Denmark

Taxation of Various Crowdfunding Alternatives

Michael Tell[*] **and**
Steffen Bonde Jensen[**]

Issue: Derivatives & Financial Instruments, 2015 (Volume 17), No. 1
Published online: 22 January 2015

The authors discuss various crowdfunding alternatives in Denmark and the tax treatment thereof. Also considered are existing obstacles to crowdfunding and anticipated actions that may minimize or remove such obstacles.

1. Introduction

Crowdfunding is emerging worldwide. This new and alternative funding method is used, for example, in start-ups, political campaigns, commercial projects and non-profit projects. In countries such as Italy, the United Kingdom, the United States and Germany, start-ups have had great success in raising capital through crowdfunding.[1]

Crowdfunding in Denmark is emerging, as well, even though legislative barriers limit the use of some crowdfunding models. These legislative barriers include prospect rules, banking legislation, and rules governing suppliers of payment services, securities traders, administration of alternative investment funds, money laundering and terror financing, which were addressed in a memorandum issued by the Financial Services Authorities.[2] That memorandum does not touch upon tax consequences. Despite these barriers, some crowdfunding associations and platforms have been established, including the Danish Crowdfunding Association and Booomerang.dk.

This article will analyse the tax consequences of crowdfunding in Denmark through various crowdfunding models.

2. Crowdfunding Models

Crowdfunding is a collective term for a variety of alternative financing models through which a project or company is financed by a large pool of investors (the “crowd”).[3] Crowdfunding is an alternative to more conventional funding methods such as bank loans, business angels and capital obtained through venture capital funds.[4] Often, a large number of investors invest, with each investor contributing only a relatively small amount.

There are four main models of crowdfunding:

- the donation model;
- the reward model;
- the debt model; and
- the equity model.

The models differ in levels of commitment of both the investors and investee. Further, there are many ways of composing the contract within the different crowdfunding models. The tax consequences applicable to these four models are analysed below.

---

* **Assistant Professor, CBS, Copenhagen; Senior Associate, CORIT Advisory, Kongens Lyngby.**
** **Associate at CORIT Advisory P/S, Kongens Lyngby.**

1. *See* M. Graf & R. Michels, *Germany: Overview of the Regulatory and Tax Aspects of Crowdfunding*, Derivs. & Fin. Instrums. (2014).
2. DK: Memorandum of 18 November 2013, *Orientering om samspillet mellem alternative finansiering og den finansielle regulering*.
3. A. Ordanini et al., *Crowd-funding: Transforming Customers into Investors through Innovative Service Platforms*, 22 J. Service Management 4 (2011), pp. 444-445.
4. Ordanini et al., *supra* n. 3, at 448, 452.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

3. Donation Model

The donation model involves an element of charity or generosity. The investor simply donates money to the project or company without any financial return or other tangible benefits in return. In other words, the investee is granted a donation with no strings attached. However, the donation might offer the investors the opportunity to connect with the investee or use the donation for advertising purposes.

3.1. Taxation of the investor

The investor donates money without a claim for a return. As a main rule, such a cost is not deductible for the investor. However, exceptions do apply.

First, the donation might be considered a deductible marketing expenditure within the scope of article 8(1) of the Tax Assessment Act (TAA).[5] The investor must then substantiate that the donation is used for advertising purposes, that the donation amount is reasonable and that the advertisement sufficiently targets an indefinite group of customers or potential customers.[6]

Second, the donation is deductible if the investee is recognized as a charity by the Danish tax authorities or by an EU/EEA country. If so, a Danish investor may deduct donations up to a total of DKK 14,800 per year (2014). A list of approved organizations is published online by the tax authorities.[7] In practice, only non-profit charities are approved, i.e. commercial crowdfunding projects do not fulfil this criterion.

Whether a non-resident investor may deduct the donation depends on the tax treatment in the country of residence. However, if the investor has a permanent establishment in Denmark, the investor may be able to deduct the donation in accordance with the two above-mentioned exceptions.

3.2. Taxation of the investee

The investee receiving a donation is taxable subject to article 4 of the State Tax Act (STA), with a few exceptions. First, donations given to individuals (non-incorporated) from certain family members are not taxed. Instead, a gift duty is levied on the donation in certain situations, as follows:

- donations from grandparents, step-grandparents, parents, stepparents and children are not subject to gift duty, up to DKK 59,800 (2014). Donations exceeding this amount are subject to a gift duty of 15% on the excess amount;
- donations from stepchildren and grandchildren are not subject to gift duty, up to DKK 59,800 (2014). Donations exceeding this amount are subject to a gift duty of 36.25% on the excess amount; and
- donations from in-laws are not subject to gift duty, up to DKK 20,900 (2014). Donations exceeding this amount are subject to a gift duty of 15% on the excess amount.

Donations to certain charity organizations, associations and independent foundations are tax exempt. This does not include limited liability companies or individuals. Most commercial crowdfunding projects do not fulfil this criterion, while some non-profit organization may fulfil this criterion.

4. Reward Model

The reward model is rather similar to the donation model, and the two models are often used simultaneously. Under the reward model, the investor is rewarded for the investment with a tangible benefit (asset) – typically the first specimen of the product developed by the investee. Differentiated rewards are often used to attract larger investments. Typically, there is a significant time lapse between the investment and the receiving of the reward. If the product is never developed, the investor is often paid back the investment, if possible. The reward model therefore has many similarities with the purchase of goods or services.

---

5. *See also* DK: SKM2011.85.SR.
6. DK: SKM2004.262.LR.
7. List available at https://www.skat.dk/SKAT.aspx?oID=2061734.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

4.1. Taxation of the Investor

The investor invests in the project or company in return for receiving a reward. The investment is considered a non-deductible acquisition cost for the investor, and the received reward is tax exempt. A resale of the reward is also tax exempt. However, two exceptions apply.

First, if the investor uses the reward (asset) in the course of business, the investor might be able to write off depreciation of the asset in accordance with the Depreciation Act. Assets with a purchase price of less than DKK 12,600 (2014) may be written off in the purchase year. Assets exceeding DKK 12,600 may be written off using the declining balance method or on a linear basis, depending on the asset.

Second, if the investor invests with the purpose of making profit on the resale of the reward (asset), the resale of the asset will be taxed and the investment (acquisition cost) may be deducted from the sales price. Further, a resale of an asset in all cases could result in taxation of recaptured depreciation in accordance with the Depreciation Act.

Third, if the investor never receives the reward due to bankruptcy, the investor may deduct the loss on the claim. However, where an investor controls the investee, or the investor and investee are group companies, the investor may not deduct the loss. Further, individuals suffering a yearly net capital loss of less than DKK 2,000 may not deduct the loss (*de minimis* rule).

If the investment far exceeds the value of the reward, the investment may be wholly or partly considered a donation. In practice, the tax authorities will challenge the reward model only if the investment clearly differs from the market value of the reward.[8] Nonetheless, if the investment is considered a hybrid, the donation portion of the investment is treated as described in section 3.1.

Lastly, if the reward constitutes an option for the investor to buy an asset at a fixed price at a specific time in the future, capital gains may be taxed in the period between the investment and the exercise date. However, the actual treatment depends on the specific circumstances and must be analysed in each specific case.

Whether a non-resident investor may deduct an investment depends on the tax treatment in the country of residence. However, if the investor has a permanent establishment in Denmark, the above-mentioned tax consequences apply.

4.2. Taxation of the investee

The investee receives payment for the sale of the reward (goods or services). Therefore, the investee is taxed on the profit or may deduct a loss, depending on whether the sales price exceeds the cost of the good or service.

As mentioned in section 4.1., if the investment far exceeds the value of the reward, the investment may be wholly or partly considered a donation. If so, the donation portion of the investment is treated as described in section 3.2.

Lastly, if the reward constitutes an option for the investor to buy an asset at a fixed price at a specific time in the future, capital gains may be taxed in the period between the investment and the exercise date. However, the actual treatment depends on the specific circumstances and must be analysed in each specific case.

5. Debt Model

The debt model is a lending arrangement between the investors (crowd) and the investee. The debt model is also known as peer-to-peer lending. The loan is to be repaid and the investor receives a financial return. Usually, the investor receives higher interest than otherwise available on bank deposits, while the investee pays lower interest rates than on conventional funding – if such funding is even available. The advantage of the debt model compared to the equity model is that the investor is exposed to less risk (default risk), while the ownership of investee remains the same.

In Denmark, specific banking and investment rules are imposed on intermediaries and the investee using the debt model. This includes intermediaries (facilitators) operating an internet platform where investors and investees can meet. These rules include approval to exercise banking or investment activity, solvency requirements and supervision by the Danish Financial Supervisory Authorities. However, it seems that there might be political willingness to amend these legislative constraints in order to facilitate crowdfunding.

---

8. DK: Administrative Legal Guidelines (*Juridisk Vejledning*), sec. C.A.6.1.2.1.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

5.1. Taxation of the investor

The investor lends money to the investee. The mere disbursement of the loan is not deductible, nor is the repayment of the loan taxable. However, the return on the loan is taxable. Interest is taxed at a rate of up to 42% for individuals and 24.5% for companies.[9] Capital gains on claims are also taxed at 24.5% for companies, while individuals with yearly net capital gain of less than DKK 2,000 are not taxed under the *de minimis* rule.[10] Capital gains above DKK 2,000 are taxed at a rate of up to 42%.

Whether a foreign investor is taxed on the return on the loan depends on the tax laws in the country of residence. A foreign investor is taxed in Denmark (withholding tax) only if the investor and investee are group companies (which seldom is the case in crowdfunding).

The investor might incur a capital loss on the claim if the investee is not able to repay the loan. In such cases, the investor may generally deduct the loss.[11] However, some exceptions do apply. For individuals, situations in which a loss on a claim is not deductible include the following:

- the total yearly net capital loss is less than DKK 2,000 (*de minimis* rule);
- claims against controlled companies;
- claims against family; and
- claims where the taxation of interest or capital gains is restricted under an applicable to a tax treaty.

For companies, loss on claims are not deductible in the following situations:

- claims against group companies; and
- claims where the taxation of interest or capital gains is restricted under an applicable tax treaty.

A non-resident investor may not deduct such a loss in Demark unless the claim is allocated to a Danish permanent establishment. Whether the non-resident investor may deduct such a loss in the country of residence depends on the tax laws in the country of residence.

5.2. Taxation of the investee

The investee is not taxable of the disbursement of the loan and may not deduct the repayment of the loan. However, the return (interest and capital losses) on the loan may generally be deducted as described below.

Interest is deductible for both individuals and companies under article 6 of the STA. However, companies may incur a restriction on the deductibility if (i) the net financial cost exceeds DKK 21.3 million or (ii) the investor is a group company and the investee is thinly capitalized.[12]

Capital losses on debt are deductible for individuals only if the loan is not issued in Danish kroner (DKK) and the losses exceed DKK 2,000 in the income year.[13] Capital losses on debt incurred by companies are deductible.[14] However, companies may also be subject to a restriction on the deductibility of the capital losses if (i) the net financial costs exceeds DKK 21.3 million or (ii) the investor is a group company and the investee is thinly capitalized.[15]

If the investee is not able to repay the loan, the investee will earn a capital gain on the debt. For individuals, capital gains are tax exempt, but certain exemptions apply if the loan is written down below market value, the loan was to be repaid at an amount less than the initial loan amount or the loan is not issued in Danish kroner. For companies, such a capital gain is generally taxable. However, capital gains are tax exempt if (i) the loan is written down to the market value in a collective arrangement with creditors or a compulsory settlement or (ii) the investor and investee are group companies.

9. DK: art. 4 STL.
10. DK: Capital Gains Tax Act (CGTA).
11. DK: Capital Gains Tax Act.
12. M. Tell, *Interest Limitation Rules: An Analysis of the Danish Legislation*, Nordic Tax J. (2013).
13. DK: art. 23 CGTA.
14. DK: art. 6 CGTA.
15. Tell, *supra* n. 12.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

6. Equity Model

Under the equity model, the investor invests in the investee in return for shares (ownership) in the investee. The equity model therefore often results in many shareholders (crowd) with small shareholdings. The equity model is often more complex than the other crowdfunding models, due to the risk and change in ownership. However, the equity model also has the biggest upside because the residual return accrues to the equity holders.

In Denmark, both the investee and the intermediary (facilitator) must comply with non-tax legislative rules. For example the investee must comply with different prospectus rules, depending on the volume of the public offering – ranging from limited prospectus rules on public offerings up to EUR 1 million, to full range prospectus rules on public offerings exceeding EUR 5 million.[16] Further, the facilitator of the investment may be considered an investment company. If so, the facilitator must comply with the same requirements as banks, such as solvency requirements and be supervised by the Danish Financial Supervisory Authority. However, again it seems that there may be political willingness to amend the legislative constraints on equity crowdfunding.

6.1. Taxation of the investor

The investor invests in the investee in return for shares in the investee. The mere disbursement of the investment is not deductible for the investor, and the mere receipt of the shares is tax exempt. Proceeds from the resale of the shares, as well as received dividends are generally taxable.

For individuals, dividends and capital gains on shares are taxable at a rate of 27% up to DKK 49,200 (2014), and 42% on excess amounts. Further, capital losses on shares are deductible; however, for a deduction of capital losses on listed shares, the purchase must have initially been reported to the Danish tax authorities (SKAT).

For companies, capital gains on shares are tax exempt if the company owns at least 10% of the share capital (listed or unlisted) or owns less than 10% of the share capital in an unlisted company. On the other hand, capital losses are not deductible under such circumstances. Dividends are tax exempt if the investor owns at least 10% of the share capital. In all other circumstances, dividends are taxable. The typical crowdfunding investor would own less than 10% of the share capital and therefore be tax exempt on capital gains, but taxable on dividends. Dividends are taxable at a rate of 24.5% (declining to 22% in 2016).

A non-resident investor is not taxed in Denmark on capital gains on shares, but will be taxed on dividends received (withholding tax). Dividends are taxed at a rate of 27%, unless a reduced rate (15% or even lower) applies under an applicable treaty between Denmark and the investor's country of residence. However, for corporate investors, dividends are tax exempt if the investor owns at least 10% of the share capital and the taxation would be reduced under either an applicable treaty between Denmark and the investor's country of residence or the Parent-Subsidiary Directive.

6.2. Taxation of the investee

The investee receives an investment in exchange for issuing shares. The invested capital is tax exempt for the investee, and the issuance of shares is not deductible. If the investee distributes dividends, such distributions are not deductible.

7. Tax Policy Considerations

Access to capital is essential for all companies, but even more so for start-up companies. On 8 May 2014, the Danish government presented its growth plan, titled "Denmark Fully Out of the Crisis: Growing Enterprises". The growth plan contains 89 initiatives, including two related to equity crowdfunding.

First, the government proposes to introduce a deduction from 2016 of up to DKK 650,000 for equity investments carried out by individuals subscribing shares in small companies. This would truly encourage equity crowdfunding of Danish start-up companies, and the authors would welcome such an initiative. In addition, the government is awaiting further analysis of whether such a deduction system is compatible with EU State aid legislation.

Second, the government proposes to reduce the taxation of dividends paid from unlisted companies. The government proposes to tax only 70% of the dividends paid from unlisted companies to shareholders owning less than 10% of the share capital. If enacted, the effective taxation of such dividends would be approximately 16% from 2015.

---

16. DK: Statutory Order 643 of 19 June 2012 on prospectuses for securities traded on a regulated market, and public offerings of securities over EUR 5 million.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

While the authors would welcome such an initiative, without a reduction of some of the non-tax legal barriers, equity crowdfunding will still be subject to poor conditions in Denmark. The government still needs to discuss various solutions with the rest of the parliament, and a bill was recently proposed which calls on the parliament to force the government by the end of 2014 to identifying the legal obstacles to crowdfunding and make appropriate legislative proposals to ensure that crowdfunding can be realized in Denmark. Hopefully, the debate and draft bill will generate a new legislative basis for crowdfunding, thereby making crowdfunding more attractive as an alternative financing source. Changes are especially needed in relation to non-tax barriers (e.g. prospectus, solvency, banking rules) to stimulate the use of the debt and equity models.

8. Conclusion

Crowdfunding is emerging worldwide, including in Denmark. This new and alternative funding method is used by, for example, start-ups, political campaigns, commercial projects and non-profit projects. In certain other countries, start-ups have had success with crowdfunding, but in Denmark several legislative barriers limit its use.

The four main crowdfunding models all have different tax consequences for the investor and the investee, which are summarized in Table 1.

Table 1

	Investor	**Investee**
Donation model	General rule: No deduction Exception 1: Donations related to the business of the investor Exception 2: Donations to an approved charity (deductible up to DKK 14,800 per year (2014))	General rule: Taxable Exception: Donations received from family are tax exempt, but may be subject to gift duty
Reward model	General rule: No deduction for the investment and no tax on the reward received; no tax on resale of the reward Exception 1: Investor using the reward (asset) in business might be able to write-off depreciation on the asset; if so a resale of the asset will result in taxation of recaptured depreciation Exception 2: Investors investing with the purpose of making profit on the resale of the reward; capital gains on resale are taxable and capital losses may be deducted	Tax/deduction on the net gain/loss
Debt model	No deduction for disbursement; no taxation of repayment Interest and capital gains are taxable; capital losses are deductible Exceptions apply; *see* section 5.1.	No taxation on disbursement; no deduction for repayment Companies: interest and capital losses are deductible; capital gains are taxable Individuals: interest is deductible; capital losses are not deductible, while capital gains are tax exempt Exceptions do apply; *see* section 5.2.
Equity model	No deduction for disbursement; no taxation of received shares However, received dividends and capital gains on subsequent sale of shares are taxable; capital losses are deductible Exceptions apply for companies; *see* section 6.1.	Investment received is tax exempt; issuance of shares is not deductible Distribution of dividends is not deductible

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.

	Investor	Investee

The government recently presented a growth plan that meets some of the needs in relation to equity crowdfunding. Two initiatives have been suggested, including a deduction for the investor of up to DKK 650,000 for equity investments carried out by individuals subscribing shares in small companies. The second initiative includes limited taxation of dividends paid by unlisted companies to those owning less than 10% of the share capital. However, further changes are needed in relation to prospectus and banking rules, for example, in order to make crowdfunding more attractive in Denmark.

© Copyright 2015 IBFD: No part of this information may be reproduced or distributed without permission of IBFD.
Disclaimer: IBFD will not be liable for any damages arising from the use of this information.