



# KROMANN REUMERT

## DANISH TAX REFORM APPROVED

*On 28 May 2009 the Danish Parliament approved a major reform to Danish tax law. In the following we present salient features of the tax reform that are of significance to corporate taxpayers.*

### **Background**

The primary purpose of the tax reform is to reduce the taxation of employment income, which, for Denmark, is currently one of the highest levels in the world. However, the tax reform will also have significant tax consequences for Danish businesses.

### **Capital gains on shares and dividends - new Danish participation regime**

The tax reform significantly changes the Danish participation regime for corporate shareholders with effect from the income year 2010.

The tax reform introduces a distinction between subsidiary shares, group shares and portfolio shares.

Dividends and capital gains on subsidiary shares and group shares will generally be exempt from taxation, while dividends and capital gains on portfolio shares will generally be taxable (at the full corporate tax rate of 25 percent). Furthermore, capital gains on portfolio shares will - as a starting point - be taxed annually on a mark-to-market basis. However, corporate taxpayers may opt for taxation on a realization basis in relation to shares that are not traded on a regulated market.

Subsidiary shares are shares where (i) the corporate shareholder owns at least 10 percent of the shares in another company, and (ii) the company is a Danish company subject to corporate tax or a foreign company where the taxation of dividends paid by such foreign company must be waived or reduced according to the EC parent/subsidiary directive or a tax treaty between Denmark and the jurisdiction where the foreign company is a tax resident.



Group shares are shares where the corporate shareholder and the company are subject to Danish national joint taxation or could elect to be subject to Danish international joint taxation (generally, this requires that the corporate shareholder controls more than 50 percent of the votes of the company).

Portfolio shares are shares that do not qualify as subsidiary shares or group shares.

In order to counter structures where two or more corporate shareholders with shareholdings below the 10 percent threshold pool their shares in a joint holding company (to reach the 10 percent threshold) an anti-avoidance rule has been introduced. According to this rule, subsidiary shares or group shares held by a holding company are for tax purposes deemed to be held by the shareholders of the holding company if the following cumulative conditions are met:

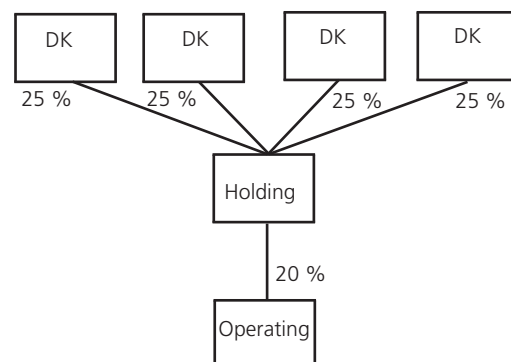
- the primary function of the holding company is to own subsidiary shares and group shares,
- the holding company does not carry out genuine economic business activities in relation to the shareholding,
- more than 50 percent of the shares in the holding company are - directly or indirectly - owned by Danish resident companies (or a Danish permanent establishment of a foreign company) that would not be able to receive tax-free dividends in case of direct ownership of the shares owned by the holding company, and,
- the shares in the holding company are not listed on a regulated market or a multilateral trading facility.

The scope of the anti-avoidance rule can be illustrated by example 1:

Four Danish corporate shareholders each own 25

percent of the shares in a holding company. The holding company owns 20 percent of the shares in an operating company. The primary function of the holding company is to own the shares in the operating company, the holding company does not carry out genuine economic business activities in relation to the shareholding in the operating company, and the shares in the holding company are not listed on a regulated market or a multilateral trading facility. Since each of the four corporate shareholders indirectly own 5 per cent of the shares in the operating company, the four corporate shareholders would not be able to receive tax-free dividends in case of direct ownership. Therefore, the four corporate shareholders are, according to the anti-avoidance rule, deemed to be the direct owners of the shares in the operating company with the effect that these shares have status as portfolio shares.

Example 1



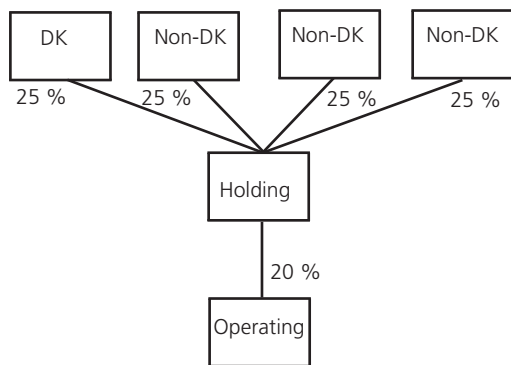
As mentioned above, the anti-avoidance rule only applies if more than 50 percent of the shares in the holding company - directly or indirectly - are owned by Danish resident companies. Consequently, the anti-avoidance rule will not apply if three out of the four corporate shareholders are foreign companies (that do not have a permanent establishment in Denmark) as illustrated in example 2:

Four corporate shareholders each own 25 percent of the shares in a holding company. Three of the corpo-



rate shareholders are foreign companies that are not tax resident in Denmark while the last shareholder is a Danish company. Since only 25 per cent of the shares in the holding company are owned by a Danish company, the anti-avoidance rule does not apply.

Example 2



It should be emphasised, however, that it is unclear to what extent the Danish tax authorities would try to argue that the holding company in example 2 does not fulfil the “beneficial owner” requirement set out in the OECD Model Tax Convention.

### Bonds - mark-to-market taxation

Gains and losses on most types of bonds held by companies are to be taxed annually on a mark-to-market basis.

### Deductibility of financing expenses

In 2007, new rules limiting the deductibility of interest and other financing costs were introduced. These rules limit the deductibility of interest and other financing costs to the extent that such expenses exceed an “interest ceiling” calculated with reference to the tax value of the company’s assets. Currently, 20 percent of the acquisition costs for shares in foreign subsidiaries are included in this calculation.

However, as part of the tax reform, this 20 percent will be gradually phased out in the period 2010 - 2017, thereby effectively rendering financing ex-

penses related to acquisitions of shares in foreign companies as non-deductible.

### Carried interest

From the income year 2010, carried interest earned by partners in private equity funds and venture funds will be taxed as ordinary income, i.e. at personal income tax rates (as opposed to their present taxation classification as share income), regardless of whether the carried interest is received by the partners in the private equity fund or venture fund or a company controlled by the partners.

### Management fees

Advisory fees paid by private equity funds, venture funds and similar and related to the acquisition of shares in companies with the purpose of participating in the management of such companies will no longer be deductible.

### Tonnage tax

The Danish tonnage tax regime allows companies that carry on shipping activities to elect to be taxed on the basis of the tonnage of the ships operated by them (instead of being taxed under the ordinary corporate tax regime). With effect from the income year 2010, the rates used under the tonnage tax regime will be increased by 15 percent as set out below:

Tonnage	Current rates	New rates
Up to 1000 NT	DKK 7.80 for every 100 NT	DKK 8.97 for every 100 NT
1,001 NT to 10,000 NT	DKK 5.60 for every 100 NT	DKK 6.44 for every 100 NT
10,001 NT to 25,000 NT	DKK 3.35 for every 100 NT	DKK 3.85 for every 100 NT
Above 25,000 NT	DKK 2.20 for every 100 NT	DKK 2.53 for every 100 NT



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