Denmark

Government Announces Long-Term Tax Reform Plan

The Danish government on August 30 presented a major 2025 reform plan that contains several significant tax initiatives.

It remains to be seen whether the minority government during the next few months will be able to secure the support needed from other political parties to implement the plan. Also, a number of the initiatives are subject to the prior approval of the European Commission, which is generally expected to support the measures.

Allowance for Corporate Equity

In one of the main corporate initiatives, the plan would address the difference in the treatment of debt and equity by allowing corporations a notional interest deduction on their equity. The allowance is intended to reduce the debt financing bias and reduce the tax motivations for leverage, thereby reducing the need for specific antiavoidance and anti-arbitrage legislation.

The equity constituting the basis for the allowance is the tax value of a company's assets, less all debts and liabilities. The notional interest rate would be fixed on an annual basis by the Danish Central Bank, based on the average two-year corporate interest rate (capped at 3 percent per annum).

The allowance would be introduced in 2019 and would apply only to equity in excess of the equity existing at the end of 2018.

Superdeduction for R&D

To further stimulate growth and development, the government would introduce a superdeduction for research and development from 2017 through 2025 in addition to increases in the ordinary tax allowances.

Currently, R&D expenses may either be deducted (100 percent) in the year they were incurred or written off in equal amounts over five years, starting the year the expenses were incurred.

In addition to the ordinary deduction, a superdeduction of 50 percent (for a total deduction of 150 percent) would be introduced for R&D expenses incurred by small and medium-size enterprises. The superdeduction would be 25 percent (for a total deduction of 125 percent) for R&D expenses incurred by large enterprises.

Qualifying R&D is defined as the application of scientific or technical knowledge to develop new or significantly improved materials, products, processes, systems, or services. The term also includes applied research (that is, research carried out to acquire new knowledge for the purpose of applying it in practice).

Tax Holiday for Entrepreneurs

The reform plan also includes a three-year, tax-exempt start-up period for new entrepreneur companies, capped at total taxable income of approximately €950,000.

The tax holiday would be introduced in 2017 and expire in 2021, unless a new political agreement to extend the scheme is reached before then.

Investment Incentives for Individuals

To encourage individuals to invest in small enterprises, the reform plan proposes a tax allowance for half of equity investments, up to approximately €90,000 per year, in small, unlisted companies. An investment of, for example, €80,000 would result in a tax allowance of €40,000 (the actual tax value being approximately 26 percent, or €10,400).

Further, the rules placing restrictions on individuals' investment of pension savings in unlisted companies would be partially eased.

Also, the reform plan includes a reduced tax rate for share income (dividends and capital gains on shares, and so forth) and on capital income (interest income, capital gains on debt, capital gains on certain financial instruments, and so forth) earned by individuals. The current tax rates for share income are 27 percent for income up to approximately €7,000 and 42 percent for any excess amount. For capital income, the marginal tax rate is about 42 percent.

The proposed reduced rates for share income are 25 percent for income up to about €7,000, 35 percent for income between €7,000 and €20,000, and 42 percent for any excess amount. The reduced marginal tax rate for capital income would be about 37 percent.

Collective Investment Funds

As part of the reform plan, an allocation of approximately €8.1 million per year would be made to align the tax treatment of investments in Danish and foreign collective investment funds and to improve the regulatory framework affecting the international competitiveness of Danish investment fund managers.

Employment Income

One of the initiatives receiving the most media attention is a proposal to reduce the marginal tax rate for income between €72,500 and €135,000 by 5 percentage points (to 47 percent). At the same time, the tax value of interest expenses would be reduced by 5 percentage points (to 28 percent).

Leasing of Private Properties

The annual tax-exempt allowance would be increased by approximately €1,400 for the leasing of private houses and apartments through an agent and by approximately €700 for the leasing of holiday houses and apartments.

Observations

If ultimately implemented, the initiatives will improve the tax climate in Denmark, which has been somewhat lacking in attracting foreign investments and risk capital for start-ups. However, because the Danish government is a minority government that needs political mandates from various parties with conflicting tax interests, it remains to be seen whether and to what extent the ambitious tax plan will ultimately prevail.

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