

# Hungarian Energy Market

## Details published of windfall taxes and tax increases affecting the energy sector

June 2022

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### Key takeaways

- The Hungarian Government adopted and published the detailed rules of the new windfall taxes and other related amendments affecting the energy sector.
- The special tax will primarily affect petroleum product manufacturers, power plants producing electricity from renewable energy sources, waste or by using cogeneration, and those liable to pay the energy suppliers' income tax (Robin Hood tax).
- The pertinent provisions of the government decree will enter into force on 1 July 2022.
- The tax rate is 25% for petroleum product manufacturers and 65% for power producers.
- The taxation of the spread between Brent and Ural oils by introducing the special tax on petroleum product manufacturers and the new obligation of companies producing bioethanol, biofuels and other similar downstream products to pay Robin Hood tax are expected to primarily affect the state oil company, MOL. More than 80% of the tax income is projected to come from these funds.
- The special tax on power producers does not apply to all projects receiving state subsidies, but only to those that have left or will leave the mandatory offtake or support price provided by the KÁT or METÁR system in 2022 or 2023. The possibility to do so has already been significantly reduced by legislative measures in the past weeks. This is now complemented by the fact that, in addition to leaving the KÁT and METÁR schemes, those who do not "enter" these schemes in the first place (i.e., do not conclude the contracts necessary to qualify for the mandatory offtake or support price) even though they are eligible for the state subsidy are also penalised by the payment of the new special tax.
- There are considerable uncertainties about the new rules: it is not clear whether the 0.5 MW size limit should be considered per KÁT or METÁR decision, per generation license or per project (aggregation), and the producers concerned will have to self-assess, declare and pay the special tax due for each month of the period between 1 January 2022 and the date of entry into force of the special tax, i.e., 1 July 2022, by 20 September 2022 (retroactivity).
- Overall, it will be very difficult or almost impossible for KÁT and METÁR producers to take advantage of high market prices in the future. At the same time, it is clear that the government is not counting on the abolition of the Robin Hood tax, which has long been a painful issue for the energy sector. However, the spread of consumer-centred corporate PPAs and onsite power generation project may gain ground.

## 1 Background

As expected, the Government of Hungary adopted and published in the National Gazette on 4 June 2022 **the detailed rules of the new windfall taxes and other related amendments affecting the energy sector** (see Government Decree No. 197/2022 (4.VI.) in the National Gazette No. 2022/93).

The government has justified the introduction of the special tax regime, which covers 8 sectors in total (energy, banks, insurance, retail, pharmaceuticals, telecoms, airlines, and advertising), by the need to balance the budget, which it expects to generate HUF 815 billion (EUR 2.06 billion) in additional revenue this year, of which HUF 300 billion (EUR 760 million) will come from the energy sector. The cabinet expects an additional HUF 100 billion (EUR 250 million) to be raised from other public charges that are not special taxes (i.e., company car tax, public health product tax). The government's top priority is to use the increased public revenues to finance the current and expected future substantial costs of public services provided at limited utility prices set by law (in Hungarian: *rezsicsökkentés*) and military developments.

From the energy sector's perspective, the special tax will primarily affect petroleum product manufacturers, power plants producing electricity from renewable energy sources, waste or by using cogeneration, and those liable to pay the energy suppliers' income tax (Robin Hood tax), as described below.

Most of the government decree will enter into force on **1 July 2022**, except for e.g., the rules on mining royalties, which will apply from 1 August 2022.

## 2 Special tax on petroleum product manufacturers

According to the Government Decree, petroleum product manufacturers are obliged to assess, declare and pay the extra profit tax for the tax years 2022 and 2023 by self-assessment.

The special tax is based on the price difference between the world market price of crude oil originating in the Russian Federation calculated in line with the Government Decree, and the quantity of crude oil in barrels originating in the Russian Federation purchased during the reference month. For the purposes of the Government Decree, "price difference between the world market price of crude oil" shall mean the difference between the arithmetic average of the daily quotations of Platts Crude Oil Marketwire Brent (Platts Dated Brent-PCAAS0) Mid values (US dollars/barrel) for the reference month and the arithmetic average of the monthly purchase prices per barrel of crude oil originating in the Russian Federation for the reference month, if positive, with the obligation for petroleum product manufacturers to use the official average monthly US dollar exchange rate of the Hungarian National Bank for the calculation of the tax liability. The purchase price is the invoiced purchase price in US dollars, which cannot be reduced by any additional purchase costs.

**The special tax rate is 25%.**

Petroleum product manufacturers are obliged to assess, declare (on a special form provided by the National Tax Authority for this purpose) and pay the special tax on a monthly basis by the 20th day of the month following the reference month. These obligations must be fulfilled by petroleum product manufacturers for the first time for the full tax year beginning after 31 December 2021 and including 1 July 2022. Petroleum product manufacturers must establish, declare and pay the special tax due for each month of the period from 1 January 2022 to 1 July 2022 by 20 September 2022.

## 3 Special tax on certain power producers

The following generators with an installed capacity exceeding 0.5 MW are subject to the self-assessment, declaration and payment of the special tax on electricity generators:

- a) producers eligible for the mandatory offtake of the electricity they generate under Government Decree No. 389/2007 (XII. 23.) of Hungary (KÁT Decree), if the balancing group membership or premium support

contract of the given producer terminates in the tax year 2022 or 2023, or if the given producer starts its commercial operation in the tax year 2022 or 2023, but does not conclude a balancing group membership or premium support contract;

- b) producers eligible for the mandatory offtake of the electricity they generate under Government Decree No. 299/2017 (X. 17.) of Hungary (METÁR Decree, and such mandatory offtake is the METÁR-KÁT), if the balancing group membership or premium support contract of the given producer terminates in the tax year 2022 or 2023, or if the given producer starts its commercial operation in the tax year 2022 or 2023, but does not conclude a balancing group membership or premium support contract;
- c) producers eligible for green premium under the METÁR Decree, if the given producer's contract for green premium expires in the tax year 2022 or 2023 or if the given producer starts its commercial operation in the tax year 2022 or 2023 but does not conclude a premium support contract.

However, KÁT producers are exempt from the special tax for electricity produced from solid biomass.

The basis of the special tax varies according to the different types of taxable entities:

- a) in the case of KÁT, producers without a balancing group membership or premium support contract with the transmission system operator, the positive amount of the revenue after the quantity of electricity injected into the electricity network by the generator in the reference month, minus the quantity of electricity injected into the electricity network in the reference month multiplied by the mandatory offtake price or support price applicable for the reference year, as determined by the Hungarian Energy and Public Utility Regulatory Authority (HEPURA);
- b) in the case of a METÁR-KÁT, producers without a balancing group membership or premium support contract with the transmission system operator, the positive amount of the revenue after the quantity of electricity injected into the electricity network by the generator in the reference month, minus the quantity of electricity injected into the electricity network in the reference month multiplied by the mandatory offtake price or support price applicable for the reference year, as determined by the HEPURA;
- c) in the case of METÁR, producers eligible for green premium without a support contract concluded with the transmission system operator pursuant to its business code, the positive amount of the sales price set in the power trading contract concluded by the generator, minus the support price for the reference year multiplied by the amount of electricity injected into the electricity network by the generator during the reference month.

For KÁT and METÁR-KÁT producers, the mandatory offtake price shall be the price set out in the final decision of the HEPURA establishing the entitlement to KÁT or METÁR-KÁT.

#### **The special tax rate is 65%.**

Power producers are obliged to assess, declare (on a special form provided by the National Tax Authority) and pay the special tax on a monthly basis by the 20th day of the month following the reference month. Power producers must fulfil these obligations for the first time on the day following the date of termination of the contract for balancing group membership, premium support or green premium or, in the case of producers who start trading but do not conclude a contract for balancing group membership, premium support or green premium, for the entire tax year in which the commercial operation starts, but not earlier than the tax year beginning in 2022 and not later than the full tax year that includes 31 December 2023. Power producers must self-assess, declare and pay the special tax due for each month of the period from 1 January 2022 to 1 July 2022 by 20 September 2022.

## 4 Changes affecting the Robin Hood tax

Notwithstanding Act No. LXVII of 2008 on making district heating more competitive, for the tax years 2022 and 2023, manufacturing producers will also be subject to the special income tax of energy suppliers (Robin Hood tax). "Manufacturing producers" mean enterprises producing bioethanol, starch and starch products and sunflower oil.

Manufacturing producers must determine the tax advance payable for the 2022 tax year by self-assessment, declare it by 20 September 2022 (on a special form provided by the National Tax Authority) and pay it in equal monthly instalments by the 20th of each month, starting from 20 September 2022. The tax advances payable for the tax year 2023 must also be determined by self-assessment, declared by 20 January 2023 (on a separate form provided by the National Tax Authority) and paid in equal monthly instalments by the 20th day of each month. These obligations must be fulfilled for the first time by manufacturing producers for the full tax year starting after 31 December 2021 and including 1 July 2022.

## 5 Expected market impacts

The taxation of the spread between Brent and Ural oils by introducing the special tax on petroleum product manufacturers and the new obligation of companies producing bioethanol, biofuels and other similar downstream products to pay Robin Hood tax are expected to primarily affect the state oil company MOL Magyar Olaj- és Gázipari Nyrt. In total, the government expects to raise HUF 250 billion (EUR 630 million) from these funds, which is more than 80% of the total tax burden on the energy sector. Regardless of this, other domestic petroleum product manufacturers and manufacturing producers will of course also be affected by the new tax burden, and their market presence is not negligible.

As regards the special tax on power producers, it should be stressed that it does not apply to all projects receiving state subsidies, but only to those that have left or will leave the mandatory offtake or support price provided by the KÁT or METÁR system in 2022 or 2023. This possibility has already been significantly reduced following legislative actions in recent weeks, given that as of 25 May 2022, KÁT producers will only be entitled to join a different balancing group instead of the KÁT balancing group if they opt for the application of the premium support regime under the METÁR Decree instead of the support under the mandatory off-take system, with no possibility to withdraw; while the premium support contract cannot be terminated by the generator until the end of the support period or until the total amount of electricity subject to support has been settled (whichever is earlier). This is now complemented by the new rules, partly by imposing a special tax on producers leaving the KÁT and METÁR schemes, and partly by penalising, in addition to leaving the KÁT and METÁR schemes, those who do not "enter" these schemes in the first place (i.e., do not conclude the contracts necessary to qualify for the mandatory offtake or support price), even though they are eligible for the state subsidy.

From the above, it is easy to see that in the future it will be even less attractive than before to opt for free market electricity sales instead of the KÁT and METÁR systems, as far as this is of course possible at all. The legislative steps taken in recent weeks and the new special tax are likely to encourage generators eligible for the KÁT, METÁR-KÁT or green premium to remain in the support schemes. Some movement is expected only from the KÁT system in the direction of the METÁR regime, however, in this case generators will have to face the risk of paying the difference between the premium support and the market price to the transmission system operator in case of high free market electricity prices, and the risk of having to use third parties (balance responsible parties) to balance their production and thus to conclude the balancing group contract themselves.

In addition, the spread of power purchase agreements (PPAs), which are intended to replace the KÁT and METÁR systems as financing structures in the long term, may slow down and be limited to the user side (corporate PPAs), instead of producer-centric structures, i.e., industrial users (such as office buildings, factories) may become the

main initiators instead of producers. Furthermore, given that the calculation of the new special tax is based on the amount of "electricity injected into the public grid", it can be concluded that onsite electricity generation projects could gain ground, as in such cases the electricity generated is not injected into the public grid but is delivered to the user via private lines without using the public network. Projects along these lines have been proposed in the past, and the legislative changes discussed above could further boost these investments in the future – although it should be noted that in the absence of state support, developers will still face the Robin Hood tax.

There are also considerable uncertainties about the new rules. On the one hand, the issues that have been raised in the past in relation to the exit from the KÁT and METÁR schemes, i.e., what happens for the exit of generators that have not yet commissioned their KÁT or METÁR plant or have terminated their balancing group membership contract with the transmission system operator but it has not yet entered into force, remain unclear. Second, it is not clear whether the 0.5 MW size limit should be considered per KÁT or METÁR decision, per generation license or per project, given for example that many of today's projects of tens of MW are composed of several KÁT decisions of less than 0.5 MW in the name of the same holder, for which a separate generation license (so-called combined small power plant license) is not required because the power is below 0.5 MW. It will therefore be worthwhile to monitor how the legislator interprets the scope of the obligation for the purposes of aggregation.

It is also important to note that although the special tax on certain power producers will enter into force on 1 July 2022, some producers may already have to pay tax for the period before that date. This liability may arise for those producers who have already terminated their contract for the granting of the KÁT or METÁR aid in the tax year 2022, but before the entry into force of the special tax, or who have started their commercial operation without having concluded a contract for receiving the aid. The producers concerned will have to self-assess, declare and pay the special tax due for each month of the period between 1 January 2022 and the date of entry into force of the special tax, i.e., 1 July 2022, by 20 September 2022, which will make them liable to pay the tax retroactively.

Overall, it can therefore be concluded that it will be very difficult or impossible for KÁT and METÁR producers to take advantage of high market prices in the future. At the same time, it is clear that the government is not counting on the abolition of the Robin Hood tax, which has long been a painful issue for the energy sector, in the short term; on the contrary, it is extending the scope of the tax and stipulating that it will almost certainly remain part of the tax system for the next two years, and should therefore be taken into account by developers and investors.

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