Decision 8/2007 (II. 28.) AB

IN THE NAME OF THE REPUBLIC OF HUNGARY

In the matter of petitions seeking posterior review of the unconstitutionality of a statute, the Constitutional Court has – with concurrent reasoning by *dr. László Kiss*, Judge of the Constitutional Court, and with dissenting opinions by *dr. András Bragyova* and *dr. András Holló*, Judges of the Constitutional Court – adopted the following

d e c i s i o n :

1. The Constitutional Court holds that Section 6 paras (5) to (9) of Act LXXXI of 1996 on Corporate Tax and Dividend Tax are unconstitutional and, therefore, annuls them as of the date of promulgation of this Decision.

2. The Constitutional Court holds that Section 225 para. (16) of Act LXI of 2006 on the Amendment of Certain Acts on Financial Subjects is unconstitutional and, therefore, annuls it as of the date of promulgation of this Decision.

The Constitutional Court publishes this Decision in the Hungarian Official Gazette.

R e a s o n i n g

I

The Constitutional Court has received several petitions seeking posterior constitutional review and annulment of Section 6 paras (5) and (6) of Act LXXXI of 1996 on Corporate Tax and Dividend Tax (hereinafter: the ACT) as specified in Section 25 of Act LXI of 2006 on the Amendment of Certain Acts on Financial Subjects (hereinafter: the AAF).

Under Section 28 (1) of amended and consolidated Decision 3/2001 (XII. 3.) Tü. by the Full Session on the Constitutional Court's Provisional Rules of Procedure and on the Publication Thereof (ABH 2003, 2065; hereinafter: the Rules of Procedure) the Constitutional Court has consolidated the petitions and judged them in a single procedure as they are of the same subject.

a) One of the petitioners challenges Section 25 of the AAF amending Section 6 of the ACT as of 1 January 2007 by introducing a new paragraph (5). According to the petitioner, the relevant provision of the AAF violates Article 70/I of the Constitution by not allowing a subject of taxation – having a verifiable real income less than the »expected« tax base regulated in the AAF – to bear the public burdens on the basis of his income and wealth.

Therefore, the petitioner seeks establishment of the unconstitutionality and annulment of the challenged provision of the AAF.

b) Other petitioners formally request the Constitutional Court to establish the unconstitutionality of, and to annul the whole Section 25 of the AAF, but – according to the contents of their petitions – they only challenge it in respect of the provisions supplementing Section 6 of the ACT with the new paragraphs (5) and (6).

As argued by the petitioners, the challenged statutory regulation "considers all enterprises generating loss to be tax evaders and, therefore, it applies tax as a »quasi sanction« contravening the rule of law granted in Article 2 para. (1) of the Constitution as well as the principle of proportionate bearing of public burdens enshrined in Article 70/I of the Constitution." The petitioners further support their arguments by making reference to Decision 31/1998 (VI.25.) AB. (ABH 1998, 240)

As explained by the petitioners, the challenged provision of the AAF introduces among the rules of the ACT an "expected tax", which is a "minimum tax" to be paid – with a few exceptions – by all enterprises, including the ones that generate loss.

The petitioners complain about "forcing the enterprises that comply with the law and have no real profits to pay the supertax just because some enterprises choose to evade paying taxes."

As another argument of the petitioners, although the challenged regulation draws the tax evading enterprises into the scope of taxpayers, at the same time, by imposing a tax payment obligation upon the loss-making enterprises as well, it surely makes their future operation impossible, closing them out of the scope of taxpayers peremptorily.

The petitioners hold this to lead to the violation of the proportionate bearing of public burdens as the legislator "applies the same judgement to unequal subjects".

With reference to the reasoning of Decision 29/2005 (VII. 14.) AB by the Constitutional Court (ABH 2005, 316), the petitioners argue that the "expected tax"- similarly to the excessive tax of "confiscating character" mentioned in the above decision – results in the elimination of the loss-making enterprises, contravening this way the aim of taxation, i.e. the proportionate bearing of public burdens.

The petitioners also complain about the challenged regulation allowing the deduction of only the procurement value of goods sold (hereinafter: the PVGS) from the revenues of the taxpayer when

defining the base of corporate tax, which is a kind of profit tax, and it does not acknowledge several other outgoings typical in the case of enterprises – such as personnel costs or the value of mediated services - as items deductible from the tax base.

The petitioners specify Article 70/I and Article 2 para. (1) as the constitutional provisions violated by the challenged regulation.

c) Another petitioner also asks the Constitutional Court to annul the whole of Section 25 of the AAF due to the violation of Article 70/I of the Constitution. As argued by the petitioner, the challenged provision of the AAF levies tax on an income actually not obtained by the taxpayer.

d) Another petitioner requests the Constitutional Court to establish the unconstitutionality of Section 21 para. (1) and Section 25 of the AAF, furthermore, to annul the challenged statutory regulations with *ex tunc* effect based on Article 2 para. (1) and Article 57 para. (2) of the Constitution. According to the petitioner, by regulating the "expected tax", the legislature has established an incontestable statutory presumption without a chance for proving the contrary. In the petitioner's opinion, the constitutional principle of the presumption of innocence is impaired by the legislature applying the "expected tax" as a kind of collective sanction based on the taxpayer's alleged conduct aimed at tax evasion.

The petitioner holds that an expected public burden "of flat-rate nature" may not be the tool of suppressing the taxpayers' conduct aimed at tax evasion – under the principle of the "aim justifying the measures" – and the adequate tool to achieve this goal would be increasing the efficiency of tax control.

e) As challenged by another petitioner, the relevant provisions of the ACT oblige even the loss-making companies to pay corporate tax as from 1 January 2007. The petitioner also challenges Section 225 para. (16) of the AAF providing for an obligation to pay an advance on tax – even for the year 2007 – in respect of the so-called "expected corporate tax".

As argued by the petitioner, when adopting the challenged statutory provisions, the legislature failed to examine the public burden bearing capacity of the society and the "subjects of the economy".

In respect of Section 6 para. (5) of the ACT, the petitioner refers to the legislature defining the tax base of the so-called "expected corporate tax" ("the pre-tax profit shall be positive even in case of making losses") by regarding a certain percentage of the revenues as the tax base – not allowing any deduction of costs and expenses.

According to the petitioner, the challenged statutory provisions are contrary to Articles 70/I and 70/A of the Constitution.

f) Another petitioner raises objections against Section 6 paras (5) and (6) of the AAF, as specified in Section 25 of the AAF, by virtue of Article 2 para. (1), Article 70/A para. (1) and Article 70/I of the Constitution.

The petitioner holds the challenged provisions to violate the constitutional provision of the democratic rule of law granted in Article 2 para. (1) of the Constitution.

As argued by the petitioner, the challenged statutory provisions aim at a revenue-proportionate taxation of the companies that "pretend to make losses", thus withdrawing themselves – in a "manipulative manner" – from the obligation of paying corporate tax.

The challenged regulations [defining the tax base as laid down in Section 6 para. (5) of the ACT] do not take into account the real conditions of the economy and the requirements resulting from the application of the accounting rules, using the presumption of bad faith, "not being concerned about who and to what extent are sanctioned".

According to the petitioner, "the regulation introduces a taxation sanction the application of which is independent from the actual breach of the law, alienating from the abusive conduct aimed at tax evasion to be sanctioned, and this way it may impose excess taxation – as a sanction – upon law obeying tax subjects acting in good faith."

As held by the petitioner, "the flat-rate sanction as an excess tax burden to be applied independently from establishing the breach of the law – based on the presumption of an unlawful conduct – is clearly against the requirement of the democratic rule of law granted in Article 2 para. (1) of the Constitution."

The petitioner argues that "the regulation on the minimum corporate tax base" [Section 6 para. (5) of the ACT] violates the constitutional provision on the prohibition of discrimination as granted in Article 70/A para. (1) of the Constitution.

On the one hand, it makes an unjustified discrimination between the subjects of corporate tax on the basis of their activities and, on the other hand, similar unjustified discrimination between the subjects of taxation is applied by way of "the arbitrary determination of the items deductible from the minimum tax base".

As challenged by the petitioner, in the case of the taxpayers where – due to the features of the business (the activity of the enterprise) or to the application of the regulations on accounting settlement related to the activity – the net income (profit) is low relatively to the full amount of revenues collected in the tax year, the rule on the minimum tax base leads to an unjustified excess tax payment obligation – compared to the real income conditions – resulting in discrimination concerning the tax subjects.

In the petitioner's opinion, the legislature "arbitrarily" defining the items deductible from the "minimum corporate tax base" results in further discrimination, as the tax subjects who do not perform

entrepreneurial activity at a site abroad and the ones who – in connection to their manufacturing or service activity – typically do not set off PVGS have no chance to decrease the tax base.

The petitioner holds the provisions on the "minimum corporate tax base" to be contrary to Article 70/I of the Constitution as they levy tax upon a "fictional" tax object: a significant part of the tax subjects have to pay corporate tax upon an income (profit) actually not realized.

g) Another petitioner also challenges Section 6 paras (5) and (6) of the ACT as specified in Section 25 of the AAF, proposing annulment of the statutory provisions held unconstitutional. The petitioner considers the challenged provisions to be contrary to the principle of the proportionate sharing of public burdens as laid down in Article 70/I of the Constitution, the prohibition of discrimination regulated in Article 70/A of the Constitution, and the constitutional requirement of the rule of law granted in Article 2 of the Constitution. With regard to Article 70/I of the Constitution, the petitioner complains about Section 6 para. (5) of the ACT "not complying with the principle of proportionality, as this provision is going to cause, in respect of certain tax subjects, taxation not being proportionate to their conditions of income and wealth."

To support the above arguments, the petitioner refers to Section 6 para. (5) of the ACT, according to which the tax subjects engaged in commercial activities may deduct PVGS from their revenues when determining the tax base, while the tax subjects producing goods "practically may not deduct anything from their revenues."

According to the petitioner, the challenged provision of the ACT is in particular disadvantageous for the tax subjects who produce goods subject to excise duty as in their case the net turnover contains the excise duty including the VAT, too, and therefore the level of the tax is "unreasonably high in their case as compared to other sectors." The petitioner also challenges the fact that the legislature failed to allow – with the exception of PVGS – deducting the excise duty including the VAT from the net turnover when determining the tax base under Section 6 para. (5) of the ACT.

The petitioner holds this to be discriminative in respect of the tax subjects engaged in commercial activities and the ones producing goods subject to excise duty, as the former ones may deduct PVGS from the net turnover while the latter ones "have to pay tax even upon the tax they pay".

During its procedure, the Constitutional Court has obtained the opinions of the Minister of Justice and Police as well as of the Minister of Finance.

II

1. The provisions of the Constitution relevant to the petition are as follows:

"Article 2 (1) The Republic of Hungary is an independent democratic state under the rule of law."

"Article 57 (2) In the Republic of Hungary no one shall be considered guilty until a court has rendered a final legal judgment determining criminal culpability."

"Article 70/A para. (1) The Republic of Hungary shall respect the human rights and civil rights of all persons in the country without discrimination on the basis of race, colour, gender, language, religion, political or other opinion, national or social origins, financial situation, birth or on any other grounds whatsoever."

"Article 70/I. All natural persons, legal persons and unincorporated organizations have the obligation to contribute to public revenues on the basis of their income and wealth."

2. The provisions of the AAF challenged by the petitioners are as follows:

"Section 21 Section 1 para. (1) of Act LXXXI of 1996 on Corporate Tax and Dividend Tax (hereinafter: the ACT) shall be replaced by the following provision:

(1) In the Republic of Hungary, on the basis of an economic activity aimed at, or resulting in, gaining income or wealth (hereinafter: entrepreneurial activity), the obligation to pay corporate tax under this Act of Parliament shall be performed – with due account to the constitutional provision on bearing public burdens – in accordance with the provisions of this Act and with account to the provisions of the Act on the Rules of Taxation as well."

"Section 25 Section 6 para. (4) of the ACT shall be replaced by the following provision, and at the same time the following paragraphs (5) and (6) shall be added to it:

(4) In the case of foundations, public foundations, social organizations, public bodies, churches, housing co-operatives, voluntary mutual insurance funds, target organizations, Employees' Co-ownership Programme, non-profit companies, higher education institutions with a public benefit or extra public benefit status, social co-operatives, water management associations and foreign entrepreneurs, the provisions of paragraphs (1) and (2) shall apply, in due consideration of Sections 9 to 14.

(5) If the taxpayer's tax base under paragraph (1) is less than 2% of the total revenues less the procurement value of the goods sold and the revenues at the foreign site in the tax year, then the tax base shall be the latter amount.

(6) The provisions of paragraph (5) shall not be applied by the taxpayer

a) in the tax year of the pre-company and the next year, or

b) if the tax subject falls under Section 2 para. (2) items *e)* to *h)* or para. (3), and if the taxpayer is a social co-operative, school co-operative or a non-profit company with a public benefit or extra public benefit status, or

c) in the tax year, the annual turnover is lower than 75% of the annual turnover of the previous tax year, or

d) if in the tax year or the previous tax year, the tax subject had a natural disaster damage."

"Section 225 (16) If the taxpayer is to declare an advance on tax on the basis of the tax payable for the year 2006, then the amount of the advance shall be calculated by taking into account the provisions under Section 6 paras (5) and (6) of the ACT in force as of 1 January 2007."

3. The provisions of Act LXI of 2006 on the Amendment of Certain Acts on Financial Subjects (hereinafter: the AACF) under examination are as follows:

"Section 8 (1) The following new paragraph (5) shall be added to Section 6 of the ACT:

»(5) If the taxpayer's tax base under paragraph (1) is less than 2% of the total revenues less the procurement value of the goods sold and the revenues at the foreign site in the tax year, after the corrections under paragraphs (7) and (8), then the tax base shall be the latter amount.«"

(2) The following new paragraphs (7) and (8) shall be added to Section 6 of the ACT:

»(7) The following shall be deductible from total revenues:

a) the revenues settled in the tax year – as the original cost of the shareholding obtained in the tax subject established by way of preferential transformation – by the member or shareholder of the legal predecessor, when applying the provision under Section 7 para. (1) item *gy)*,

b) the revenue settled in the tax year by the transferring company, in the case of preferential transfer of assets, on the basis of the transfer of its independent organizational unit, when applying the provision under Section 16 para. (12),

c) the exchange profit settled in the tax year by the member or shareholder of the acquired company, in respect of the shareholding charged off on the basis of preferential exchange of shareholdings, when applying the provision under Section 7 para. (1) item *h)*.

(8) When applying the provisions under paragraph (7), the following shall be added to the total revenues:

a) with account to the preferential transformation of the legal predecessor or to a preferential exchange of shareholdings, the member or shareholder shall add the amount settled in the tax year

under any title from the amount taken into account as a deductible item, as the deduction of the original costs of the acquired shareholding by way of charging off the book value thereof (but not more than the accumulated amount taken into account as a deductible item in respect of the shareholding under the relevant provision), and in the case of termination without a legal successor, the relevant part in the tax year not yet settled as an increasing item,

b) at the company handing over, the company taking over – based on the declaration by the party handing over – shall add the amount of depreciation settled according to the bookkeeping rules for the material assets and intangibles, calculated in proportion to the original costs of the assets taken over, from the amount taken into account as the deduction from the total revenues, and in the tax year of termination without a legal successor, the remaining amount shall be added.«

(3) The following new paragraph (9) shall be added to Section 6 of the ACT:

»(9) For the purpose of paragraph (6), natural disaster damage means damage caused by a natural disaster (in particular, hail, flood, inland inundation, freeze, sandstorm, drought, destruction caused by snow, ice or wind, storm, earthquake and fire of a natural or biological cause), the level of which amounts to at least 15% of the taxpayer's annual turnover of the previous tax year (in the case of a taxpayer established by way of transformation, calculated from the turnover of the legal predecessor as the identical, accumulated or divided turnover – according to the form of the transformation). The natural disaster damage shall be verified by a document certifying that the damage has been done (e.g. expert opinion, minutes or other document issued by the insurance company, the authority of agricultural administration, the authority of disaster management), or – if the taxpayer does not possess any document issued by an independent organization – the minutes taken by the taxpayer. The taxpayer shall send the minutes taken by the taxpayer to the tax authority in charge within 15 days of the damage event. In the case of a failure to keep the deadline, no application for relief may be submitted.«"

"Section 126 (1) The provisions of this Act amending the ACT – with the exception of the provisions under paragraphs (2) and (3) – shall enter into force as of 1 January 2007.

(2) Section 6 para. (9) of the ACT as specified in this Act shall enter into force on 15 February 2007, and its provisions shall be applied in respect of natural disaster damage occurred after its entry into force."

"Section 172 The following shall not enter into force: (…)

b) Section 6 para. (5) of the ACT as established in Section 25 of the Amending Act, (...)"

4. The relevant provisions of Section 6 paras (5) to (9) of the ACT in force at the time of judging upon the petitions are as follows:

"Section 6 (5) If the taxpayer's tax base under paragraph (1) is less than 2% of the total revenues less the procurement value of the goods sold and the revenues at the foreign site in the tax year, after the corrections under paragraphs (7) and (8), then the tax base shall be the latter amount.

(6) The provisions of paragraph (5) shall not be applied by the taxpayer

a) in the tax year of the pre-company and the next year, or

b) if the tax subject falls under Section 2 para. (2) items *e)* to *h)* or para. (3), and if the taxpayer is a social co-operative, school co-operative or a non-profit company with a public benefit or extra public benefit status, or

c) in the tax year, the annual turnover is lower than 75% of the annual turnover of the previous tax year, or

d) if in the tax year or the previous tax year, the tax subject had a natural disaster damage.

(7) The following shall be deductible from total revenues:

a) the revenues settled in the tax year – as the original cost of the shareholding obtained in the tax subject established by way of preferential transformation – by the member or shareholder of the legal predecessor, when applying the provision under Section 7 para. (1) item *gy)*,

b) the revenue settled in the tax year by the transferring company, in the case of preferential transfer of assets, on the basis of the transfer of its independent organizational unit, when applying the provision under Section 16 para. (12),

c) the exchange profit settled in the tax year by the member or shareholder of the acquired company, in respect of the shareholding charged off on the basis of preferential exchange of shareholdings, when applying the provision under Section 7 para. (1) item *h)*.

(8) When applying the provisions under paragraph (7), the following shall be added to the total revenues:

a) with account to the preferential transformation of the legal predecessor or to a preferential exchange of shareholdings, the member or shareholder shall add the amount settled in the tax year under any title from the amount taken into account as a deductible item, as the deduction of the original costs of the acquired shareholding by way of charging off the book value thereof (but not more than the accumulated amount taken into account as a deductible item in the respect of the shareholding under the relevant provision), and in the case of termination without a legal successor, the relevant part in the tax year not yet settled as an increasing item,

b) at the company handing over, the company taking over – based on the declaration by the party handing over – shall add the amount of depreciation settled according to the bookkeeping rules for the material assets and intangibles, calculated in proportion to the original costs of the assets taken over, from the amount taken into account as the deduction from the total revenues, and in the tax year of termination without a legal successor, the remaining amount shall be added.

(9) For the purpose of paragraph (6), natural disaster damage means damage caused by a natural disaster (in particular, hail, flood, inland inundation, freeze, sandstorm, drought, destruction caused by snow, ice or wind, storm, earthquake and fire of a natural or biological cause), the level of which amounts to at least 15% of the taxpayer's annual turnover of the previous tax year (in the case of a taxpayer established by way of transformation, calculated from the turnover of the legal predecessor as the identical, accumulated or divided turnover – according to the form of the transformation). The natural disaster damage shall be verified by a document certifying that the damage has been done (e.g. expert opinion, minutes or other document issued by the insurance company, the authority of agricultural administration, the authority of disaster management), or – if the taxpayer does not possess any document issued by an independent organization – the minutes taken by the taxpayer. The taxpayer shall send the minutes taken by the taxpayer to the tax authority in charge within 15 days of the damaging event. In the case of a failure to keep the deadline, no application for relief may be submitted."

III

The petitions are well-founded.

1. It has been established by the Constitutional Court with respect to the contents of the petitions that the petitioners had originally filed a definite request suitable for assessment concerning the establishment of the unconstitutionality and the annulment of Section 6 paras (5) and (6) of the ACT – established in Section 25 of the AAF – as well as of Section 225 para. (16) of the AAF.

The Constitutional Court has noted in the course of its procedure that upon the submission of the petitions, on 23 December 2006, the AACF was put into force, partly modifying and partly amending Section 6 of the ACT.

Under Section 172 item *b)* of the AACF, Section 6 para. (5) of the ACT – established by Section 25 of the AAF – shall not take effect as of 1 January 2007.

Section 8 para. (1) of the AACF provided for a new normative text of Section 6 para. (5) of the ACT with effect as of 1 January 2007.

Section 8 para. (2) of the AACF added two new paragraphs to Section 6 of the ACT [Section 6 paras (7) and (8)] similarly with effect as of 1 January 2007.

Furthermore, Section 8 para. (3) of the ACF introduced a new paragraph (9) into Section 6 of the ACT with effect as of 15 February 2007.

Having regard to the above amending provisions of the AACF affecting the ACT, the Constitutional Court called upon the petitioners to make their relevant statements. After being called upon, most of the petitioners refined their petitions, upholding them in respect of Section 6 paras. (5) to (8) of the ACT – taking force as of 1 January 2007 and being in force at the time of the constitutional review – as well as of Section 6 para. (9) of the ACT, taking force as of 15 February 2007. The petitioner challenging Section 225 para. (16) of the AAF has still maintained his request seeking establishment of the unconstitutionality and annulment of the relevant statutory provision.

When reviewing the contents of the challenged provisions of the ACT as established by the AAF and the AACF, the Constitutional Court has – according to its standing practice – examined the provisions of the statute (in the present case: the ACT) incorporating the challenged amended statutory provisions rather than the statutory provisions putting the amended statutory provisions into force. [Decision 174/B/1999 AB, ABH 2005, 870, 871; Decision 8/2003 (III. 14.) AB, ABH 2003, 74, 81; Decision 51/2004 (XII. 8.) AB, ABH 2004, 679, 683; Decision 28/2005 (VII. 14.) AB, ABH 2005, 290, 297]

In accordance with the practice of the Constitutional Court referred to above as well as with the contents of the petitions refined after calling upon the petitioners, the Constitutional Court has performed substantial examination in respect of the challenged statutory provisions of the ACT and the AAF mentioned before.

2. Examining the contents of the consolidated petitions, the Constitutional Court has first reviewed the petitions alleging violation of Article 70/I of the Constitution.

The petitioners hold the challenged provisions of the ACT and the AAF to violate the constitutional provision on proportionate bearing of public burdens as granted in Article 70/I of the Constitution. As argued by them, Section 6 para. (5) of the ACT, taking effect on 1 January 2007, introduced an "expected tax" ("expected tax base") into the ACT, imposing a burden – with a few exceptions – on all enterprises, including the loss-making ones.

Another complaint of the petitioners is related to the subjects of corporate tax that verifiably have tax bases less than the bases of the "expected tax" and that – by paying the "expected tax" – contribute to

the bearing of public burdens not proportionately to their actual conditions of income and wealth, but bearing an unjustifiably heavier tax burden than the taxpayers that declare their tax bases under Section 6 para. (1) of the ACT and pay corporate tax accordingly. Consequently, in the case of both loss-making enterprises and the ones that actually have tax bases lower than the bases of the "expected tax", Section 6 para. (5) of the ACT imposes tax upon an income not obtained in reality.

According to the petitioners, by the introduction of the "expected tax", the legislator has applied the same rules to unequal subjects, as the enterprises creating their corporate tax bases with the intention of tax evasion enjoy the same treatment as the loss-making enterprises, making loss despite lawfully operating their businesses. The further operation of the latter enterprises becomes impossible due to the "expected tax", and it prevents the tax to reach its goal.

The petitioners hold that the definition of the base of the "expected tax" also violates the proportionate bearing of public burdens, as the legislature has only acknowledged a few deductible items to decrease the amount of the taxpayer's total revenues in the tax year, setting up an incontestable statutory presumption which excludes the verification of the actual amount of the income obtained by the taxpayer (to prove contrary to the statutory presumption).

3. When judging upon the petitions alleging violation of Article 70/I of the Constitution, the Constitutional Court has made an overview of the challenged statutory regulations in the ACT.

Section 6 paras (5) and (6) of the ACT – taking force as of 1 January 2007 – supplements the provisions on determining the corporate tax base in Part II Chapter II of the ACT.

By way of the challenged provisions, the legislature has attempted to regulate the corporate tax – for the purpose of facilitating the balance of state finances – by making it mandatory for all actors in the sphere of the economy (i.e. for "everyone") to contribute to the bearing of public burdens.

In the opinion of the legislature, the enterprises falling under the ACT have in practice a wide scale of measures to influence their results, and therefore – in order to achieve the above objective – the law prescribes a "minimum" level of "expected income" to be the tax base.

Section 6 para. (5) of the ACT – taking force as of 1 January 2007 – has introduced the statutory provision on tax base of the "expected tax" challenged by the petitioners. Accordingly, the base of the "expected tax" corresponds to the total revenues of the taxpayer in the tax year, less the procurement value of the goods sold and the revenues at the foreign site, after the corrections – under Section 6 paras (7) and (8) of the ACT – with the items increasing or decreasing the amount of total revenues.

Section 8 para. (2) of the AACF has – as from 1 January 2007 – introduced into Section 6 of the ACT the amending provisions under paragraphs (7) and (8) mentioned above, to be applied as factors

amending the amount of total revenues in the tax year in the legal transactions made after 1 January 2007, in the case of preferential transformation, preferential transfer of assets and preferential exchange of shareholdings

If the taxpayer's corporate tax base determined under Section 6 para. (1) of the ACT is less than 2% of the base of the "expected tax" – defined in accordance with the above rules – then the taxpayer's corporate tax base shall be the base of the "expected tax".

Section 6 para. (6) of the ACT – taking force as of 1 January 2007 – as well as its paragraphs (7) and (8) are closely connected in terms of contents to the provisions on the base of the "expected tax" specified in Section 6 para. (5) of the ACT. Section 6 para. (6) of the ACT defines the cases when the taxpayer is not obliged to apply the provisions of paragraph (5) to the base of the "expected tax". Section 6 para. (7) of the ACT regulates the amending items to be deducted from the total amount of revenues in the tax year, while paragraph (8) contains the ones that increase it.

The content of Section 6 para. (9) of the ACT – taking force as of 15 February 2007 – is closely connected to Section 6 para. (6) of the ACT. On the one hand, it gives a definition of natural disaster damage for the purpose of Section 6 para. (6) of the ACT and, on the other hand, it regulates the verification of same.

4. In the present case, the Constitutional Court has to form an opinion in the constitutional question of whether by way of the statutory definition of the base of the "expected tax" – and the resulting introduction of the "expected tax" – the legislature has caused the legal institution of the tax to fall so far from the constitutional basis under Article 70/I of the Constitution as to make the challenged regulation unconstitutional. In addition, the Constitutional Court has to examine whether the challenged regulation results in taxing an income (profit) actually not obtained.

As pointed out by the Constitutional Court in many of its earlier decisions, the obligation of bearing public burdens is regulated in Article 70/I of the Constitution. On the one hand, Article 70/I of the Constitution requires all natural persons, legal entities and unincorporated organizations to contribute to public revenues and, on the other hand, the Constitution empowers the State to specify such payment obligations in Acts of Parliament. The manner and the level of contributing to public burdens are laid down in the relevant specific laws (among others, the tax laws).

As pointed out by the Constitutional Court in Decision 448/B/1994. AB (hereinafter: CCDec. 1) with regard to regulating the corporate tax, "it is within the legislature's scope of competence to determine the amount of profit that forms the base of the corporate tax, the accounting and tax-technique rules

necessary for establishing it, as well as the items decreasing or increasing the tax base." (ABH 1994, 724, 725)

There is only one requirement in the Constitution pertaining to the legislation with regard to the contribution to public burdens, i.e. that the given payment obligation should be in line with – proportionate to – the subjects' conditions of income and wealth. (Decision 1558/B/1991 AB, ABH 1992, 506-507)

As underlined by the Constitutional Court in CCDec.1 to reinforce the position explained in the above decisions, the legislation is not absolutely free in selecting the economic resource serving as the basis of taxation and in defining the subject of the tax; according to the constitutional provision on the sharing of public burdens, the taxation should remain bound to the conditions of income and wealth. (ABH 1994, 724, 727)

As also pointed out by the Constitutional Court, the constitutional restriction of compliance with the conditions of income and wealth – as laid down in Article 70/I of the Constitution – is a restriction to be enforced in the case of all tax types, the enforcement of which is to be examined by the Constitutional Court individually (case by case) with due account to all the particular features of the concrete tax regulation, especially the provisions on defining the tax base. [Decision 61/2006 (XI. 15.) AB, (hereinafter: CCDec. 2), ABK November 2006, 891, 896]

Examining the constitutionality of the various tax regulations related to "conformity" between the public burden (tax) and the conditions of income and wealth of the subjects obliged to make contribution, the Constitutional Court has already established in several earlier decisions that the obligation to make a contribution to public burdens must be in direct relation to the citizens' (obliged subjects) conditions and status of income and wealth. (Decision 66/B/1992 AB, ABH 1992, 735, 737; Decision 544/B/1998 AB, ABH 2000, 893, 898)

In CCDec.2, the Constitutional Court examined on the basis of Article 70/I of the Constitution the constitutionality of the tax on petty cash, as a supertax of asset type, establishing that the asset-type supertax (public burden) under review was not directly connected to the income and wealth status (conditions) of the obliged subjects, and consequently it failed to comply with the constitutional requirement of proportionate bearing of public burdens. (ABK November 2006, 891, 897.)

When examining the constitutionality of the regulations on the taxation of the free securities of cooperatives in the rules on personal income tax (income taxation), the Constitutional Court pointed out in principle in the reasoning of Decision 3/1993 (II. 4.) AB that "(...) an income actually not obtained by the citizen may not be considered taxable income." (ABH 1993, 41, 45)

In Decision 57/1995 (IX. 15.) AB, (hereinafter: CCDec.3; ABH 1995, 284), the Constitutional Court examined the constitutional questions related to the personal income tax payable upon the so-called company cars used by private individuals.

Upon examining the constitutional questions related to the statutory presumption in the field of the tax regulation, the Constitutional Court established in the reasoning of CCDec.3 the following:

"In the cases when the actual amount of the income cannot be established in general, the legislation may – with account to financial and economic aspects – select various legislative techniques in order to have the extent of the tax payable established. Therefore, it is not unconstitutional in itself if the legislature regulates the economy by levying a flat-rate amount or by setting a statutory presumption.

However, the Constitutional Court points out that in both cases there is a constitutional restriction in the form of the principle laid down in Article 70/I of the Constitution, according to which everyone should only contribute to bearing public burdens in proportion to his/her condition of income and wealth.

It follows from the concept a contestable statutory presumption that the presumption only remains valid until the contrary of it has been proven. (...) A statutory presumption is nothing more than an exceptional tool of simplifying the drafting and the application of statutes.

The exceptional nature of the presumption can also be found in the fact that the State supposes – without complying with the general obligation of producing evidence – the gaining of income and the State imposes a tax on it. The burden of proof is thus turned to the opposite, but, according to Article 70/I of the Constitution, the possibility of proving the falseness of the statutory presumption cannot be excluded. Consequently, as pointed out by the Constitutional Court as a constitutional requirement, the person obliged to pay the tax should have a chance to prove the actual situation.

Therefore, according to the Constitutional Court, the presumption may only be applied in the tax procedure as an exception with additional guarantees, and it may not be the tool of taxing unreal income." (ABH 1995, 284, 285-286)

As in its earlier decisions – partly referred to above – the Constitutional Court reviewed the constitutionality of various tax types and tax regulations on the basis of Article 70/I of the Constitution, the individual decisions assessing the constitutionality of the (concrete) tax regulations were based on different grounds – taking into account all the particular features of the regulations under examination – in respect of judging upon the legislature's compliance with the constitutional restriction laid down in Article 70/I of the Constitution.

In the present case, the Constitutional Court reinforces its position in principle established in CCDec.2, according to which it shall decide whether the regulation remains within the limits of being

bound to the conditions of income and wealth - as specified in Article 70/I of the Constitution - when it examines the concrete provisions of a tax law under constitutional review, assessing it on a case-by-case basis with due account to all features of the regulation, and in particular to the object of the tax.

The Constitution itself does not provide for a definition of "public burdens", but this category includes, beyond doubt, the payments that may be required to be effected to the State under the Act on Public Finance, as sources of revenue for the State, in order to finance the State's economic activities and the operation of its institutions. (Decision 821/B/1990 AB, ABH 1994, 481, 486) Beyond doubt, taxes fall in the category of public burdens and the legislature enjoys a wide range of discretion in the question of determining the object (the economic source) of taxation. Accordingly, the legislature may regulate various tax types, including – among others – income- and asset-type taxes, outlay taxes, turnover-type taxes or excise duties.

In respect of both central and local taxes, the Constitutional Court examined in several earlier decisions the constitutionality of the concrete tax regulations on different tax types, and it judged upon the constitutionality of the rules case-by-case, bearing in mind all the particular features of the regulation concerned.

As underlined by the Constitutional Court in the present case as well, the standard laid down in Article 70/I of the Constitution is to be regarded as a standard equally applicable to all tax types, and when applying the standard due account must be paid to the particular features of the concrete tax regulations and the specific character of the economic source which is the object of the taxation. Consequently, the earlier decisions of the Constitutional Court reviewing – the constitutionality of – concrete tax types by virtue of the standard laid down in Article 70/I of the Constitution, judged upon the compliance with the relevant standard with due account to the particular features of the reviewed tax type and of the economic source as the object of taxation.

For example, based on the standard laid down in Article 70/I of the Constitution, the Constitutional Court evaluated differently the constitutionality of the challenged provisions of the local tax levied – according to the general rules – upon the permanent business activity performed in the territory of jurisdiction of a local government (local business tax) (Decision 122/B/1996 AB, ABH 2002, 737, 742) and of an asset-type supertax (tax on petty cash) examined in CCDec.2. The application of the constitutional standard laid down in Article 70/I of the Constitution leads to different interpretations and constitutional conclusions – with due account to the particular features of the concrete regulations – in the case of the local business tax over the revenues from the business activity – "as a potential source of economy" – permanently performed in the territory of jurisdiction of the local government, and in

the case of income- and asset-type taxes imposed upon the income and the wealth actually gained by the subjects of the tax.

As pointed out by the Constitutional Court, in the case of income- and asset-type taxes – such as corporate tax, which is an income-type tax – the concept of the constitutional standard specified in Article 70/I of the Constitution consists of several components. These elements of the concept are to be deducted from the constitutional provisions of Article 70/I, from the requirements laid down in the earlier decisions of the Constitutional Court – partly referred to in this Decision, too – examining the constitutionality of the income- and asset-type taxes, as well as from the Constitutional Court's practice to be followed. In the case of income- and asset-type taxes, the elements of the concept are the following:

- compliance with the conditions of income and wealth of the subjects of the tax (public burden);
- direct link between the tax and the taxable income or the wealth of the subjects of taxation;
- imposing the tax upon the actually gained income or wealth of the subjects of taxation;
- proportionality between the tax and the burden-bearing capacity of the subjects of taxation.

In the case of income- and asset-type taxes – with due account to all of the particular features of the concrete regulation – all the conceptual elements of the constitutional restriction laid down in Article 70/I of the Constitution must exist at the same time in order to make the reviewed regulation compliant with the relevant constitutional standard.

Accordingly, if the legislature – exercising its wide range of discretion – decides to levy a tax upon the income (profit) gained by or the wealth possessed by the subjects of the taxation, then the reviewed regulations are deemed to be compliant with the constitutional standard laid down in Article 70/I of the Constitution provided that the above conceptual elements are fully complied with, i.e. there is a direct link between the tax and the income or the wealth of the subjects of taxation, the object of the tax is the income or wealth actually (really) obtained by the subjects of the tax, proportionally to the burden-bearing capacity of the subjects of taxation.

When taxing income (profit) or wealth, the constitutional restriction laid down in Article 70/I of the Constitution may become violated if the regulation under review, or any element of it, is considered to impose tax upon an income (profit) not obtained in reality, or similarly when there is no direct link between the taxed income or wealth of the subjects of taxation and the tax (public burden).

5. As held by the Constitutional Court – having regard to the decisions referred to above as well – Section 6 para. (5) of the ACT defines the base of the "expected tax", and thus the "expected tax" itself

to be paid by the subjects of corporate tax, without a direct connection between the tax and the tax subjects' conditions and status of income and wealth."

The tax payment obligation does not depend on the above factors – wherefore it is considered to be disproportionate – as the tax is levied upon an income (profit) not obtained in reality, to be paid by the subjects of corporate tax, required to establish their tax bases according to Section 6 para. (5) of the ACT and to pay the "expected tax" upon the tax base established this way.

The constitutional function of the tax is to secure proportionate contribution to public burdens by the taxpayers obliged to pay the tax. In the course of determining the object of the tax and the tax base – including the amendment of the regulations pertaining to the tax base in the case of a tax regulation already introduced and operating – the legislature enjoys a wide range of discretion.

The restriction laid down in Article 70/I of the Constitution is a constitutional limitation – to be enforced in the case of all tax types – concerning the above-mentioned discretional right of the legislature.

As held by the Constitutional Court, in the case of income- and asset-type taxes, the above constitutional restriction means that the tax base defined in the framework of the concrete tax regulation and the tax payment obligation based on it must be directly linked to the income and wealth conditions and status of the subjects of taxation (taxpayers).

Consequently, if – in the framework of statutory tax regulations already introduced and operating in the field of taxing the profit gained from entrepreneurial activities – the legislature amends (modifies) – for the purpose of increasing the revenues of the budget by way of widening the scope of the subjects of taxation – the existing provisions (pertaining to the tax base based on the pre-tax profit established (corrected) according to the provisions of Act C of 2000 on Accounting [hereinafter: the AA]), then the statutory regulations on the new tax base (and the resulting tax payment obligation) – within the regulation of the income-type tax imposed upon the profit – must be directly linked to the income and wealth conditions and status of the taxpayers.

In the assessment of the present case, the Constitutional Court has taken account of Section 6 para. (1) of the ACT, according to which the tax base is the actual income (revenue) obtained by the tax subjects, resulting from an economic activity (entrepreneurial activity) aimed at, or resulting in, gaining income or wealth: this is the tax base forming the basis of the taxpayers' obligation of tax payment. The mere fact that by Section 21 of the AAF – effective as from 1 January 2007 – the legislature has amended the normative text of the Principles of the ACT regulated in Section 1 para. (1) does not change - regarding the establishment of the base for the reviewed tax-type levied upon the profit - Section 6 para. (1), ordering the tax payment obligation to cover the profit gained and actually obtained

from the entrepreneurial activity, and similarly it remains unchanged that the legislature has introduced the new tax base related to the corrected and amended revenues as laid down in the challenged Section 6 para. (5) within the tax law regulations operating in the framework of an income-type tax payable upon profit.

Consequently, in the case of the reviewed tax imposed upon an income (revenue) gained from entrepreneurial activity – similarly to the asset-type tax examined in CCDec.2 – the Constitutional Court has to verify the existence of a direct connection between the tax and the income (profit) gained by the tax subject in the course of the entrepreneurial activity, with due account to the constitutional restriction under Article 70/I of the Constitution (compliance with the conditions of income and wealth).

When defining the tax base in Section 6 para. (5) of the ACT, the aim of the legislation was to improve the balance of state finances by widening the scope of subjects obliged to pay corporate tax – through the definition of the tax base.

In order to achieve this legitimate legislative objective – without taking into account the above-mentioned constitutional restriction – the legislature has ordered – with a few exceptions – all subjects of the corporate tax to pay tax upon a "minimum" level of "expected" income (profit) determined unilaterally by the legislature. The "minimum" level of "expected income" that forms the basis of the "expected tax" as required by the legislature is a so-called "expected" amount since it is not obtained in reality by the subjects of taxation.

Under Section 6 para. (1) of the ACT, with regard to the establishment of the corporate tax base, the basis of corporate tax is, in the case of domestic taxpayers and foreign entrepreneurs, the pre-tax revenue, corrected with the items increasing or decreasing the tax base as regulated in the relevant provisions of the ACT (Sections 7, 8, 16, 18, and 28) and amended according to the provisions in Chapter VII of the ACT.

Under Section 8 para. (1) of the AACF, the above statutory provision on the establishment of the tax base has been supplemented with the definition of the base of the "expected tax" as from 1 January 2007 [Section 6 para. (5) of the ACT].

As Section 6 para. (5) of the ACT does not define the tax base on the basis of the taxpayer's (corrected) pre-tax revenues – in accordance with the provisions of the AA – but on the ground of the total amount of revenues collected by the taxpayer in the tax year, this regulation does not reflect the taxpayer's real conditions of income or wealth and it is not connected at all to the taxpayer's income (profit) gained from entrepreneurial activity.

Under Section 6 para. (5) of the ACT, the loss-making enterprises under the scope of the ACT – having a negative corrected pre-tax result – must pay the ”expected tax” even upon the negative tax base (loss).

This is because there is some turnover necessarily resulting from the entrepreneurial activity of operating but loss-making enterprises, and the 2% level of the corrected amount of that turnover would in each case exceed the negative tax base mentioned above. Consequently, the loss-making taxpayers must pay the “expected tax” (“minimum” tax) despite having a negative (corrected) pre-tax result “reflecting” their actual conditions of income and wealth (as their performance in the relevant tax year), i.e. the after tax results (losses) actually gained in the tax year does not cover this.

[The Constitutional Court notes that prior to putting into force as from 1 January 2007 the statutory provision on the “expected tax base” regulated in Section 6 para. (5) of the ACT, the taxpayers with a negative tax base established under Section 6 para. (1) of the ACT had not been obliged to pay corporate tax.]

Regarding the enforcement of the constitutional restriction laid down in Article 70/I of the Constitution, a constitutional concern similar to the one connected to the loss-making enterprises is raised about the definition of the tax base under Section 6 para. (5) of the ACT in the case of the taxpayers having a positive (corrected) pre-tax result according to the AA if its level is lower than 2% of the total amount of corrected revenues in the tax year.

Even those taxpayers pay the corporate tax upon the base of the “expected tax”, i.e. in their case, too, the taxation is not based on their performance (results) – reflected in their conditions of income and wealth – but on an income (result) defined by the legislature but not obtained by the taxpayer in reality.

In the case under review, in addition to the income (profit) gained from the entrepreneurial activity according to Section 6 para. (5) and Section 1 para. (1) of the ACT – under certain statutory conditions – the legislature ordered tax payment obligation upon the corrected and amended total revenues in the tax year resulting from the above activity, this way not only widening the scope of the tax subjects obliged to pay tax but at the same time imposing a tax payment obligation upon a revenue which is completely different from the income (profit) obtained from the entrepreneurial activity to be taxed according to the law.

Consequently, the tax base specified in Section 6 para. (5) of the ACT creates a tax payment obligation irrespectively of the income (profit) obtained through the entrepreneurial activity – i.e. without regard to the actual income conditions (the profits from the entrepreneurial activity) of the subjects of taxation – within the examined tax type originally destined to levy the tax upon the profit.

The challenged regulation of the ACT is at the same time an incontestable statutory presumption set by the legislature in respect of which the taxpayers bound to pay the “expected tax” may not present any counter-evidence and they may not state and verify that they have not actually obtained the income (result) that forms the basis of the “expected tax” presumed by the legislature and that their actual profit (income) gained from the entrepreneurial activity does not cover the payment of the “expected tax”.

As held by the Constitutional Court, in the present case, the legislature has set an incontestable statutory presumption as the general rule by way of determining a new tax base (together with the “expected tax” based on it) in a regulation of substantive tax law by totally neglecting the guarantee regulations specified in the constitutional requirement found in CCDec.3.

In the opinion of the Constitutional Court, the constitutional requirements specified in CCDec.3 must be enforced not only in respect of the regulations on taxation procedure but also in the case of substantive tax laws. Accordingly, if the legislature sets a statutory presumption when regulating substantive tax law, then the taxpayer must be allowed to present counter-evidence against the statutory presumption (in order to have the statutory presumption contested). In the case under review, the legislature has established an incontestable statutory presumption within the operating tax law regulations of income-tax type (tax on profit), among the rules of substantive law about the definition of the tax base. According to the incontestable statutory presumption mentioned above, the taxpayer has to pay the “tax expected” by the legislature as a kind of “minimum tax” on the basis of the entrepreneurial activity aimed at gaining profit as the sole ground of paying the tax.

Based on this presumption, the taxpayers who make profit but have a tax base which is actually less than the tax base of the “expected tax” have no chance to present counter-evidence and they have to pay the tax not upon the real profit but on the basis of a presumed “expected profit resulting from a potential source of economy” never realized by the taxpayer in reality, irrespectively of the actual result of the entrepreneurial activity performed in the tax year – i.e. the tax base established on the basis of Section 6 para. (1) of the ACT and to be verified in the course of tax supervision.

In the regulatory system of the income-type tax under review, the incontestable statutory presumption regulating the “expected tax” – based on the performed activity as a “potential source of economy” not linked to the profit actually made verifiably according to the records at the subjects of the tax – is not an exceptional rule of legal technique to simplify the application of the law, allowing the tax subject to prove the contrary, the existence of which could be justified by the “general incapacity to establish” the level of the profit to be taxed under the ACT.

Based on the above arguments, the Constitutional Court has established that the “expected tax base” and the “expected tax” based on it, as specified in Section 6 para. (5) of the ACT and in force as of 1

January 2007, is not directly connected to the taxpayers' conditions/status of income and wealth and it imposes tax upon an income (profit) not obtained in practice, which is against the constitutional principle of the proportionate bearing of public burdens as determined under Article 70/I of the Constitution.

The Constitutional Court emphasizes that in the case concerned, it does not take a position in the theoretical constitutional question of whether or not it is constitutional – without regard to the particular features of the concrete regulation – to levy tax on the revenues resulting from the entrepreneurial activity performed, as a potential source of economy. The Constitutional Court has examined whether or not – within the operating tax law regulations related to the income-type tax (on profit) – the (newly regulated) concrete statutory provision under Section 6 para. (5) of the ACT about the establishment of the tax base complies with the constitutional standard mentioned in the present Decision and regulated in Article 70/I of the Constitution, as applicable to income- and asset-type taxes.

The Constitutional Court has established the unconstitutionality of the concrete regulatory method chosen by the legislature in Section 6 para. (5) of the ACT, with due account to all of the particular features of the examined tax law regulation – in particular the tax type of the income-type tax (tax upon profit) and the object of the tax – also paying attention to the fact that the definition of the challenged tax base is regulated within the existing rules on an income-type tax already in operation.

For the purpose of putting right the balance of the budget, the legislature may decide freely in choosing the public burden to be used as the basis of increasing the revenues of the budget. If the legislature chooses taxation as the source of increasing the revenues of the budget, it has to take account of the constitutional restriction under Article 70/I of the Constitution even in the case of amending the tax regulations of income and asset types, already introduced and being in operation, and it has to pay attention to all the particular features of the regulation (the tax type) already introduced and being in operation, in particular the taxable economic source and the definition of the tax base under the relevant regulation. In view of the above, the Constitutional Court has annulled the unconstitutional statutory provision as of the day of promulgation of this Decision as laid down in point 1 of the holdings.

6. Section 6 para. (6) of the ACT also challenged by the petitioners, providing for exceptions from the application of the provisions in paragraph (5), as well as paragraphs (7) and (8) regulating the correction factors mentioned in Section 6 para. (5) of the ACT have contents closely connected to the unconstitutional statutory provisions. Section 6 para. (9) of the ACT challenged by the petitioners and annulled in point 1 of the holdings provides for a definition of the natural disaster damage mentioned in

Section 6 para. (6) of the ACT, together with provisions about verifying such damage, and consequently, its contents are closely connected to Section 6 para. (6) of the ACT.

With regard to their close connection of substance and taking account of the fact that by the annulment of Section 6 para. (5) of the ACT, the above-mentioned provisions of the ACT have been emptied, the Constitutional Court has also annulled Section 6 paras (6), (7), (8), and (9) of the ACT, as laid down in point 1 of the holdings, based on the same reasoning and with the same effect in time as detailed in respect of Section 6 para. (5) of the ACT.

7. Under Section 225 para. (16) of the AAF, if the taxpayer is to declare an advance on tax on the basis of the tax payable for the year 2006, then the amount of the advance shall be calculated by taking into account the provisions under Section 6 paras (5) and (6) of the ACT in force as of 1 January 2007.

As the Constitutional Court has annulled in point 1 of the holdings Section 6 paras (5) to (8) of the ACT, the provision in Section 225 para. (16) of the AAF contains a meaningless statutory reference to determining the advance on tax for the "expected tax" and to the related exemptions – referring back to the annulled Section 6 paras (5) and (6) of the ACT. Based on the close connection of substance with the annulled Section 6 paras (5) and (6) of the ACT, and with account to the emptying of the normative content of the challenged provision according to point 2 of the holdings, the Constitutional Court has annulled the statutory provision under Section 225 para. (16) of the AAF, with the same force in time as the above-mentioned statutory provisions.

8. As the Constitutional Court has established the unconstitutionality of the statutory provisions specified in the holdings on the ground of Article 70/I of the Constitution, the Constitutional Court – acting in line with its established practice – has not performed any further review of unconstitutionality with regard to other constitutional provisions [Article 2 para. (1) and Article 70/A para. (1) of the Constitution] referred to in the petitions. [Decision 61/1997 (XI. 19.) AB, ABH 1997, 361, 364; Decision 16/2000 (V. 24.) AB, ABH 2000, 425, 429; Decision 56/2001 (XI. 29.) AB, ABH 2001, 478, 482; Decision 35/2002 (VII. 19.) AB, ABH 2002, 199, 213; Decision 4/2004. (II. 20.) AB, ABH 2004, 66, 72; Decision 9/2005 (III. 31.) AB, ABH 2005, 627, 636]

In view of the above, the Constitutional Court has decided as contained in the holdings of the Decision.

The publication of the Decision is based on Section 41 of the ACC.

Budapest, 27 February 2007.

Dr. Mihály Bihari
President of the Constitutional Court
Judge of the Constitutional Court, Rapporteur

Dr. Elemér Balogh
Judge of the Constitutional Court

Dr. András Bragyova
Judge of the Constitutional Court

Dr. Mihály Bihari
President of the Constitutional Court
on behalf of
Dr. Árpád Erdei
Judge of the Constitutional Court, prevented from signing

Dr. Attila Harmathy
Judge of the Constitutional Court

Dr. András Holló
Judge of the Constitutional Court

Dr. László Kiss
Judge of the Constitutional Court

Dr. Péter Kovács
Judge of the Constitutional Court

Dr. Péter Paczolay
Judge of the Constitutional Court

Concurrent reasoning by Dr. László Kiss, Judge of the Constitutional Court

1. I agree with the provisions contained in points 1 and 2 of the majority Decision, according to which the Constitutional Court has established that Section 6 paras (5) to (9) of Act LXXXI of 1996 on Corporate Tax and Dividend Tax as well as Section 225 para. (16) of Act LXI of 2006 on the Amendment of Certain Acts on Financial Subjects are unconstitutional and, therefore, annulled them as of the date of promulgation of the majority Decision.

However, I would have focused the reasoning on the fact that in the case of the challenged provisions, the constitutional requirement laid down in Decision 57/1995 (IX. 15.) AB has not been enforced, as according to it the taxpayer should have been offered a chance to prove the actual situation. (ABH 1995, 284, 286) As I see it, in this case [just like in the case of Decision 57/1995 (IX.15.) AB], this would be the guarantee of enforcing the principle laid down in Article 70/I of the Constitution. The decision referred to above contains other important statements related to judging upon the present case. For example, “The exceptional nature of the presumption lies in the fact that the State supposes – without complying with the general obligation of producing evidence – the gaining of

income and the State imposes a tax on it. The burden of proof is thus turned to the opposite, but, according to Article 70/I of the Constitution, the possibility of proving the falseness of the statutory presumption cannot be excluded. Consequently, as pointed out by the Constitutional Court as a constitutional requirement, the person obliged to pay the tax should have a chance to prove the actual situation.

Therefore, according to the Constitutional Court, the presumption may only be applied in the tax procedure as an exception with additional guarantees, and it may not be the tool of taxing unreal income." (ABH 1995, 286)

In the present case, the legislature has failed to guarantee for the taxpayer the conditions for proving the real situation. However, in the absence of proving the contrary the State might impose the tax payment obligation upon an income (profit) not obtained in reality, and similarly it might happen that there is no direct connection between the tax (public burden) and the taxable income or wealth of the tax subject.

Thus, I would have focused on the application of an incontestable presumption depriving the obliged taxpayers even of the chance of proving that in their case, the "expected tax" did really fall far from the requirement (requisite or condition) under Article 70/I of the Constitution. Accordingly, I share the views expressed in the majority opinion as follows: "In the regulatory system of the income-type tax under review, the incontestable statutory presumption regulating the »expected tax« – based on the performed activity as a »potential source of economy« not linked to the profit actually made verifiably according to the records at the subjects of the tax – is not an exceptional rule of legal technique to simplify the application of the law, allowing the tax subject to prove the contrary, the existence of which could be justified by the »general incapacity to establish« the level of the profit to be taxed under the ACT."

2. At the same time, it is to be stressed that no constitutional concern may be raised against the government's objective stating the following: "Today, a significant part of the enterprises pretend to make loss through many years, fully withdrawing themselves from the obligation of paying corporate tax. In the future, all tax subjects bound to pay corporate tax must pay the corporate tax upon a minimum level of profit economically expected for sustaining the enterprise." However, the constitutionally acceptable aim can only be achieved through constitutionally acceptable means and methods. Nevertheless, it is not constitutionally acceptable to allow the legislature to deprive the obliged person of the possibility of proving that in his case there is no ground to maintain the presumption upon which the government's objective is based.

The present method – institutionalizing the incontestable presumption – has an undifferentiated effect, not allowing a chance to find out who are the ones considering it worthwhile to maintain their loss-making enterprises throughout the years, and who are the ones verifiably hiding their income. In the absence of such an investigation, the State chooses a simpler legal technique as the solution, applying the general rule of "everyone lies and everyone is fraudulent".

Budapest, 27 February 2007

Dr. László Kiss

Judge of the Constitutional Court

Dissenting opinion by Dr. András Holló, Judge of the Constitutional Court

I do not agree with the holdings and the reasoning of the majority Decision.

1. For the past 17 years, the Constitutional Court's practice related to tax law has been based on the principle that in a constitutional State the definition of the budget's sources of revenue is the competence of the Parliament, while the Government is responsible for forming the economic policy. The Constitutional Court may not take over the responsibility of the Parliament or of the Government for forming the budgetary policy. Therefore, the Constitutional Court's practice related to examining the constitutionality of tax laws was characterized by the interpretation of its scope of competence in a strict sense.

The interpretation of Article 70/I of the Constitution has consistently rested upon the Constitution's neutrality concerning economic policy. As consistently stressed by the Constitutional Court when interpreting Article 70/I of the Constitution in line with the Constitution's neutrality concerning economic policy, the legislation has a wide range of constitutional discretion by virtue of Article 70/I in adopting tax laws. The Constitutional Court has explained in its decisions that due to the Constitution's neutrality concerning economic policy, the legislative decisions on regulating tax laws allow only limited possibilities for reviewing the discretionary decisions. Determining the economic policy – including the supporting of certain activities and encouraging or discouraging of investments – is, in itself, not a constitutional issue. It becomes a constitutional concern, however, when the concrete statutory regulations implementing the economic policy violate a constitutional right or they are of discriminative nature. [Decision 620/B/1992 AB, ABH 1994, 542, Decision 59/1995 (X. 6.) AB, ABH 1995, 300; Decision 963/B/1993 AB, ABH 1996, 440; Decision 26/2004. (VII. 7.) AB, ABH 2004, 398, 429, Decision 333/B/2000 AB, ABK September 2006, 682, 485]

Under Article 70/I of the Constitution, the obligation of bearing public burdens is a fundamental obligation according to which all natural persons, legal persons and unincorporated organizations must contribute to public burdens on the basis of their income and wealth. This is the constitutional basis of the State's right to levy taxes, and the only restriction set in Article 70/I of the Constitution in respect of this right is to make the public burden bearing obligation compliant with the obliged person's conditions of income and wealth. Of course, the Constitutional Court also requires compliance with other constitutional requirements as well, originating not from Article 70/I but from the Constitution's provisions on the fundamental rights, interpreting the requirements of the rule of law and of equal rights with regard to tax law.

In my dissenting opinion attached to Decision 61/2006 (XI. 15.) AB (ABK November 2006, 891, 900-902), I analyzed the Constitutional Court's practice developed for the interpretation of Article 70/I of the Constitution in the course of exercising normative control over the tax laws. According to this analysis, the Constitutional Court interpreted Article 70/I of the Constitution as the representation of the principle of the proportionate sharing of public burdens, and therefore the obliged person's load-bearing capacity was the basis of the Constitutional Court's assessment. As consistently held by the Constitutional Court in respect of defining the source of the obligation to bear public burdens, Article 70/I of the Constitution does not specify the titles under which the State may provide for payment obligations, and therefore the legislator has a wide scale of discretion in choosing various economic resources as the basis of sharing public burdens, and, accordingly, in determining the objects of public burdens.

With regard to income- and asset-type taxes, the Decision deducts from Article 70/I of the Constitution constitutional requirements that fall beyond the conditions elaborated in the practice of the Constitutional Court, modifying the Constitutional Court's role in examining tax laws. In my opinion, the constitutional standard and the deducted consequences of principle (incorporating into the constitutional standard the concept of actually obtained income – which cannot be clearly interpreted in the tax law – and interpreting the direct connection between the tax and the taxpayer's conditions of income and wealth) bear a risk of washing away the borders between the constitutional assessment of tax laws and their evaluation under economic policy.

2. According to the Decision, establishing the unconstitutionality of the examined regulations is based upon the alleged violation of the constitutional restriction laid down in Article 70/I of the Constitution, due to defining the tax base of the income-type corporate tax on the ground of the turnover, by way of imposing a tax payment obligation upon a profit not obtained in reality, and thus

the “expected tax” is not connected directly to the conditions of income and wealth of the subjects of corporate tax.

I can accept the starting point of the Decision, stating that when examining the collision between the tax laws and Article 70/I of the Constitution and when assessing the proportionality the tax burden, due attention must be paid to the position and the role of the tax type in the system of taxation. The proportionality of sharing public burdens may be impaired if the legislature fails to take into account the particular features of the given tax type when defining the tax regulations. In fact, this was the basis of the Constitutional Court establishing the violation of Article 70/I by certain tax law provisions in the case of income-type taxes. [Decision 3/1993 (II. 4.) AB, ABH 1993, 41, 45; Decision 57/1995 (IX. 15.) AB, ABH 1995, 284, 286; Decision 5/1997 (II. 7.) AB, ABH 1997, 55, 62; Decision 31/1998 (VI. 25.) AB, ABH 1998, 240, 249-250]

However, the tax regulations reviewed in the petition are of a different nature. In the case under examination, the legislature modified the system of corporate taxation. Section 21 of the AAF amended Section 1 para. (1) of the ACT, thus changing the economic source selected as the ground of corporate taxation. Under Section 1 para. (1) of the ACT in force, the economic source of the tax is not the income resulting from the enterprise but the entrepreneurial activity itself. At the same time, Section 6 paras (5) to (9) of the ACT, as introduced by Section 25 of the AAF and Section 8 of the AACF, created a *sui generis* tax form differing from the general rules on the corporate tax in respect of the tax subjects, the object and the basis of the tax as well as the rules on tax exemptions. This has resulted in the introduction of a “minimum tax”, extending the obligation of bearing public burdens also to the companies where the pre-tax revenue is lower than 2% of the net turnover.

Therefore, in my opinion, during the assessment of the constitutionality of the rules on the “minimum tax”, the constitutional problem is raised not in the form set out in the Decision – i.e. whether the basis of the income-type corporate tax can be determined on the basis of the revenue – but the question to be answered on the ground of Article 70/I of the Constitution is whether the turnover can be a constitutional object of taxation, and whether or not the tax regulated in Section 6 paras (5) to (9) of the ACT impairs the requirement on the proportionality of bearing public burdens.

In Decision 122/B/1996 AB, the Constitutional Court did not establish the unconstitutionality of taxing the net turnover resulting from the entrepreneurial activity when reviewing the constitutionality of the rules on the basis of the local business tax. (ABH 2002, 737)

The tax payment obligation of 16% upon 2% of the net turnover – in particular when taking into account the preferences, exemptions and the option of deferring losses as regulated under Section 6

para. (6) of the ACT – may not be regarded as a disproportionate tax burden unconstitutionally burdening the capacity of the tax subjects.

Therefore, in my opinion the unconstitutionality of the challenged provisions may not be established on the basis of Article 70/I of the Constitution.

Budapest, 27 February 2007

Dr. András Holló

Judge of the Constitutional Court

Dissenting opinion by Dr. András Bragyova, Judge of the Constitutional Court

I agree with the dissenting opinion delivered by Dr. András Holló, Judge of the Constitutional Court.

Without repeating my dissenting opinion attached to the decision on the tax on petty cash [Decision 61/2006 (XI. 15.) AB, ABK November 2006, 891], I find it necessary to add the following.

Having regard to the Decision, it is particularly important to define the meaning of income – to be more specific, taxable income – as according to the majority Decision, in the case of an income tax, only the taxing of the actually obtained income may be held constitutional. Undoubtedly, an income tax may only levy tax upon an income. However, the correctness of this statement depends on the constitutional concept rather than on the tax law definition of income.

The majority Decision considers the concept of income to be the clear or net income, and this is regarded as the income the tax is based upon within the meaning under Article 70/I of the Constitution. However, it does not follow obviously at all from the Constitution. The constitutional concept of taxable income does not necessarily correspond to the income concept represented in the earlier statutes on corporate tax. Therefore, one should act vice-versa, i.e. the constitutional concept of income should not be identified with the income concept represented in the earlier corporate tax laws – or other tax laws – and the content of the income concept applied in Article 70/I of the Constitution should be defined irrespectively of the above concepts. Indeed, this is all the more justified as the income concept in the specific tax laws is always the result of a legal construction, and most of the time it may not be identified with a specific economic terminology such as for example gain or profit etc.

Serious arguments support the view that in the terms of bearing public burdens all revenues (or equivalent takeover of expenditure or bearing expenses) disposable by the tax subject can be regarded as income. Its constitutional reason is the following: income in the sense of revenue is a part of "wealth" mentioned together with income in the wide sense in Article 70/I of the Constitutional Court. All the revenues and wealth of the tax subject are identical with the economic assets over which the tax

subject enjoys a certain disposing right. Under Article 70/I of the Constitution, the legislature shall define in proportion to the above the level of the pecuniary payment obligations – in particular the tax payment obligation – to cover the State's revenues necessary for bearing public burdens – i.e. by taking into account the load-bearing capacity of the tax subject. It is reasonable to presume that a higher volume of total income – i.e. total revenues – implies a bigger capacity of bearing public burdens, since with a higher volume of revenues the tax subject may dispose over more economic resources. According to the primary principle of equitable sharing of public burdens – the fairness of taxation – the bigger one's economic power is – reflected in the volume of income and wealth – the more public burdens it can bear.

Therefore, I do not see any reason to hold it unconstitutional to establish the taxable income on the basis of all the revenues of the tax subject. According to the regulation claimed by the majority Decision to be unconstitutional, the starting point is the total revenues of the tax subject, then – as done in Section 6 paras (5) to (8) of the ACT – it is corrected with the items increasing or decreasing the amount of revenues, moreover, upon the compliance with certain conditions, the tax subject is exempted from paying the expected tax. The tax amount of HUF 3,200 to be paid upon one million forints of net turnover in accordance with the ACT can hardly be regarded as an unconstitutionally excessive one.

One should note that Act CXVI of 1995 on Personal Income Tax, as the fundamental Act of income taxation in Hungary, uses a principle which is the opposite of the one applied in the ACT. Under Section 4 para. (1) of this Act, "Income shall mean the totality of the revenues gained by the private individual in the tax year under any title and in any form, or the part of it remaining after decreasing it with the deductibles acknowledged in this Act, or the proportion of it as determined in this Act." Accordingly, under personal income taxation, income means all the revenues of the taxpayer – allowing the deduction of certain costs acknowledged by the law.

In this case, the income concept of the Act of Parliament differs significantly from the income concept applied in the ACT, still it can hardly be considered unconstitutional.

Budapest, 27 February 2007

Dr. András Bragyova
Judge of the Constitutional Court

Constitutional Court file number: 670/B/2006

Published in the Official Gazette (*Magyar Közlöny*) MK 2007/23