

RECLAIM OF DANISH WITHHOLDING TAXES ON DIVIDENDS BY FOREIGN INVESTMENT FUNDS

1 KEY TAKE AWAYS

Foreign investment funds may be entitled to reclaim Danish withholding taxes going back to 2008 on dividends distributed from Danish portfolio companies as a consequence of the Court of Justice of the European Union's (CJEU) decision in the *Fidelity Funds* case.

Pending final decision by the Danish High Court (the referring court) in the underlying cases as well as any interpretive guidance which may be issued by the Danish legislator or the Danish tax authorities, the EU decision, however, still raises the questions as to which type of foreign investment funds that can expect to successfully reclaim Danish withholding tax and when the repayment claims will be time barred.

It is generally recommendable to file a reclaim application as soon as possible and before 21 December 2018 due to the level of uncertainty on the statute of limitations. Given the technical reasoning behind the CJEU's decision, it may, however, potentially prove to be quite unattractive for many foreign funds to seek to reclaim Danish withholding taxes. Foreign funds should therefore carefully consider the best approach rather than incurring costs for processing and submitting futile reclaims.

2 LONG-READ

Background

Under current Danish tax rules, dividend distributions from Danish portfolio companies to foreign investment funds are generally subject to withholding tax at a rate of 22% or 27%. In practice, the effective rate may be reduced to 15% if the fund is resident within the EU or if the tax authorities in the country of tax residence of the investment fund exchanges information with the Danish tax authorities etc.

Qualifying Danish investment funds are, however, eligible to receive dividend distributions on Danish shares without any withholding tax. Such investment funds are instead required to calculate and report a technical income ("minimum distribution"), which is allocated to its members for Danish tax purposes in accordance with section 16 C of the Danish Tax Assessment Act ("Section 16C"), and to retain and pay a withholding tax on such income (a rate of 22% or 27%, which may be reduced to 15% for certain types of investors). Further, Section 16C only applies if the participants in the fund are entitled to the same proportional share of the fund's yearly return on each of its assets and liabilities, calculated as the ratio between the face value of each participant's certificate in the fund and the total face value of all certificates. The minimum distribution income is calculated as the sum of the revenue and net amounts received during the tax year (e.g. interest, share dividends, gains on receivables and financial contracts and gains on disposal of shares) less deductions for losses and administration costs. Further, funds covered by Section 16C must adhere to a number of specific reporting requirements.



On 21 June 2018, the CJEU ruled (case C-480/16) that it was inconsistent with the EU rules on free movement of capital when Denmark levies withholding tax on dividends on Danish portfolio shares paid to foreign investment funds while exempting comparable funds resident in Denmark from such withholding tax. The ruling concerned the period from 2000-2009 but while the relevant rules have been slightly adjusted since then, the current rules in our view still present the same overall inconsistency with the EU rules on free movement of capital.

Foreign investment funds entitled to repayment

The CJEU's decision in the *Fidelity Funds* case concerned foreign resident undertakings for collective investment in transferable securities (UCITS) within the meaning of EU Directive 85/611 (now 2009/65).

However, as Section 16C does not only concern UCITS but also certain types of alternative investment funds (in Danish: *kapitalforeninger*), not only UCITS, but also certain non-UCITS may be eligible for repayment of withholding taxes. Further, since the CJEU decision concerns the free movement of capital which also applies to non-EU states, also UCITS and non-UCITS resident in countries outside of the EU should be comprised by the decision.

The CJEU established that it would not be contrary to EU law if, in order to qualify for an withholding tax exemption on dividends received, foreign UCITS are required to (i) meet the same formal criteria as the Danish investments funds and (ii) calculate and pay a tax equivalent to the tax which the Danish investments funds comprised by Section 16C are required to withhold.

Accordingly, the Danish tax authorities are likely to argue that only foreign UCITS which have continuously met all requirements under Section 16C, except for being resident in Denmark, should be eligible for repayment of withholding taxes. This would be in accordance with the opinion of Advocate General Mengozzi delivered to CJEU on 20 December 2017 and which the CJEU decision to a large extent seems to be coherent with.

Further, not least foreign investment funds resident outside of the EU should expect to be required to provide the Danish tax authorities with extensive information and documentation about their structure etc. in order for the Danish tax authorities to get confident that the foreign fund complies with Section 16C.

This may in practice prove to be a task involving significant resources, and not much guidance provided by the decision by CJEU to convince the Danish tax authorities should be expected to be quite reluctant in granting exemption on the basis of the CJEU decision.

Statute of limitations for repayment

It seem to be the prevailing view among Danish advisors that withholding taxes covered by the *Fidelity Funds* ruling may be recoverable going 10 years back and, consequently, that withholding taxes paid as from 10 years prior to the publishing date of the CJEU's decision should be eligible for repayment, provided that an application for repayment is filed within 6 months from the publishing date of the decision.

So far, the Danish tax authorities' general position in cases regarding reclaim of withholding tax has, however, been that claims on repayment of withholding taxes may be statute barred already 3 years after the withholding tax payment date, as mentioned in our previous newsletter which can be found here: <http://accura.dk/media/4126271/denmark-2016-tax-highlights.pdf>

Given the uncertainty about the statute of limitations, it is generally recommendable to file a reclaim application before 21 December 2018 in order to secure the best possible access to seek repayment of withholding taxes paid after 21 June 2008.

What's next?

The underlying, national cases is scheduled for a hearing before the referring Danish High Court in February 2019.

While the CJEU decision implies a relatively clear dismissal of the Danish legislation in general, the High Court will need to address certain important issues in order to rule on the specific cases. The open issues are, in particular, to which extent the CJEU decision is to be interpreted in accordance with the opinion of Advocate General Mengozzi and consequently to which extent the foreign funds should (i) have complied with Section 16C in the period in question, even though such funds were precluded from applying Section 16C, (ii) retroactively calculate and pay a tax equivalent to the tax which the Danish investments funds comprised by Section 16C and (iii) whether foreign taxes are taken into account or the foreign funds need to pay *Danish* taxes equivalent to the Danish taxes payable by Danish resident funds, i.e., not disregarding foreign sourced

income and/or investors. If Danish taxes are to be paid on both Danish and foreign sourced income, an option to reclaim Danish withholding taxes on Danish sourced dividends will likely be completely unattractive for most foreign funds.

Once the Danish courts have made a final decision in the underlying case, the Danish tax authorities are expected to publish an official notice containing details on which type of funds will be eligible for the repayment, the period for which repayment can be claimed and the procedure and deadline for filing a claim etc.

Further, the CJEU decision entails that the Danish government will need to amend the existing legislation to eliminate the inconsistency with EU law. It remains to be seen how the Danish government will achieve this, i.e., whether it will implement a withholding tax exemption for certain foreign investment funds, subject to the relevant foreign investment funds paying taxes in accordance with Section 16C, or whether the government instead will repeal or amend the current exemption for Danish investment funds.

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