A Comparative Study of the Vietnam-Hungary Agreement for the Avoidance of Double Taxation and the OECD Model Tax Convention

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Abstract

In international tax law, double taxation agreements (DTAs) are important instruments to allocate taxing rights between countries and eliminate double taxation on cross-border economic activities. This article conducts a comparative analysis of the 1994 double taxation agreement between Vietnam and Hungary, based on a comparison with the 1963 OECD model convention of the Organization for Economic Co-operation and Development. The OECD Model convention is considered an international standard for designing tax agreements. While the Vietnam-Hungary double taxation agreement maintains structural conformity with the OECD model, it also exhibits legal differences to ensure the tax sovereignty of each country. This article will utilize comparative legal analysis and textual analysis to examine the similarities and differences between the OECD Model convention and the Vietnam-Hungary agreement. The results illustrate that although the bilateral agreement adheres to the OECD standard framework, it proactively eliminates property taxes and strengthens the taxing rights of the source country. These differences reflect policy choices aimed at protecting Vietnam's tax base and financial sovereignty. At the same time, the study proposes recommendations to ensure a balance between the trend of international harmonization and the protection of national financial interests in the negotiation of future tax agreements.

Keywords: *Hungary, Vietnam, tax, double taxation, OECD Model, agreement, DTAs.*

JEL Classification: K34, H87, K33

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1. Introduction

1.1. Background

In the context of increasingly deep economic globalization, investment, trade, and capital movements across national borders have increased significantly. This development causes major challenges to traditional tax systems, which are designed based on national territory. When income can be generated in multiple countries, it leads

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to double taxation (double taxation imposes the same tax on the same taxpayers, same subjects, and same period of time by two or more states)[2]. This also creates a barrier for countries wishing to attract foreign investors. This phenomenon makes investors potentially burdened with large tax liabilities and required to pay taxes in multiple countries. To address this issue, countries have signed Double Taxation Agreements (DTAs), aiming to divide taxing power and minimize legal conflicts between tax systems. In this context, the OECD Model Agreement serves as an important international standard, guiding the development and interpretation of bilateral tax agreements.

However, in practice, not all countries fully apply the OECD standards. Differences in economic development levels, fiscal policies, and investment attraction goals lead to certain adjustments in the content of the agreement, especially between developed and developing countries. The tax agreement between Vietnam and Hungary (1994) is a typical case, reflecting the intersection between a developing economy and a transitional economy, where the rules on Permanent Establishments (PE) and profit allocation are customized compared to the OECD model.

1.2. Academic Novelty

This paper will focus on analyzing the similarities and differences between the Vietnam-Hungary agreement and the OECD model. Additionally, the article will use the theoretical framework of "convergence and divergence"[3] to explain why countries accept the standard OECD structure but include different provisions.

Convergence is the process by which legal systems, rules, or methods of law interpretation become similar or move closer together to address common challenges. Convergence is demonstrated by the Vietnam-Hungary agreement's strict adherence to the structure and core principles of the OECD model, creating a familiar legal environment for international investors.

Divergence occurs when countries adjust provisions to suit their level of economic development, investment incentive policies, or procedural autonomy. Adjusting regulations to suit specific economic conditions and policy objectives creates a balance between international standards and national sovereignty.

The development of the Organization for Economic Cooperation and Development (OECD) Model Convention on Taxation from 1963 to 1977 and 1992[4] subsequent updates reflect the increasing degree of legal convergence in international tax law.

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[2] Organisation for Economic Co-operation and Development (OECD), *Model Double Taxation Convention on Income and on Capital* (OECD Publishing, 1977), 7, para. 3, https://doi.org/10.1787/9789264055919-en.

[3] Sungjoon Cho and Jürgen Kurtz, "Convergence and Divergence in International Economic Law and Politics," *European Journal of International Law* 29, no. 1 (2018): 169–203, https://doi.org/10.1093/ejil/chy011.

[4] OECD, *Model Tax Convention on Income and on Capital: Condensed Version September 1992* (OECD Publishing, 1992), https://doi.org/10.1787/mtc_cond-1992-en.

1.3. Research Methods

This paper will use comparative legal analysis and text analysis

Comparative legal analysis: directly compare the text of the bilateral agreement with the OECD 1963 model to identify similarities and differences in structure and wording.

Text analysis: analyzing the text to clarify the meaning of specialized terms and the argumentative structure in the agreement. Identifying key keywords and how they are defined differently between the bilateral agreement and the OECD standard model, thereby indicating Vietnam's tendency towards domestication or internationalization in negotiating the tax agreement.

The paper includes the following sections:

- Introduction
- Theoretical basis of double taxation and the shaping role of the OECD Model
- Overview of the context of signing and scope of application of the Vietnam-Hungary Agreement
- Comparative analysis of the provisions of the Vietnam-Hungary Agreement and the OECD Model
- Evaluation and recommendations
- Conclusion

2. Theoretical Basis of Double Taxation and the Shaping Role of the OECD Model

2.1. Theoretical Basis of Double Taxation

According to international tax law, the right of states to tax is based on two main principles:

- Residence (residence, location, place of residence). This is the personal principle.
- And the principle of source. This is the principle of territory[5].

These connecting rules (that connect the tax system with the taxpayer) can be divided on two aspects: personal and economical.[6]

The principle of personal connection is based on personal relationships such as nationality, place of residence, or business location. This also known as the universal/total principle, establishes absolute and comprehensive tax obligations based on residence. Taxpayers under this principle have unlimited tax obligations, meaning they must pay taxes on all income regardless of where in the world that income is

[5] Charles I. Kingson, "The Coherence of International Taxation," *Columbia Law Review* 81, no. 6 (1981): 1152–53, https://doi.org/10.2307/1122118; Jon E. Bischel and Robert Feinschreiber, *Fundamentals of International Taxation*, 2nd ed. (Practising Law Institute, 1985), 4–5, https://lawlibrary.courts.wa.gov/cgi-bin/koha/opac-detail.pl?biblionumber=16726.

[6] Éva Erdős, *Law of Public Finances in the EU: The European Tax Harmonization* (Editura Universității "Petru Maior", 2011), 42, https://jogikar.uni-miskolc.hu/p%C3%BC_eu_tax_law.

generated[7].

The connecting rule of the economic principle is based on economic relationships, where income is generated or where assets are located (territorial principle). According this principle, a country limits its taxing rights and tax sovereignty within its territory. The taxpayer's tax obligation is limited, only to income generated or assets located within that country[8].

Applying these principles can lead to overlapping tax jurisdictions and cause double taxation. To address the issue of double taxation, countries have established Double Taxation Agreements (DTAs), which aim to allocate taxing authority and establish coordination mechanisms between tax systems. The purpose of these agreements is through distributive rules to eliminate or reduce overlapping taxing rights between countries[9]. Thus, the essence of a DTA is not only to eliminate double taxation but also to be a tool for allocating tax power among sovereign states. In addition, these agreements contribute to strengthening legal certainty and minimizing tax disputes in international transactions.

2.2. The Role of the OECD Model

The OECD Model Tax Convention serves as the "centerpiece of the global tax agreement system" and is the primary guiding tool for international standards in this field. The OECD Model provides the basic structure and regulations that most countries (both within and outside the OECD) use as a basis for negotiating and signing bilateral tax agreements[10]. The majority of current double taxation avoidance agreements are based on or significantly influenced by this model.

In addition, the Commentaries accompanying the OECD Model play a special role in interpreting the agreement's provisions and are often used by tax authorities and courts as an important reference source. The Commentaries accompanying the model agreement provide detailed guidance on how to understand and apply the provisions. They help address ambiguous wording and make the application of the agreement more effective[11]. Although the 1963 Model Agreement laid the initial foundation, a complete and systematic system of Commentaries was only officially introduced with the 1977 Model of the Organization for Economic Co-operation and Development[12]. Since then, these Commentaries have been continuously updated and play a crucial role in

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[7] Arnold A. Knechtle, *Basic Problems in International Fiscal Law*, trans. W. E. Weisflog (Kluwer, 1979), 35–36, https://ci.nii.ac.jp/ncid/BA00773724.

[8] Knechtle, *Basic Problems in International Fiscal Law*, 35–36.

[9] Ekkehart Reimer and Alexander Rust, eds., *Klaus Vogel on Double Taxation Conventions*, 4th ed., 2 vols. (Kluwer Law International, 2015), 1:183, https://research.wu.ac.at/en/publications/klaus-vogel-on-double-taxation-conventions-4th-edition-3/.

[10] Michael Kobetsky, *International Taxation of Permanent Establishments: Principles and Policy* (Cambridge University Press, 2011), 152–78, https://doi.org/10.1017/CBO9780511977855.

[11] Michael Lang and Florian Brugger, "The Role of the OECD Commentary in Tax Treaty Interpretation," *Australian Tax Forum* 23, no. 2 (2008): 95–108, https://www.wu.ac.at/fileadmin/wu/d/i/taxlaw/Institut_the_Institute/Institute/staff/publications/langbrugger_australiantaxforum_95ff.pdf.

[12] OECD, *1977 Model Convention*.

interpreting and applying international tax agreements.

The OECD Model provides distributive rules to determine the taxing rights between the source and resident countries for different types of income (such as corporate profits, dividends, and interest on loans). It helps create uniformity in how countries protect their tax sovereignty while avoiding double taxation.

The OECD Model also promotes the convergence of tax laws, bringing national tax systems closer together, thereby reducing transaction costs for multinational corporations and limiting opportunities for tax evasion. Consequently, the adoption of a common legal framework increases the consistency and predictability of the global tax system.

In short, although the OECD Model Agreement is not a legally binding document, it is an essential "guide" for the development, implementation, and interpretation of modern international tax law.

3. Overview of the Vietnam-Hungary DTA

The Agreement between the Socialist Republic of Vietnam and the Republic of Hungary on the avoidance of double taxation and the prevention of tax evasion with respect to taxes on income was concluded on the basis of the desire to strengthen economic cooperation between the two countries. The Agreement was signed in Budapest on August 26, 1994. It officially entered into force on June 30, 1995.

The Agreement is made in two copies in Vietnamese, Hungarian, and English, all texts being equally authentic. However, in the event of differing interpretations, the English text shall prevail. The Agreement applies to residents of one or both Contracting States and to taxes on income levied by a Contracting State or its local authorities/local commissions, regardless of the method of collection. Any taxes of a fundamentally similar nature enacted after the date of signing of the agreement to supplement or replace the taxes provided for in the agreement shall also be subject to this agreement.

This Agreement plays a crucial role in clarifying, standardizing, and protecting the rights of taxpayers from one country conducting business in the other, through the application of common solutions for cases of double taxation.

The Agreement contains the following main provisions:

- Scope of application: the Agreement applies to individuals and companies that are residents of one or both Contracting States. It applies to taxes on income. In Vietnam, this includes personal income tax, profit tax, and tax on income repatriation in Hungary, it includes personal income tax and corporate tax.

- The Agreement also defines key concepts such as:

• Permanent establishment (PE) includes fixed locations such as branches, offices, factories, or construction projects and installations lasting more than 6 months. The provision of consulting services through employees also constitutes PE if it lasts more than 6 months in any 12-month period.

• Residents are determined based on the domestic laws of each country (such as place of residence, place of business). If an individual resides in both locations, the Agreement prioritizes criteria such as place of permanent residence, center of living

interests, or nationality.

- The agreement defines the principles for taxing specific types of income as follows: income from real estate transfers, business profits, international transport, dividends, interest on loans, royalties, profits from asset transfers, independent personal service activities, dependent personal service activities, director's fees, artist and athlete fees, pensions, student and trainee fees, teacher, professor and researcher fees, and other income.

- Methods for eliminating double taxation:

• Vietnam applies the credit method which allows the deduction of taxes paid in Hungary from the taxes payable in Vietnam.

• Hungary mainly applies the exemption method for most types of income. However, for dividends, interest on loans, and royalties, Hungary applies the deduction method.

- Administrative and special provisions:

• Non-discrimination aims to ensure fair treatment between residents of one country and the other.

• The Agreement also provides for taxpayers to appeal against non-compliance with the Agreement within three years.

• In addition, competent authorities will exchange necessary information to implement the Agreement and prevent tax evasion.

4. Comparison OECD Model vs. Vietnam-Hungary Agreement

4.1 Agreement Structure

OECD Model consists of 7 parts: validity, definitions, income types, property tax, elimination methods, special and closing provisions

Vietnam-Hungary Agreement follows the structure of the international model. However, the Hungary-Vietnam agreement does not include provisions on property tax; the agreement focuses only on income. At the time of negotiations (1994), the focus of both countries was to promote trade and investment by addressing dynamic income streams (such as business profits, dividends, interest) rather than taxing static property values. The absence of provisions on property tax reflects the customization of the bilateral agreement to suit the domestic tax systems and practical needs of Vietnam and Hungary.

4.2 Agreement Content

Personal validity. According to the OECD, the following principles are primarily applied:[13]

- Natural person (resident principle) is based on the time factor to determine

[13] OECD, *Draft Double Taxation Convention on Income and Capital* (OECD, 1963), art. 4, https://doi.org/10.1787/9789264073241-en.

residency. The determination of permanent address is the primary factor, followed by habitual residence exceeding 183 days.

- Legal person (resident principle) is usually based on the place of registration or place of management.

The Vietnam-Hungary Agreement also applies the resident principle. However, the determination of residency under the agreement is more detailed. Accordingly, in the case where an individual is considered a resident of both Contracting States, the determination will be made according to the priority of specific rules. First, the individual will be considered a resident of the State where he or she has a permanent residence. However, if the individual has a permanent residence in both States, he or she will be considered a resident of the State with which he or she has closer personal and economic ties, known as the center of living interests. If the State where the individual has a center of living interests cannot be determined, or if the individual does not have a permanent residence in either State, he or she will be considered a resident of the State where he or she habitual residence. In cases where an individual habitual residence in both States or does not reside in either State, that person shall be considered a resident of the State of which that person is a national. Ultimately, if that person is a national of both States or is not a national of either State, the competent authorities of the two Contracting States shall resolve the matter through bilateral agreement procedures[14]. This provision ensures that the State with the right to preferential taxation is the State with the most actual and close relationship to the taxpayer. If a non-individual is considered a resident of both Contracting States under the rules above, it shall be deemed a resident of the State where its place of effective management is located (resident principle).

Permanente establishment. According to the OECD Model, construction sites, construction projects, or assembly works are considered a permanent establishment (PE) if they last longer than 12 months. This duration helps determine whether an enterprise has participated sufficiently long in the economic life of the host country[15].

The Vietnam-Hungary Agreement defines PE as including building sites, construction projects, assembly or installation works, as well as related supervisory activities. These activities constitute a PE only if they last for more than 6 months. Services (including consultancy) provided through employees or agents form a PE only if they last over 6 months within any 12-month period[16].

The provision for a shorter period (only 6 months) to establish a Permanent Establishment (PE) compared to the 12 months of the OECD Model allows the country where the economic activity originates (source country) to prioritize taxation of foreign investor profits sooner. This is particularly important for developing or transitional countries, aiming to secure government revenue from actual business activities taking

[14] Agreement between the Republic of Hungary and the Socialist Republic of Vietnam for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (Vietnam–Hungary Tax Agreement), August 26, 1994, 2044 UNTS 111, art. 4, https://treaties.un.org/doc/Publication/UNTS/Volume%202044/v2044.pdf.

[15] OECD, *1963 Draft Convention*, art. 5.

[16] Vietnam–Hungary Tax Agreement, art. 5.

place within their territory.

Income from immovable property. Both the OECD Model and the Vietnam-Hungary Agreement are essentially the similar as they both apply the source principle. Income earned by a resident of Contracting State from immovable property located in immovable property may be taxed in the State where that property is located. The taxing right of the source state applies to income from the direct use, rental, or use in any other form of immovable property[17].

Although similar in principle, the Vietnam-Hungary Agreement specifies more clearly which means of transport are not considered immovable property. Specifically, it excludes "ships, boats, aircraft and road transport vehicles". Meanwhile, the OECD Model in the source document only lists the exclusion for "ships, boats and aircraft"[18].

Income from business profit. Both documents agree on the resident principle. The profits of an enterprise in one Contracting State will only be taxed in that State, unless the enterprise conducts business in the other State through a Permanent Establishment (PE). If the enterprise has a Permanent Establishment (PE) in another State, profits of that PE are taxed in the PE's State (source principle).

Regarding this income, the Vietnam-Hungary Agreement provides more specific regulations.

The Vietnam-Hungary Agreement (Article 7, paragraph 1.b) allows the source State to tax profits from the sale of goods of the same or similar type as the goods the PE is selling in that State, even if the transaction does not go through the PE. In contrast, the OECD Model only permits the taxation of profits actually and directly attributable to the PE. This provision helps the source State (e.g., Vietnam) prevent foreign enterprises from evading PE tax by contracting directly with the head company for similar goods.

The Vietnam-Hungary Agreement stipulates very specifically that PEs are not allowed to deduct payments (such as royalties, service fees, or interest on loans - except in the case of banks) made to the head office or other offices of the enterprise. The OECD model provides a more general provision allowing deductions for general operating and administrative expenses serving the PE[19].

Although both are based on the OECD framework, the Vietnam-Hungary Agreement has been modified to prioritize the tax collection rights of the Source State more than the standard OECD model through stricter restrictions on internal expenses.

Income from international transportation. The OECD defines profits from international transport as taxable in the country where the enterprise has effective management (resident principle). However, for ships, the right to tax belongs to the country of the harbor (source principle). The scope of transport includes both ships and air shipping[20].

The Vietnam-Hungary Agreement grants the right to tax to the country of

[17] OECD, *1963 Draft Convention*, art. 6; Vietnam–Hungary Tax Agreement, art. 6.
[18] Vietnam–Hungary Tax Agreement, art. 6.
[19] Vietnam–Hungary Tax Agreement, art. 7.
[20] OECD, *1963 Draft Convention*, art. 8.

residence of the enterprise (enterprise of a Contracting State). Profits derived by an enterprise of a Contracting State from the operation of ships, boats, aircraft, or road-transport vehicles in international traffic shall be taxable only in that Contracting State. However, the means of transport defined in the agreement are broader and include road-transport vehicles in the definition of international transport.[21]

Associated enterprises. The provisions on associated enterprises in the Vietnam-Hungary Agreement and the OECD model are almost identical in both structure and content. Both documents establish a legal basis for tax authorities to regulate the profits of enterprises with special relationships in order to combat transfer pricing. Both the Vietnam-Hungary agreement and the OECD model define two cases that constitute associated enterprises and stipulate that if conditions are imposed on two associated enterprises in a commercial or financial relationship different from those between independent enterprises, then any profit that would have been generated for one enterprise but was not generated due to those conditions will be included in that enterprise's profit and taxed accordingly[22].

Income from dividend taxation. Regarding this income, both documents share a similar legal framework and determine that both countries have the right to tax it. However, there are significant differences in the tax rate limits to suit each country's economic policy.

Dividends paid by a company resident in one Contracting State to a resident of the other Contracting State may be taxed in the recipient's country of residence (resident principle).

The country where the company paying the dividends is resident also has the right to tax (source principle). In this case, two tax rates apply: 5% if the recipient company holds ≥25% of the capital of the paying company, and 15% in all other cases. Exception for permanent establishment: the 5%/15% withholding tax limits do not apply if the dividends are connected to a permanent establishment (PE) or fixed base of the recipient in the source country. In such cases, the income is treated according to article 7 (business profits)[23].

However, under the Vietnam-Hungary Agreement (article 10), the two countries agreed on a uniform withholding tax rate of no more than 10% of the total dividends if the recipient is the beneficial owner (regardless of the ownership percentage, a flat 10% rate applies to all beneficial owners), aimed at encouraging bilateral investment.

The exception for permanent establishment is the 10% withholding tax limit, which does not apply if the dividends are connected to a permanent establishment (PE) or a fixed base of the recipient in the source country.[24]

In such cases, the income is treated according to article 7 (business profits) or article 14 (Independent Personal Services).

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[21] Vietnam–Hungary Tax Agreement, art. 8.
[22] OECD, *1963 Draft Convention*, art. 9; Vietnam–Hungary Tax Agreement, art. 9.
[23] OECD, *1963 Draft Convention*, art. 10.
[24] Vietnam–Hungary Tax Agreement, art. 10.

For Vietnam (a capital-importing country), applying a 10% rate (instead of 5% as in the OECD) helps protect the right to levy higher taxes at source on large corporations, ensuring budget revenue from economic activities taking place within its territory.

Income from interest. Both documents stipulate that interest on loans can be taxed in both countries as follows[25]:

The country where the recipient of the interest is resident has the right to tax this interest (the resident principle).

The country of the payer also has the right to tax under its domestic law (source principle), but if the recipient is the beneficial owner, the tax rate is limited to a maximum of 10% of the total interest.

However, the 10% limit does not apply if the interest is effectively connected with a permanent establishment (PE) or a fixed base of the recipient in the source country. In such cases, the interest is treated as business profits or service income and is taxed under article 7 (business profits).

According to the Vietnam-Hungary Agreement, there is a difference in the definition of interest rate, clearly stating that late payment penalties are not considered interest on loans[26].

Royalty. This is the income that has a big difference between the model agreement and the Vietnam-Hungary agreement.

According to the OECD, it is determined that royalties generated in one country and paid to a resident of another country can be taxed in the recipient's country of residence (resident principle). This provision grants exclusive taxing power to the country in which the recipient resides.[27]

According to Vietnam-Hungary Agreement, royalties may be taxed in both countries[28]:

- The country of residence of the recipient (resident principle)
- The source country (source principle)

If the recipient is the beneficial owner, the tax in the source country shall not exceed 10% of the gross royalties. However, this rate does not apply if the royalties are effectively connected with a permanent establishment (PE) or a fixed base of the recipient in the source country. In such cases, the income is taxed under article 7 (business profits) or article 14 (independent personal services).

Gains from the alienation of property. Both documents agree on the principle of distributing taxing rights to two main types of assets:[29]

- Immovable property gains from the alienation of immovable property are taxable in the country where the property is situated (source principle).
- Movable property of PE/fixed base gains from the alienation of movable

[25] OECD, *1963 Draft Convention*, art. 11; Vietnam–Hungary Tax Agreement, art. 11.
[26] Vietnam–Hungary Tax Agreement, art. 11(3).
[27] OECD, *1963 Draft Convention*, art. 12.
[28] Vietnam–Hungary Tax Agreement, art. 12.
[29] OECD, *1963 Draft Convention*, art. 13; Vietnam–Hungary Tax Agreement, art. 13.

property forming part of the business property of a PE or fixed base may be taxed in the country where the PE or fixed base is located (source principle). However, if it falls under the special movable property (ships and aircraft) in article 22(3), it is taxable only in the country where the property is taxable under article 22 (resident principle).

- Other property gains from the alienation of any property not covered by the above two categories are taxable only in the country of residence of the alienator (resident principle).

The Vietnam-Hungary Agreement has a specific provision (clause 3): Gains from the alienation of shares may be taxed at the source if the company's assets consist mainly of immovable property in that other country (source principle). This provision helps Vietnam secure its right to tax.

The Vietnam-Hungary Agreement expands the scope to include "road-transport vehicles" while the OECD Model only mentions ships and aircraft. It also determines that the right to tax belongs to the Contracting State where the business operating the vehicle resides.

Independent personal services. For this income, both documents agree on the tax principle, the resident principle. Income from independent personal services of a resident of a Contracting State is taxable only in the State of residence (resident principle). If the person has a fixed base in the other Contracting State to carry out their activities, the portion of income attributable to that fixed base may be taxed in that State (source principle for the income related to the fixed base). Professional services include independent scientific, literary, artistic, educational, or teaching activities, as well as independent professions such as physicians, lawyers, engineers, architects, dentists, and accountants[30].

Dependent personal services. The provisions on dependent personal services in the Vietnam-Hungary Agreement and the OECD Model both agree on the basic principle that wages, salaries, and similar remuneration from hired workers will only be taxed in the worker's country of residence. However, the source principle may also apply if the work is actually performed in the other country. Both documents apply the "183-day rule" to determine exceptions, according to which remuneration is still taxed only in the country of residence if all three conditions are met: the worker is present in the other country for no more than 183 days, the remuneration is paid by an employer who is not a resident of the other country, and the amount is not borne by a permanent establishment or fixed base in the other country[31].

However, there are some differences such as: the 183-day period is calculated "in any twelve-month period", it explicitly includes remuneration from work on road transport vehicles, and it also observes the provisions of article 21 (regarding teachers, professors, and researchers)[32].

Directors' fees. The provisions on directors' fees in the Vietnam-Hungary Agreement and the OECD Model are entirely similar in principle regarding the

[30] OECD, *1963 Draft Convention*, art. 14; Vietnam–Hungary Tax Agreement, art. 14.
[31] OECD, *1963 Draft Convention*, art. 15; Vietnam–Hungary Tax Agreement, art. 15.
[32] Vietnam–Hungary Tax Agreement, art. 15(2).

allocation of taxable rights. Both documents agree that director's fees and other similar payments received by a resident of one Contracting State as a member of the board of directors of a company that is a resident of the other Contracting State may be taxed in that other Contracting State. The Vietnam-Hungary Agreement further clarifies the scope of application to include members of "any similar organ" of the company[33].

Artists and sportsmen. The regulations on income of artists and athletes in the Vietnam-Hungary Agreement and the OECD Model both agree on the principle of prioritizing taxation at source, that is, at the place where the actual performance or competition takes place. The core similarity is that both documents allow the country where the activity takes place to tax the income of artists (such as actors in theater, film, radio, television, and music) and athletes, regardless of whether these activities are independent or dependent on others. In addition, both establish provisions to prevent tax evasion in cases where income is not paid directly to the individual artist but to another person or organization (such as a management company), whereby the country where the performance takes place retains the right to tax this income[34].

However, the Vietnam-Hungary Agreement differs in that it includes specific tax exemptions to promote diplomatic relations, such as: income will be tax-exempt in the country where the activity takes place if that activity is significantly supported by public funds of either country, or is carried out in accordance with cultural agreements or arrangements between the two countries[35].

Pensions. Both documents provide that pensions and similar remuneration paid to a resident of a Contracting State in compensation for former services rendered shall be taxable only in the State of residence of the recipient[36].

Governmental function. Regarding this income, both documents establish the principle that the paying State (source State) has the priority right to tax remuneration and pensions arising from the State budget. Both documents agree that remuneration paid to individuals performing public services for a Contracting State, local government agency, or local authority will only be taxed in that State[37].

However, the Vietnam-Hungary Agreement (1994) stipulates the following:

The Vietnam-Hungary Agreement clearly separates remuneration (article 1) and pensions (article 2) into separate items with specific conditions for transferring the right to tax. Meanwhile, the OECD Model 1963 combines remuneration and pensions into a single paragraph and emphasizes the performance of government functions.

Furthermore, the Agreement also stipulates that the right to tax belongs to the country where the service is performed (the other country) if the individual is a resident and citizen of that country, or does not become a resident solely for the purpose of performing the aforementioned services. These criteria in the bilateral agreement help to determine the right to tax more transparently based on the individual's legal and

[33] OECD, *1963 Draft Convention*, art. 16; Vietnam–Hungary Tax Agreement, art. 16.
[34] OECD, *1963 Draft Convention*, art. 17; Vietnam–Hungary Tax Agreement, art. 17.
[35] Vietnam–Hungary Tax Agreement, art. 17(3).
[36] OECD, *1963 Draft Convention*, art. 18; Vietnam–Hungary Tax Agreement, art. 18.
[37] OECD, *1963 Draft Convention*, art. 19; Vietnam–Hungary Tax Agreement, art. 19.

residential relationship with the host country.

Students. Both texts agree that funds received by students or trainees for living expenses, studies, or training are not taxed in the country where they reside. However, the individual's presence in the host country must be solely for the purpose of studying or training[38].

Teachers, professors, and researchers[39]. This income represents a typical divergence from the OECD Model, as the bilateral agreement added a separate preferential provision to promote educational and academic cooperation.

Specifically, the Vietnam-Hungary Agreement allows individuals from one country to teach or conduct research in the other at the invitation of universities, colleges, or equivalent educational institutions, with tax exemption in the host country for a period not exceeding two years. The condition for enjoying this preferential treatment is that the income is taxable in the country of original residence, and the research activity must not primarily serve the private interests of any particular individual or organization.

In contrast, the 1963 OECD Model does not have a separate provision for teachers and researchers. Income of these individuals within the OECD framework is typically treated according to general rules on wage labor (Article 15) or falls under the category of "unspecified income" (article 21 of the OECD) and is taxed in the country of residence.

Other income. The provision on other income (article 22) in the Vietnam-Hungary Agreement significantly expands the taxing rights of the source country compared to article 21 of the OECD Model. While the OECD Model stipulates that income not specifically mentioned in previous provisions will only be taxed in the country of residence of the income recipient, the Vietnam-Hungary Agreement allows the country where the income is generated to also tax such income. The addition of the right to tax at source in the bilateral agreement is an important strategy to help Vietnam protect its right to tax newly arising income in the context of economic development that is not detailed in the agreement[40].

Taxation of capital[41]. The provisions on taxation of capital reveal a fundamental difference in scope between the two documents while the OECD Model Agreement (1963) established a separate framework in article 22 for wealth taxes, the Vietnam-Hungary Agreement (1994) focuses primarily on income tax and has no provisions for assets. The Vietnam-Hungary Agreement only addresses assets within article 2 (taxes included) for "profits from the transfer of assets", "increases in asset value" and handles these fluctuations through the transfer rules in article 13. A strategic difference is that the bilateral agreement proactively expanded the right to tax in the source country the transfer of shares in real estate companies and included road

[38] OECD, *1963 Draft Convention*, art. 20; Vietnam–Hungary Tax Agreement, art. 20.
[39] Vietnam–Hungary Tax Agreement, art. 21.
[40] OECD, *1963 Draft Convention*, art. 21; Vietnam–Hungary Tax Agreement, art. 22.
[41] OECD, *1963 Draft Convention*, art. 22. For the following discussion of relief from double taxation, see OECD, *1963 Draft Convention*, arts. 23 A–23 B and commentary on those articles, 149, paras. 47–51; Vietnam–Hungary Tax Agreement, art. 23(1)–(2), especially art. 23(2)(d)–(e).

transport vehicles. This divergence shows that the Vietnam-Hungary Agreement prioritizes protecting the right to tax the increase in value of assets arising in the country of origin (the source principle) rather than establishing a comprehensive property tax structure according to the standards of developed countries in the OECD bloc.

Methods for eliminating double taxation. Regarding methods for eliminating double taxation (article 23), both the Vietnam-Hungary Agreement and the OECD Model (1963) agree on two main pillars: the exemption method and the credit method.

The OECD Model provides a flexible legal framework, allowing countries to choose between progressive exemption (article 23a) -meaning that income from foreign countries is not included in the tax base but is used to determine the progressive tax rate, or ordinary credit (article 23b) meaning that the amount of tax paid in the country of origin is deducted from the tax liability in the country of residence but not exceeding the tax rate applicable in that country of residence.

In the bilateral agreement, Vietnam consistently applies the credit method to all types of income arising in Hungary. Conversely, Hungary uses a mixed model applying a tax-exempt method to most types of income, but using a tax deduction method for dividends, interest on loans, and royalties. The most strategic and important difference between the Vietnam-Hungary Agreement and the 1963 OECD Model is the inclusion of a hypothetical tax deduction mechanism. Accordingly, Hungary accepts that taxes exempted or reduced by Vietnamese investment incentive laws are considered as actual taxes paid for deduction purposes, ensuring that Vietnam's fiscal incentives are not negated when investors repatriate profits. In particular, for royalties, Hungary sets a default deductible rate of 15%, even if the actual tax paid in Vietnam is lower due to preferential policies. These adjustments show that the bilateral agreement has adapted the OECD's technical framework to become a tool for protecting Vietnam's foreign investment attraction policy.

Non-discrimination. Both documents prohibit higher taxation based on nationality, and permanent establishments (PEs) must be treated no less favorably than domestic businesses. At the same time, interest payments and royalties paid to residents of the other country must be deductible expenses in the same way as payments to domestic entities[42]. Furthermore, foreign-invested enterprises are also protected from higher taxation. However, there are differences in scope the OECD model protects stateless persons, while the Vietnam-Hungary Agreement does not. The bilateral agreement allows Vietnam to not apply the principle of non-discrimination to taxes on profits repatriated abroad (maximum 10%) and agricultural tax regulations. Vietnam is entitled to continue applying specific tax rates in investment licenses (according to the Law on foreign investment) without being considered in violation of the non-discrimination rule. Both texts agree that the host country is not obligated to grant non-residents the same tax benefits based on personal circumstances or civil status as residents.

Mutual agreement procedure. Both the Vietnam-Hungary Agreement and the OECD Model establish a consultation mechanism between competent authorities to

[42] OECD, *1963 Draft Convention*, art. 24; Vietnam–Hungary Tax Agreement, art. 24.

resolve taxpayer complaints when they believe they have been unfairly taxed in accordance with the Agreement. A core similarity is that both documents allow taxpayers to present their cases to competent authorities in their country of residence without being subject to domestic law remedies. These authorities are responsible for making efforts to resolve the issue by mutual agreement if the complaint is justified, and any agreement reached will be implemented regardless of the time limits stipulated in the domestic law of the Contracting States. In addition, both agreements allow competent authorities to communicate directly or establish a Joint Committee to exchange views directly to resolve difficulties in interpreting and applying the Agreement[43].

However, the Vietnam-Hungary Agreement has more specific and stringent provisions. The Vietnam-Hungary Agreement clearly stipulates a three-year period from the first notification of a measure resulting in taxation inconsistent with the Agreement. Meanwhile, the OECD Model does not specify a particular timeframe in the clause. The bilateral agreement expands taxpayer rights by allowing them to present the case to the competent authority of their country of citizenship if the case relates to non-discrimination provisions. On the other hand, the OECD Model, on the other hand, focuses primarily on the country of residence. Both allow consultations to eliminate double taxation in cases not covered by the Agreement, but the Vietnam-Hungary Agreement emphasizes that competent authorities will "jointly endeavor" to resolve any difficulties that arise.

Exchange of information. Both texts agree on the purpose of information exchange to implement the provisions of the Agreement or domestic law. At the same time, both stipulate three limitations on refusing to provide information: unlawful administrative measures, information that cannot be obtained by law, and information that reveals trade secrets or is contrary to public order[44].

However, the bilateral Agreement is more detailed, allowing disclosure to agencies involved in prosecution or complaint resolution, and specifically permitting public disclosure in court proceedings or judicial decisions. Meanwhile, the OECD Model limits disclosure only to parties involved in tax calculation and collection.

Diplomatic agents and consular officers. This provision is absolutely identical between the two documents. Both the Vietnam-Hungary Agreement and the OECD Model affirm that nothing in the Agreement affects the tax privileges of diplomatic or consular officers as stipulated in the general rules of international law or in the provisions of special agreements[45].

Territorial extension[46]. The OECD model includes a provision allowing Contracting States to extend the scope of the Agreement (in whole or with necessary modifications) to overseas territories or any other territory for which the State is responsible for international relations.

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[43] OECD, *1963 Draft Convention*, art. 25; Vietnam–Hungary Tax Agreement, art. 25.
[44] OECD, *1963 Draft Convention*, art. 26; Vietnam–Hungary Tax Agreement, art. 26.
[45] OECD, *1963 Draft Convention*, art. 27; Vietnam–Hungary Tax Agreement, art. 27.
[46] OECD, *1963 Draft Convention*, art. 28.

The Vietnam-Hungary Agreement does not include a provision on territorial extension. This reflects the fact that neither Vietnam nor Hungary, at the time of signing, had overseas territories with independent tax systems that would require provisions for territorial extension as in the OECD model.

Entry into force. The OECD model requires countries to ratify and exchange instruments of ratification directly at a designated location for the Agreement to take effect. In contrast, the Vietnam-Hungary Agreement uses a diplomatic notification mechanism, whereby the two countries notify each other after completing their internal constitutional procedures. The bilateral agreement officially enters into force on the date of the last notification[47].

Regarding the actual application date, the OECD model is flexible, leaving specific dates blank for countries to agree upon based on the tax year or calendar year of their domestic legal system. The Vietnam-Hungary Agreement stipulates the following specific and consistent application: for taxes withheld at source, the Agreement applies to income arising from January 1st of the calendar year following the year of entry into force. For other income taxes, the Agreement applies to tax years beginning on or after January 1st of the calendar year following the year of entry into force[48].

Termination. Regarding the validity of the agreement, both documents stipulate that it is valid indefinitely and that termination must be notified through diplomatic channels at least 6 months before the end of the calendar year[49].

However, the Vietnam-Hungary Agreement adds that it can only be terminated after a period of 5 years from the date of entry into force to ensure investment stability. The OECD model leaves this timeframe blank for countries to negotiate independently[50].

5. Assessment and Recommendations

The Vietnam-Hungary Agreement is a skillful customization of the OECD Model to suit a developing country like Vietnam at the time of signing. Shortening the time for establishing a permanent establishment (PE) to six months (instead of 12 months as in the OECD Model) allows Vietnam to exercise taxing rights over foreign contractors sooner. The most significant highlight is the tax sparing provision. This is a mechanism that the 1963 OECD Model does not have. It ensures that tax incentives granted by Vietnam to Hungarian investors are not neutralized when they remit profits home, thereby maintaining the effectiveness of Vietnam's FDI incentive policies.

Furthermore, including road transport in the definition of "international traffic" is a practical step reflecting geographical characteristics and the need for trade connectivity between countries with shared land borders, a point not emphasized in the

[47] OECD, *1963 Draft Convention*, art. 29.
[48] Vietnam–Hungary Tax Agreement, art. 28.
[49] OECD, *1963 Draft Convention*, art. 30.
[50] Vietnam–Hungary Tax Agreement, art. 29.

OECD Model (which primarily focuses on air and sea transport). The bilateral agreement maintains the right to tax at source for Royalties (10%) and Other Income, creating a balance of budget interests for the host country, as opposed to the OECD's trend of prioritizing the residence state.

Based on the detailed analysis of the flexible application of international rules to protect source-based taxing rights and promote investment, it is evident that the 1994 Agreement has created a solid legal foundation for cooperation between the two countries over several decades. However, in light of the global economy's shift toward the digital era and more stringent requirements for financial transparency, the maintenance of traditional provisions must be evaluated in correlation with modern trends against revenue erosion. Although the Vietnam -Hungary Agreement included provisions for the prevention of fiscal evasion within its very title, research in countries with similar circumstances, such as Ecuador (2025), indicates that multinational corporations can still exploit loopholes through "treaty shopping" tactics and aggressive tax planning to artificially reduce tax liabilities. This confirms that traditional regulations alone are insufficient to protect a nation's fiscal sustainability. Furthermore, the recommendation to supplement the treaty with anti-abuse provisions (such as PPT or LOB) becomes even more urgent when considering the lessons from Ecuador. Even though that country has adopted certain actions from the OECD BEPS plan, operational gaps still persist. This demonstrates that Vietnam not only need to update the treaty text but also must strengthen enforcement capacity and global cooperation to effectively control transactions between associated enterprises[51]. Prasad's 2025 study examines the interaction between domestic anti-avoidance rules and the treaty-based principal purpose test from an Indian perspective.[52]

Moreover, while the Agreement stipulates a complaint time limit of three years, the two nations could consider integrating online dispute resolution mechanisms or tax arbitration to support businesses and accelerate the progress of the mutual agreement procedure (MAP).

Although Article 26 already provides for the exchange of information, it needs to be upgraded to the automatic exchange of information (AEOI) standard. This alignment with global financial transparency trends would facilitate better control over capital flows moving abroad.

The 10% tax rate for dividends, interest, and royalties may require more flexible adjustments to remain competitive with the next-generation Agreements Vietnam has signed with other major partners, thereby creating a more uniform and attractive investment environment.

The current Agreement primarily focuses on physical establishments such as offices and factories. Supplementary protocols are required to redefine "permanent

[51] Katherine Estefanía Paredes Sánchez and Giovanni David Fernandez Unuzungo, "Tax Transparency and Abusive Practices in Double Taxation Agreements: Evasion, Avoidance and Treaty Strategies in Ecuador, 2025," *Journal of Educational and Social Research* 15, no. 5 (2025): 32–39, https://doi.org/10.36941/jesr-2025-0158.

[52] P. V. S. S. Prasad, "General Anti-Avoidance Rule and Principal Purpose Test – New Era of Anti-Abuse Law," *Asia-Pacific Tax Bulletin* 31, no. 2 (2025), https://doi.org/10.59403/3skmm91.

establishment" within the context of cross-border e-commerce and digital services to ensure that revenue from these modern activities is not lost. Giuliano and Rondelli discuss how digitalisation and remote working challenge the permanent establishment concept.[53] Kukulski examines the UN Model's provisions on technical and automated digital services.[54]

6. Conclusion

The Vietnam- Hungary Agreement (1994) represents a flexible and selective application of the technical framework of the 1963 OECD Model to suit the context of a developing nation like Vietnam. The core of the Agreement is the prioritization of taxing rights in the source state (Vietnam) through provisions such as a shorter period for establishing a permanent establishment (PE) and the retention of source-based taxing rights on passive income (dividends, interest, royalties) and other income.

In particular, the tax sparing mechanism is a strategic effort to protect Vietnam's investment incentive policies, ensuring that fiscal benefits are not neutralized when investors remit profits back to their home country.

The combination of international standards and these specific adjustments have created a stable and transparent legal framework that not only assists in the avoidance of double taxation but also plays a vital role in promoting investment flows and sustainable economic cooperation between the two nations.

The comparison clarifies the relationship between convergence and divergence in international tax law. A common treaty structure can accommodate different choices about taxing rights and investment incentives. For Vietnam, these choices show how participation in international economic relations can be reconciled with the protection of national fiscal interests.

Future review of the Agreement should consider the practical operation of its safeguards. Anti-abuse provisions, information exchange and the mutual agreement procedure require coherent design and effective administrative cooperation. The literature on digitalisation also broadens the options for addressing cross-border services. Proposed adjustments should be assessed for their effects on double taxation, compliance costs and taxpayer certainty.

The findings concern the Agreement's legal design and do not establish its effect on investment flows or tax revenue. A contemporary assessment should distinguish the original treaty text from subsequent amendments and any applicable multilateral modifications. Further research comparing other Vietnamese treaties and examining dispute resolution practice would help identify suitable reforms.

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[53] Immacolata Giuliano and Emanuela Rondelli, "Permanent Establishments: A Conceptual Analysis and Challenges Ahead," *European Taxation* 65, nos. 2–3 (2025): 66–73, https://doi.org/10.59403/17qms5c.

[54] Ziemowit Kukulski, "Eliminating Double Taxation of Income from Cross-Border Services in the Digital Era from the UN Model Perspective," *Acta Universitatis Lodziensis. Folia Iuridica* 110 (2025): 65–78, https://doi.org/10.18778/0208-6069.110.04.

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