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Topic 2: Taxation, State aid and distortions of competition

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Questionnaire

Part I

- 1. Does your country offer the possibility for any degree of advance legal certainty in tax matters given by the tax authorities? If so, are there any specific requirements to be eligible for such certainty in advance?**

In Denmark, the taxpayer can get legal certainty by applying for a formal advance tax ruling (Danish: "bindende svar") or by getting an advance pricing agreement (APA). Only these two possibilities are regulated.

On very rare occasions, it is also possible for the taxpayer to claim his position according to an informal statement from the tax authorities. A few case law decisions have stated that if the informal statements from the tax authorities has had the effect that the taxpayer has not obtained proof of his cost, income etc. due to the informal statement, the taxpayer can base his right on this and the expectations will be legally protected even though the cost, income etc. are not sufficiently documented. It is very uncertain and disputable when this practice of informal statements can take place. As a main rule, statements from the tax authorities are not binding for the tax authorities in Danish taxation apart from the formal advance tax ruling and advance pricing agreement. Even if the information about tax consequences are given in writing, they will not be binding for the tax authorities if the consequences are not according to the interpretation of the law.

Below we will concentrate on a description of the two regulated options for advance certainty in tax matters. First, we will describe the advance tax ruling, which will be followed by a description of the advance pricing agreements.

The advance tax ruling can be obtained by anyone, as long as the question is about income tax. It is not possible to have advance tax rulings about e.g. customs. It is possible for a taxpayer to ask for an advance tax ruling concerning his own tax matters. Likewise a company can also ask for an advance tax ruling if it for instance wants to know the tax consequences in advance when its customers use its products, e.g. if a bank has developed a new kind of loan and wants to know the tax position of the customers.

The questions can be asked both prior and after an action/decision has been made. When the taxpayer asks in advance, it is possible to make another decision, which will imply other tax consequences. When the taxpayer asks about the tax consequences concerning actions/decisions that have already taken place, the taxpayer gets certainty sooner than according to the normal procedure of tax assessment. Questions about decisions already carried out can only be directed at the taxpayer himself. In these situations, a company cannot obtain an advance tax ruling for the tax consequences of its products.

The tax authorities can refuse to answer the questions if the questioner has not given sufficient information on the matter. The question can also be rejected if it is not possible to answer the question with the necessary certainty or if other special occasions make it impossible to answer. It is the questioner's responsibility to give sufficient information to the tax authorities.

The advance tax ruling is binding for the tax authorities for a period of up to 5 years. The ruling can be given for a shorter period than 5 years. If the question concerns the valuation of an asset, the tax ruling is only binding for a period of 6 months. In addition to this, the ruling about the valuation will not be binding, regardless of the period, if subsequent conditions indicate that the valuation differs at least 30% and at least DKK 1 m. (about 134.000 euro) from the valuation accepted in the ruling. This rule was introduced because experience showed that valuation is very difficult and could be a major problem in relation to bringing the asset out of Danish tax jurisdiction. This rule on valuation of an asset might be abolished in the near future since a proposal for its repealing is in hearing.

The advance tax ruling is binding, even if it turns out that the answer is wrong. Even if the courts later decide that a rule should be interpreted differently, the advance tax ruling is binding for the tax authorities for the entire binding period. However, it is not binding if it violates EU-law, the tax law changes or the conditions for the ruling changes.

The advance tax ruling costs a fee of about 54 euro (2017, DKK 400).

The ruling is only binding for the tax authorities, not for the taxpayer. When the taxpayer receives the advance tax ruling, the taxpayer can choose to use it or not when making his annual tax assessment. If the taxpayer's view is not accepted in the advance tax ruling, he/she can still make the annual tax assessment according to his/her belief and, thereby, not follow the advance tax ruling. The taxpayer should then, however, be aware that it is likely that he will be selected for investigation by the tax authorities.

The Danish Tax Administration (SKAT) does not have a formal bilateral APA program with published rules specifically addressing bilateral APA requests. However, the Danish Tax Administration does have an established practice of accepting, processing and negotiating bilateral APA requests. This practise is described in SKAT's guidance on the website (www.skat.dk - Jura - Den juridiske vejledning - C.D.11.15.3.) Over 30 bilateral

APAs have been concluded (including renewals) since The Danish Tax Administration began actively processing bilateral APA requests around 2000. The Danish Tax Administration can either reject or accept a potential bilateral APA request at its own discretion.

The most typical bilateral APA requests concluded by The Danish Tax Authorities include the inter-company pricing of cross-border tangible goods transactions and service transactions. However, there have also been bilateral APA cases processed addressing intangible related issues (e.g. royalties and profit splits) as well as valuation issues.

Similarly, as there are no formal bilateral APA reporting requirements in Denmark. The Danish Tax Administration typically accepts that the annual reporting requirements in the corresponding country to the transaction(s) are sufficient for Danish purposes (in demonstrating compliance to the bilateral APA agreement).

There have been isolated situations where a bilateral APA process addressed PE issues; e.g., whether a certain function constitutes a PE and whether income should be allocated. However, in the rare instances where this has been seen, it was considered an ancillary issue to the more primary transfer pricing issues requested through the bilateral APA request. No formal (or informal) guidance has been issued by The Danish Tax Administration as to whether they would agree to process a PE and/or attribution of profits to a PE issue as a main issue addressed via a bilateral APA request.

Article 25 of the OECD Model Convention with respect to Taxes on Income and on Capital is the legal basis which SKAT refers to when allowing to process bilateral APA requests; and as a result, bilateral APA processes are only accepted in situations where Denmark has a tax treaty with the other country (which includes an Article 25 of the OECD model convention).

2. Do your country's tax authorities systematically verify the facts mentioned in a request for a ruling, either prior to issuing a ruling (ex-ante) or prior to issuing the annual tax assessment (ex-post)? If so, could you explain the procedure in place?

The advance tax ruling relies only on the requester's information and the tax authorities will typically not try to verify the facts mentioned in the request. This could seem rather careless, but the advance tax ruling will only be binding if all relevant information was presented for the tax authorities before making the ruling. So, if the facts are not true, the ruling will not be binding. The risk lies on the questioner.

After the annual tax assessment, the tax authorities will verify the facts after the normal standard, independent of whether or not the taxpayer has an advance tax ruling.

3. Do anti-avoidance provisions require your tax authorities to verify the treatment given to a particular payment/transaction by the other country, as part of a tax audit or prior to issuing a tax assessment? If so, could you explain the procedure in place?

The taxpayer shall make a correct tax return. If a Danish provision for instance requires a certain tax treatment in another country, the taxpayer has to meet the conditions in order to prepare the tax return in accordance with the provision. An example: Section 2 A of The Company Tax Act deals with hybrid mismatch, where an entity is taxable in Denmark, but is considered transparent in another country. This mismatch could result in tax abuse. If the entity pays interest it will be deductible in Denmark, because the entity is taxable, but it would not be taxable in the other country, since the entity in that other country is considered transparent. To prevent such tax abuse Section 2 A was introduced. According to this provision an entity is considered transparent in Denmark, if the entity is considered transparent in another country. When making the tax return the taxpayer must take the tax treatment in the other country in to consideration; if the entity is transparent in another country it must file its tax return according to Section 2 A. Afterwards in relation to a normal control procedure the tax authorities can investigate whether the conditions are fulfilled or not in order to make a correct tax assessment.

4. Could you please elaborate in what circumstances tax authorities would (not) be bound by a ruling or any other type of advance certainty provided?

Normally, the advance tax ruling is binding for a 5-year period - or 6 months if the question concerns valuation. It is binding even if it turns out to be an incorrect interpretation of the law. Since the valuation of assets is sometimes very difficult, the ruling will not be binding if there is strong indication afterwards that the valuation in the advance ruling was wrong. Moreover, in case of evaluation, the ruling is not binding if circumstances later indicate that the value at the time of the ruling differed at least 30%, or at least DKK 1 m. from the valuation given in the advance tax ruling. Besides this, the valuation rule in the advance tax ruling is normally binding for the tax authorities.

If the information, given by the taxpayer to obtain the advance tax ruling, turns out not to be correct, the ruling will not be binding for the tax authorities. This means that if not all information are given or the information is incorrect, the ruling will not be binding for the tax authorities. By making the information, the questioners risk there will be an incentive to provide the necessary and correct information.

Other circumstances can make the ruling not binding. If the facts and circumstances for the taxpayer change, the ruling will not cover this situation. The ruling can also lose its binding character if the law changes and, finally, the advance tax ruling will not be binding if it is not consistent with the EU-law. For the taxpayer, there is a risk of asking for an advance tax ruling when it concerns a “loophole in the law”. The request makes the legislator aware of the problem and they might change the law before the taxpayer has the chance to use the ruling.

The advance tax ruling must be used within the 5-year period to be covered. If the question concerns an ongoing condition, e.g. whether a taxpayer is a self-employed person, he/she will only be considered this for as long as the ruling lasts. After the binding period, the taxpayer has no right to claim to be treated as a self-employed person, even if the facts and circumstances for the person do not change.

5. Does your country check whether any remaining income will be taxed by another country? If so, does your country allow for any correction mechanism to ensure that any remainder will still be taxed at home as to avoid double non-taxation?

If profits are shifted abroad by the Danish Tax Authorities in a transfer pricing case, then the profits in the Danish company have been reduced.

According to the Danish transfer pricing legislation, it is not possible to reduce the profits in Denmark – to make a transfer pricing downwards adjustment – without a similar upwards adjustment in the other country. The applicable rule is section 2 (6) of the Tax Assessment Act (ligningsloven), which states that it is a condition for a transfer pricing downwards adjustment of the profits that there is a corresponding upwards adjustment of the profits of the other company. In case the controlled transactions are conducted with companies or permanent establishments in another country, then it is a condition that the corresponding income is subject to taxation in the other country.

Therefore, the Danish Tax Authorities have to control whether another country taxes the corresponding income. If not taxed by the other country, then a downward adjustment is not possible.

A provision like Article 26 (2) of the tax treaty between the Nordic countries where the possibility to tax an income - in order to avoid double non-taxation - is shifted from the source country to the resident country in case the source country cannot tax according to the internal tax rules is not as effective as the Danish internal rule.

6. Does your country apply any kind of default rule when allocating profits?

In Denmark, profits are allocated between the head office and the permanent establishment within a legal entity in accordance with the arm's length principle.

According to section 2 (2) of the Company Tax Act (selskabsskatteloven), the income of a permanent establishment in Denmark is calculated as the income that it would have received if it had been an independent company dealing with the same business or a similar business under the same or similar conditions. When calculating the income, the functions performed, the assets used and the risk taken in the permanent establishment are taken into account and transactions with other parts of the undertaking are included.

However, if the double taxation treaty with the country where the undertaking is resident has a provision on business profits with a different wording, then the income is calculated in accordance with this different wording.

An undertaking in Denmark with a permanent establishment in another country shall not include profits and loss from the permanent establishment unless joint international taxation is chosen. What is considered a permanent establishment and which profits and loss to exclude from taxation in Denmark is assessed in accordance with the applicable double tax treaty and the guidance in OECD's model convention.

Moreover, the arm's length principle incorporated in Danish legislation in section 2 of the Tax Assessment Act applies for transactions between an undertaking abroad and a permanent establishment in Denmark, and between permanent establishments abroad and undertakings in Denmark, see the description of section 2 of the Tax Assessment Act in question 7 below. The arm's length principle is applicable for transactions in accordance with the rules on calculating the profits of a permanent establishment and shall be calculated in accordance with the arm's length principle.

7. Did your country adopt any kind of at arm's length pricing / transfer pricing principle, either by means of formal rules or by applying it in practice? In either case, do they have any practical or formal link to the OECD's transfer pricing guidelines?

The arm's length principle was formally incorporated into the Danish legislation in 1998. However, at that time the arm's length principle was already considered a part of the applicable rules, see the discussion on the legal base for adjustments of transactions outside the scope of section 2 of the Tax Assessment Act in question 10. In 1998, legislation on transfer pricing documentation was introduced in Denmark. In the same year, a judgment

from the Supreme Court made it subject to interpretation whether the arm's length principle was applicable in all cases, and therefore the arm's length principle was introduced in section 2 of the Tax Assessment Act.

The preparatory work to the new legislation on the arm's length principle and the transfer pricing documentation referred to OECD's transfer pricing guidelines and stated that the Danish rules would be administered in accordance with the guidelines.

Therefore, the arm's length principle is a part of the Danish legislation and there is a direct link to OECD's transfer pricing guidelines.

8. Does your country allow for unilateral adjustments of profits both upwards as well as downwards?

In Denmark, upwards adjustments in accordance with the arm's length principle are allowed. Downwards adjustments in accordance with the arm's length principle are also allowed if the profit is taxed in another country, see question 5 above.

9. Suppose the buyer is a resident of your country. Under which conditions would your tax authorities normally accept the transfer pricing result of the other country - an increase in deductible costs - and adjust the level of taxable profit downwards?

The Danish Tax Authorities accept a downward adjustment if the adjustment is in accordance with the arm's length principle.

Moreover, the time limit is 10 years for an adjustment caused by an adjustment in another country and when the Danish Tax Authorities accept the adjustment in the other country. If the Danish Tax Authorities do not accept the adjustment, then the taxpayer can ask the Authorities to open a Mutual Agreement Procedure.

10. Does your country have a GAAR? If so, does your law allow it to be applied in a case of abuse as a back-up to *lex specialis* that turns out to be ineffective in a given case?

As for now, Denmark does not have a written GAAR covering tax abuse in all situations. Denmark has several rules that aim to capture abuse in special situations, e.g. rules against hybrid mismatch (Company Tax Act section 2 A and 2 B).

In 2015, section 3 of the Tax Assessment Act was introduced which implemented the anti-abuse rule, as agreed upon at the EU-council meeting on 27 January 2015. Section 3 covers the adopted change to the European Council's Parent-Subsidiary Directive art. 1, para. 2, which we were obligated to implement. But at the same time, it was

decided that section 3 also should apply to transactions covered by the Interest-Royalty Directive, the Merger Directive or double taxation treaties. According to this article, the taxpayer cannot claim the benefits for these Directives (or double taxation treaties) if the aim of the transactions is to abuse the directives (or double taxation treaties) to get tax benefits against the meaning of the Directive (or double taxation treaties). The wording of section 3 of the Tax Assessment Act is in accordance with the change to the Parent-Subsidiary Directive art. 1, para. 2, but is expanded to also cover the Interest-Royalty Directive and the Merger Directive. In section 3 (3), the same consequences are listed, when the situation is not covered by the EU-directives, but by a double taxation treaty. The wording here differs as it is in accordance with the OECD's proposal, but it is expected to be practiced primarily the same way as the EU-related anti-abuse directives.

On 20 June 2016, the Council adopted the Anti-Tax Avoidance Directive, which contains a General Anti-abuse rule. This rule should apply as from 1 January 2019. Before implementing this rule, Denmark did not have a written GAAR, but that does not mean that the tax authorities are without means to fight tax abuse. The courts of justice in Denmark use a very pragmatic interpretation of the law, when it is clear that the taxpayer wants to abuse the tax law. The courts try to interpret the law the best possible way to prevent tax abuse. It has also occurred that the Supreme Court in Denmark has neglected a benefit even if the transactions are in accordance with the wording of the law, if it is clear that the only reason for the transaction is to obtain tax benefits. However, it is rarely used. There are about 5-6 decisions all together, depending on how the decisions are interpreted.

Several attempts have been made to analyze and generalize this case law into an unwritten GAAR. But the result is unclear and highly debated. Denmark follows the "Substance over form"-doctrine and the "Rightful owner"-doctrine, but it is highly debated to what extent these doctrines can carry the tax decisions. How much can substance differ from the form and still be the main element, when deciding on the tax matter. In Denmark, there are supporters for a "reality-doctrine" (Danish: "Realitetsgrundsætning") which allows to alter the tax consequences if the formal transactions are not in accordance with the inner meaning/substance and are structured in this way only to obtain tax benefits. If the taxpayer merely uses another way to get the wanted result instead of the more obvious way, should the taxation be on the obvious way or on the actual way? For example; if the taxpayer wants to sell shares to person B, but chooses to resell the shares to the company where, at the same time, person B purchases shares from the company, because the taxation when reselling shares to the company is tax exempted, but would have been taxed if the shares were sold directly to B? At the same time, there are supporters for "Rightful owner"-doctrine (Danish: "Rette indkomstmodtager"), which in its simple form only states what is obvious; the person who has the right to an income should also be taxed on the income. However, this also results in a view, where fixated income could be taxed, for example if a person declines from receiving an income and this action causes another taxable person to receive this income. For

example, if a taxpayer decides not to have an interest from a loan given to another related person, should the taxpayer be taxed on a fixated interest, because he/she would normally have claimed an interest, and by not doing so, he transforms his interest to the other related person? In Denmark, section 2 of the Tax Assessment Act was introduced to ensure legal authority to tax fixated income in all relations between the defined connected companies and shareholders. In other situations, the “Realitetsgrundsætning” and the “Rette indkomstmodtager” are still highly debated.

Part II

11. Briefly describe whether, and if so, which rules have been implemented in your country to ensure the effective and timely recovery of (fiscal) state aid, once ordered by the European Commission.

In Denmark, there are no specific rules regarding the effective and timely recovery of (fiscal) state aid, once ordered by the European Commission. Accordingly, the implementation of a recovery decision will be handled in accordance with the normal legal procedures applied in civil proceedings.

Under the Danish Competition Act, the Danish Competition and Consumer Authority may order the recovery of unlawful public aid. In this regard, the only specific rule concerning the implementation of the recovery decision as such is that aid ordered to be repaid, shall be paid to the state treasury.

12. Have there been any examples in your country where national judges refused to allow for the (immediate) recovery of state aid? If so, please describe those situations.

There are no Danish legal cases where national judges have had to decide on the recovery of state aid or implement a recovery decision ordered by the European Commission and consequently no cases where a national judge has refused to allow for the (immediate) recovery of state aid.

14. What position do the Courts in your country take on how to deal with conflicting obligations of European Union law and international law (including bilateral agreements with non-EU Member States)?

In general, in case of conflicting obligations of Danish law and e.g. a double taxation treaty, the double taxation treaty will take precedence over Danish law, whereas in case of conflicting obligations of EU law and Danish law or e.g. a double taxation treaty, EU law will take precedence. However, such cases are rarely seen in Danish legal and administrative practice. The “Beneficial owner”-cases currently pending before the Danish courts – of which some are subject to preliminary proceedings at the European Court of Justice – may provide further guidance on how to deal with conflicting obligations once they are concluded.

However, this position will require that EU law does not itself conflict with international obligations that the EU has taken on. This is a potential issue in a pending case before the High Court of Eastern Denmark regarding the interpretation of the EU common customs tariff Nomenclature and the possible implications of conflict with the international customs conventions GATT and ITA (The Holst Group case). In 2016, the High Court of Eastern Denmark decided to request for a preliminary ruling from the European Court of Justice regarding the interpretation of the Nomenclature. Thus it will be for the Court to interpret whether EU law is in line or in conflict with international customs law, and subsequently what position the High Court of Eastern Denmark should take if there turns out to be a conflict between EU and international law.