taxation rights over income within its territory (Frotscher, 2020). When taxpayers and/or tax objects are located in two different countries, economic double taxation may arise, as both states may claim tax rights over the same tax base during the same period (Breithecker & Klapdor, 2016; Lehner, 2021). In this situation, the taxpayer must pay taxes on the same income multiple times. International DTAs are designed to allocate tax rights between states.

Germany has signed around 100 DTA, while Hungary has signed approximately 80. There is also a DTA between HU and D, which was concluded on February 28, 2011, and has been in effect since December 30, 2011 (art. 30 I DTA-HU-D).

The distribution of taxation rights in a DTA is based on the so-called "genuine link" (Lehner, 2021), which involves identifying and weighing the relevant ties of the taxpayer and/or tax object to each country:

- a) *Multiple (residence) locations of a taxpayer:* If a person establishes multiple (residential) addresses in different countries, it must be determined which state the person is considered resident in, allowing for unlimited taxation, § 1 I EStG, § 3 I TAO, § 2 I KStG, § 1 IV, § 49 I EStG, § 3 II SZJA, § 2 IV TAO. According to the DTA, a "genuine link" is determined by evaluating the taxpayer's life circumstances (in a four-stage review process, the "Tie-Breaker Rule" (Nürnberg, 2024)). The result of this DTA-test is the identification of a resident taxpayer, so that the country of residence has the right to tax the resident's worldwide income.
- b) *Foreign income of a taxpayer:* If a taxpayer earns income from abroad, the "genuine link" is determined based on the type of income (tax objects) and whether they have a fixed connection to a specific country.

E.g. if a Hungarian taxpayer holds shares in a German GmbH and that GmbH distributes its profits to the Hungarian shareholder, the tax rights over the dividend income belong to both the country of the paying GmbH (Germany) and the country of the shareholder (Hungary) (art. 10 I, II DTA-HU-D). A graphical representation of this and other examples are in *Figure 2*.

Examples of different types of sources of income in transactions between 2 states

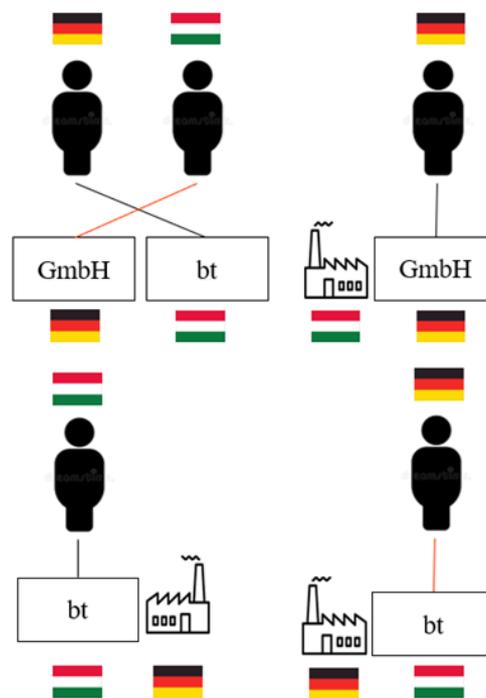


Figure 2: Representation of possible case scenarios of internationally operating taxpayers

Source: Own presentation

E.g., if a German taxpayer is involved in a Hungarian “betéti társaság” (bt) and this entity generates rental or business establishment income, the country where the property or business establishment is located generally has the right to tax the income (art. 5, art. 7 VII, art. 6 I (permanent establishment), art. 5, art. 7 DTA-HU-D). The problem arises with the attribution of income. From tax perspective of the German-government, the income is attributed to the German taxpayer due to the German “Transparenzprinzip“ and get taxed under the law of the EStG.

From Hungary’s unique tax perspective, the income belong to the “bt” as Hungary treats the company as an independent tax subject. So HU will taxed the “bt” with the tao. So the income tax for a n.p. (ESt) get in contradiction to the tax for a l.p. (tao).

Although the DTA determines the allocation of taxation rights, conflicts can arise because each state interprets the rules differently. In the worst-case scenario, as in the example provided, Germany could tax the rental/business establishment income because the German taxpayer resides there (§ 1 I EStG, § 8 AO), while Hungary would tax the same income in the “bt” under the provisions of § 1, § 2, § 4 TAO.

Although the residence country of the taxpayer has the obligation, under international treaties, to either exempt income that has already been taxed abroad from taxation (§ 32b I No. 2, 3 EStG) or to grant a tax credit for the foreign tax paid (§ 34c EStG), in the example case, the foreign taxation would not be recognized in Germany. This is because the tao is not comparable to the German EStG and applies to a different tax subject (a corporation). Even if the foreign taxation is recognized, the states involved would calculate the income differently and use different tax bases, leading to disparities in the determination of taxable income (see section 6).

8. Conclusion

The research question of this paper can be answered as follows:

Each national tax system presents specific challenges, inconsistencies, high bureaucratic demands, and complex structures (chapter 2). If international investments are pursued despite these complexities, taxpayers must thoroughly familiarize themselves with the differing formal and substantive tax laws of each country (chapters 4 and 5).

While tax savings may be achieved by taking advantage of tax rate differences between countries (chapter 3), taxpayers need to be aware of the risk of double taxation – when two states claim tax rights for the same taxpayer and/or the same taxable object. Each state retains the sovereignty to set its own tax rules (e.g. allocating income to a HU tax authority) (chapters 5, 6 and 7). In doing so, system differences arise, hence double taxation, which endanger taxpayers' liquidity and threaten economic prosperity within the system.

DTAs can mitigate cases of double taxation but cannot completely eliminate them (chapter 7), as states have different tax views on the tax subjects and objects and do not change them for international transactions.

A potential solution could involve fostering a deeper understanding of each country's legal framework and its inconsistencies, alongside improved communication and collaboration between the involved states. This approach could enhance legal certainty and build a sustainable tax system, enabling taxpayers to make optimal financial decisions.

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