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A: Group approach and separate entity approach in domestic and international tax law

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Summary and conclusions

The flavor of the Danish tax system is a separate entity approach. As a result, the liability to pay taxes follows other liabilities of the entity, i.e. limited liability companies are considered separate and legal entities for tax purposes. For companies subject to group taxation, the corporate veil is however pierced in regard to liability of paid taxes, including withholding taxes. The purpose of this joint liability of taxes is to ensure an easier administration (the administration company is a "one-stop-shop" for the tax authorities and the other companies subject to group taxation) and to prevent abuse, e.g. by making foreign payments without withholding any taxes followed by liquidation. Besides this, no tendency to (further) pierce the veil of corporations from an overall tax policy perspective seems to exist.

The Danish tax system is based on the separate entity approach and, as such, the Danish rules on transfer pricing apply to all transactions between dependent parties, i.e. also transactions between domestic companies subject to mandatory joint taxation. In addition, the Danish domestic rules on income allocation to foreign and domestic permanent establishments are based on the AOA, where allocation is based on hypothesizing the PE as a separate and independent enterprise.

Under Danish tax law it is however recognized that controlled companies may have different incentives (and planning opportunities) than independent companies. Therefore, most anti-avoidance rules are only applicable for controlled companies, e.g. transfer pricing, CFC legislation, and thin capitalization. In addition, thresholds for being subject to tax benefits or restrictions are applied on a group basis, such thresholds being company size, revenue, asset base, EBITDA, losses etc. The purpose is to ensure that it is not possible to split up entities in order to obtain a tax benefit or avoid being subject to a restriction.

Part One: Separate entity approach and group approach in domestic law

1.1. General overview

The flavor of the Danish tax system is a separate entity approach. As a result, the liability to pay taxes follows other liabilities of the entity, i.e. limited liability companies are considered separate and legal entities for tax purposes.

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In the Danish domestic corporate tax system, a distinction between separate entity taxation and transparent taxation is made, whereas only limited liability companies are generally considered legal entities for tax purposes. As such, partnerships are treated as transparent entities for tax purposes.

Legal entities subject to corporate income tax are listed in section 1 of the corporate income tax act[3] and include:

- public limited liability companies (aktieselskab, A/S) and private limited liability companies (anpartsselskab, ApS);
- other resident corporate entities in which none of the participators are personally liable for the entity's debts and which distribute their profits in proportion to the capital contributed by each participator, i.e. foreign-incorporated entities of a similar description as companies with limited liability;
- investment funds that issue negotiable documents for members' capital contributions, however only for income related to carrying on a business;
- foundations and other resident entities, such as associations, however only for income related to carrying on a business; and
- (hybrid) entities subject to the anti-hybrid rule.

Entities subject to the anti-hybrid rule[4] (first enacted in 2008 and later revised to closer align the EU ATA Directive anti-hybrid rules) are Danish transparent entities and foreign entities with a registered branch in Denmark, where one or several associated participants (entities and individuals) together hold directly or indirectly at least 50 percent of the voting rights, capital ownership of or entitlement to the profits of the taxpayer and these participants are:

1) tax resident in a jurisdiction where the Danish (hybrid) entity or the branch is treated as a separate entity for tax purposes; or
2) tax resident in a jurisdiction that does not exchange information with the Danish tax authorities under a double tax convention, any other international convention or administrative agreement on mutual assistance for the recovery of claims relating to taxes; or
3) directly owner(s) and tax resident in a non-treaty and non-EU member state.

The Danish tax system is not specifically built or inter-linked to the financial accounting system and standards, but may be considered built "on-top" of it. Some concept may therefore be inter-linked, but when a definition used for accounting purposes is also to be used for tax purposes, it is clearly stated in the law or the preparatory work. As an example, under the Danish anti-mismatch rules[5] on the definition of associated participants it is stated that "by an associated participant is also meant a separate legal entity that is part of the consolidated group for accounting purposes". However, when the same term is used for tax and accounting purposes and the term is not sufficiently defined in the tax laws, preparatory work or case law, the treatment/classification for accounting purposes may to a certain extent also be used when outlining the scope of a term for tax purposes.

In addition, in practice, the profit and loss account in the annual report is the starting point for determining taxable income, although a separate profit and loss account for tax

[3] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 1.

[4] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 2C.

[5] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 8C(1)(17).

purposes must be drafted and filed. Thus, the profit and loss account for tax purposes often deviates from the annual profit and loss account for accounting purposes, e.g. due to different depreciation, amortization, valuation and deduction principles.

1.2. General system of inter-company transactions outside special group taxation regimes

Resident companies are subject to corporate income tax and taxed under a modified worldwide income principle i.e. taxation of the worldwide income while income from foreign immovable property and permanent establishments are generally exempt. The corporate income tax rate is 22%.

In relation to the shareholders, a distinction must be made between individuals and corporations.

Danish individual shareholders are for "share income" (dividends and capital gains on shares) subject to a tax rate of 27% (2022: up to DKK 57,200)[6] and 42%[7] on the exceeding amount. The purpose is to obtain an effective taxation of 43.06%/54.76% (22% CIT-level and 27/42% shareholder level) mirroring the progressive tax rate levied on personal income of Danish resident individuals (up to approximately 56%). Even though the taxation on corporate level is not taken into account when determining the taxable income at the individual shareholder level, i.e. no credits or similar are granted, the system is based on economic double taxation.

For corporate shareholders, this economic double taxation is also taken into account – not in the form of credits or similar but in the form of low or no taxation on shareholder level. As such inter-company dividends and capital gains on shares are tax exempt. For this purpose, shares are divided into the following categories:

Category	**General characteristics / requirements**	**Dividends (gross amount)**	**Gains (and losses) (net of acquisition price)**
Subsidiary shares	Ownership of at least 10% In addition; – The subsidiary is a Danish private limited company; **or** – A similar foreign entity subject to tax in a state that has an agreement with Denmark on exchange of information.	Tax exempt	Tax exempt

6 Subject to adjustment every year.

7 As part of the government's current proposal on earlier retirement, it is politically being discussed to increase the tax rate from 42% to 45% on share income above the annual threshold as part of financing plan. However, no bill has been proposed yet.

Category	General characteristics / requirements	Dividends (gross amount)	Gains (and losses) (net of acquisition price)
Group shares	If the shareholder and the group company: – Are subject to mandatory domestic group taxation **or** – Could be subject to international group taxation.	Tax exempt	Tax exempt
Tax exempt portfolio shares	Ownership of less than 10% In addition; – The shares are non-listed; **and** – The portfolio company is a Danish private limited liability company or a similar foreign company.	70% of the dividends are taxable at the CIT rate of 22%, i.e. effective tax rate of 15.4%	Tax exempt
Taxable portfolio shares	All other shares	Taxable at the CIT rate of 22%	Taxable at the CIT rate of 22%

For most categories of shares, dividends and gains are treated similarly. However, this is not always the case and therefore several "anti-avoidance" measures are enacted for the purpose of ensuring that dividends are not "reclassified" as capital gains. As an example, the gross proceeds from the sale of shares to the issuing company and liquidation proceeds are in some cases classified and taxed as dividends.

Further, capital losses on debt claims against a group company are non-deductible for the creditor company, whereas the corresponding capital gains for the debtor company are tax exempt. This does not apply for currency losses/gains.[8]

The Danish rules on transfer pricing[9] apply to all transactions between dependent parties. Dependent parties are defined based on ownership of share capital and control (including joint control and joint management). When assessing to what extent 'control' exists, share capital and voting power owned by or at the disposal of individuals and transparent entities are also included. This may result in a situation where companies owned by different private equity funds managed by the same individuals may be considered dependent parties under the transfer pricing rules. The definition is broader than the one used under the group taxation regime.

The Danish transfer pricing rules follow the OECD Guidelines, including country-by-country reporting and transfer pricing documentation based on the master/local file concept. Transfer pricing documentation should be prepared on an annual basis and submitted no later than 60 days after the deadline for filing the tax return. As of the

8 The Danish Act on Taxation of Capital Gains and Losses on Claims and Debt [*Kursgevinstloven*] § 8.
9 The Tax Assessment Act [*Ligningsloven*] § 2.

income year 2021, pure Danish transactions are not subject to the annual transfer pricing documentation to be mandatory submitted. This exemption does only apply to the extent no foreign transactions – wholly or partly – take this Danish transaction into account, e.g. by including the transaction in a cost base.

Last, thin capitalization rules apply according to which deduction of interests and capital loss on controlled debt may be denied to the extent the total debt-equity ratio exceeds a ratio of 4:1 unless the taxpayer can substantiate that the interest and debt itself are at arm's length. If the creditor company cannot deduct interest costs under the thin cap rules, the debtor company is also tax exempt. We refer to section 1.5.2 for a more thorough description hereof.

1.3. Group taxation regimes

1.3.1. Groups of companies in commercial law and for accounting purposes

The definition of group companies is identical under commercial law and accounting principles.

In Denmark, the IAS, IFRS and the Danish GAAP accounting standards may be used. Under Danish GAAP, a group consists of a parent company and its subsidiaries, whereas the parent company has controlling influence of the subsidiary's economic and operational decisions.[10] This situation normally occurs when the parent company directly or indirectly has more than 50% of the voting rights in the subsidiary, unless it can be demonstrated that such an ownership does not constitute controlling influence. As such, controlling influence – without direct or indirect ownership of more than 50% of the voting rights – may occur, if the parent company:

1) has more than 50% of the voting power at its disposal by virtue of an agreement with other shareholders;
2) has authority to control the financial and operational affairs of the company by virtue of an agreement or the articles of association;
3) has authority to appoint or dismiss the majority of the highest management body (e.g. board of directors) and this body has the controlling influence of the company; or
4) has the power to exercise the actual majority of votes at a general meeting or equivalent body and therefore has the actual control of the business by virtue of the other shares being widespread.

A company can only have one parent company and therefore, if several companies fulfill the formal criteria for being a parent company, only the company that actually controls the subsidiary's economic and operational decisions is considered the parent company.

Group companies must have the same financial year and must prepare a consolidated financial report. The domestic accounting rules on consolidated financial reporting should be interpreted in accordance with the *IFRS 10 Consolidated Financial Statements*.

A (Danish) parent company can be exempt from preparing a consolidated financial report if:

[10] The Danish Financial Statements Act [*Årsregnskabsloven*] Annex 1B.

- the parent itself is a subsidiary of (another) parent company that prepares a consolidated financial statement in accordance with the EU directive 2013/34/EU or similar; or
- is a smaller group (class B[11]); or
- if all the parent company's subsidiaries can be excluded from the consolidation.

For commercial law purposes, the group definition is similar to the group definition for accounting purposes.[12] For commercial law purposes, the group definition does not only apply for companies with limited liability (separate entities for tax purposes) but for all legal entities, i.e. also tax-transparent entities.

As a main rule, companies in a group are not liable for other group members' liabilities (unless as participant in an entity with unlimited liability). However, based on a Supreme Court case from 1997, it is possible under very specific and rare circumstances to pierce the corporate veil as described in section 1.3.2 below.[13]

1.3.2. Existence, scope and effects of group taxation regimes

Prior to the enactment of group taxation by law, an administrative practice existed according to which it was possible to consolidate group companies for tax purposes to the extent that the companies were administratively and economically integrated, including 100% ownership, that the companies were conducting the same line of business and that the board of directors and management were coincident. At the end of the 1920s, the tax authorities tried to abolish this practice, as a new provision that eliminated the economic double taxation of dividends was enacted.[14] This resulted in several cases.

The first rules on group taxation in Denmark were enacted in 1960 as part of the introduction of the Corporate Tax Act. The now historic group taxation regime was voluntary and required full ownership of all shares in a subsidiary (i.e. a 100% ownership requirement).[15] For a long time, it was formally required that an economic integration of the subsidiary existed. It seems to follow from the preparatory work to the provision that the political rationale for legalizing the group taxation regime was the possibility to offset losses between group companies. This is still the main objective of the current system. The group taxation regime has been modified and amended several times.[16]

In 2005, the Danish group taxation reform was passed by Parliament and the current regime was enacted. Thereby a mandatory national group taxation regime was introduced. Accordingly, Danish consolidated companies (not including foreign permanent establishments and foreign immovable property) and permanent establishments and immovable property in Denmark are subject to group taxation, i.e. this regime applies

[11] Balance sum of DKK 0-44 million, net revenue of DKK 0-89 million and 0-50 employees. When assessing the equity investments in associated companies for the purpose of assessing the size of the group, *IAS 28 Investments in Associates and Joint Ventures* is applied as guidance.

[12] Defined in The Corporate Act [*Selskabsloven*] § 6 and § 7.

[13] The case is published as U1997, 1642H /TfS 1997.780H.

[14] The then applicable State Tax Act [*Statsskatteloven]* § 37(3) and (4).

[15] Some minor exceptions existed. Companies that could opt for group taxation were referred to directly in § 31 of the then applicable Corporation Tax Act [*Selskabsskatteloven*].

[16] In 1995 the Danish CFC regime was enacted, which for the covered companies/groups is in fact a mandatory group taxation regime.

to all business on Danish territory within the same group. In addition to the mandatory national group taxation, an option to choose international group taxation exists. Choosing international group taxation is voluntary, but an all-in or all-out principle has extensive consequences.

The current group definition under the group taxation regime is based on the definition in the Danish Financial Statements Act. Thus, in this regard, the group definition for tax, commercial and accounting purposes is equivalent. As such, under the group taxation regime, a group consists of a parent company and its subsidiaries, whereas the parent has controlling influence of the subsidiary's economic and operational decisions.[17] This situation normally occurs when the parent directly or indirectly has more than 50% of the voting rights in the subsidiary, unless it can be demonstrated that such an ownership does not constitute controlling influence. As such, controlling influence – without direct or indirect ownership of more than 50% of the voting rights – may occur, if the parent company:

1) has more than 50% of the voting rights at its disposal by virtue of an agreement with other shareholders;
2) has authority to control the financial and operational affairs of the company by virtue of an agreement or the articles of association;
3) has authority to appoint or dismiss the majority of the highest management body (e.g. board of directors) and this body has the controlling influence of the company; or
4) has the power to exercise the actual majority of votes at a general meeting or equivalent body and therefore has the actual control of the business by virtue of the other shares being widespread.

A company can only have one parent company and therefore, if several companies fulfill the formal criteria for being a parent company, only the company that actually conducts control of the subsidiary's economic and operational decisions is considered the parent company. When calculating the voting rights in a subsidiary, the voting rights related to shares owned by the subsidiary itself (own shares) and the subsidiary's subsidiaries ("grandchildren") should not be included.

The group taxation regime enables group companies to offset losses within the group. Therefore, even though it is possible to make tax exempt group contributions[18] between entities subject to group taxation, intra-group transactions are still recognized for tax purposes and should be in accordance with the arm's length principle. Thus, each entity is still considered a taxpayer and should still prepare a statement of taxable income on an individual basis, whereas the sum of the taxable income for each of the entities is referred to as the group tax income [*sambeskatningsindkomsten*]. Consequently, the consolidated financial accounting does not form the basis for the group taxation.

When each entity has prepared a statement of taxable income on an individual basis, each profitmaking company offsets (potential) own losses carried forward from income years before the company entered into the group taxation. Then, if there are (still) both lossmaking and profitmaking companies in the group, the current year losses are offset against profits in the profitmaking companies on a pro rata basis. If there are (still)

[17] The Danish Corporation Income Tax Act [*Selskabsskatteloven*] § 31C.

[18] Companies which are (i) subject to the mandatory national group tax regime or (ii) could opt for the international voluntary group tax regime may make tax exempt group contributions. Such group contributions are treated as non-deductible expenses and may in some situations be considered a distribution for the contributor, potentially subject to dividend withholding tax.

profitmaking companies in the group, losses carried forward from earlier income years are offset against the profits in the profitmaking companies on a pro rata basis. If on the other hand there are (still) lossmaking companies in the group, these losses are carried forward. Current losses and losses carried forward can only be offset by another group company to the extent both entities were subject to group taxation when the (offset) loss occurred. In addition, for the purpose of avoiding "double dip", losses in foreign group companies' permanent establishments in Denmark cannot be offset against income in other Danish group entities under the national group tax regime to the extent the loss can (also) be offset against the (foreign) taxable income in the state where the foreign group company is tax resident. Outside the group taxation regime, it is not possible to offset losses in one company against profits earned in another company.

Under the group taxation regime, the ultimate parent company participating in the group taxation functions as the "administration company" – a "one-stop-shop" for the authorities and to a certain extent the other group companies. Thus, the administration company is responsible for paying the total corporate tax of the group (in a timely manner). In addition, the tax authorities can pay tax refunds and compensations to the administration company with liberating effect.

Companies and Danish permanent establishments are obliged to pay the administration company any taxes etc. paid by the administration company to the tax authorities on behalf of these companies and Danish permanent establishments.

When a company or permanent establishment within the group taxation regime has utilized losses from another group company, the administration company is required to pay an amount equal to the tax value of the utilized losses to this group company. Similar, the company or permanent establishment utilizing the losses is required to pay to the administration company an amount equal to the tax value of the utilized loss.

Under the group taxation regime, the corporate veil is pierced in regard to liability of paid taxes, including withholding taxes. Thus, the administration company (the ultimate parent) and 100% directly and indirectly owned subsidiaries are joint and severally liable for corporate income tax, withholding tax, tax on account and residual tax including surcharges and interests that relate to the income allocated to/relating to the company. If none of these joint and severally liable companies can meet the (re)payment requirement, other companies in the group taxation are liable on a pro rata basis based on the administration company's direct and indirect ownership of the share capital.

1.4. Change of control rules

The Danish rules on losses carried forward entail that the losses may be carried forward without any time limit, but utilization is restricted in the sense that losses cannot be used to offset more than 60% of the taxable income above a threshold in any (future) income year. In 2022, this threshold is DKK 8,872,500 (approx. EUR 1.2 million).[19] For companies subject to group taxation, this threshold applies for the entire group on a consolidated basis, i.e. not for each entity.

In the event of change of control, the utilization of carry forward of losses may be restricted. In general, tax losses occurring prior to the qualifying change of ownership may

[19] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 12.

not be set-off against the company's net financial income; instead, such losses can only be set-off against business income.[20] In addition, tax losses occurring prior to the qualifying change of ownership may not be set-off against any future income, to the extent the company (or any of its subsidiaries) does not assume any economic risk as a consequence of the business activities.

Change of control is defined as more than 50% of the company's capital at the end of a tax year is owned by shareholders other than those existing at the beginning of the tax year in which the company incurred losses *or* if a change in ownership during the tax year represents more than 50% of the voting power. This rule does not apply for listed companies (or companies with shares traded on a regulated marked).

The "change of control"-test includes a transparency (look-through) rule. Accordingly, if at least 25% of the share capital in the company in question is owned by another company (the parent company), the test applies to the shareholders of the parent company. The purpose of this transparency (look-through) rule is to ensure that the restrictions do not apply in case of intra-group transfers and re-organizations, where the ultimate ownership of the company is not changed.

The transparency rule applies to both resident parent companies and parent companies resident in another EU member state or in a country that has concluded a tax treaty with Denmark. For non-resident companies, it is an additional requirement that:

1) the shares in the subsidiary are transferred in the period between the beginning of the lossmaking tax year and the tax year in which the losses are utilized; *and*
2) the shares are transferred to (i) the parent company or (ii) another subsidiary in which the parent company owns at least 25% of the share capital in the previously mentioned period.

1.5. Relevance of belonging to a group/control in other contexts

1.5.1. Special anti-avoidance rules (foreseen under statutory law as well as developed in administrative principles and jurisprudence) depending on "group" or "control"

As mentioned, the Danish corporate tax system is built on a separate entity approach. However, even though the Danish tax law is built on a separate entity approach, thresholds for being subject to tax benefits or restrictions are applied on a group basis, such thresholds being company size, revenue, asset base, EBITDA, losses etc. The purpose is to ensure that it is not possible to split up entities in order to obtain a tax benefit or avoid being subject to a restriction.

Under Danish tax law it is recognized that controlled companies may have different incentives (and planning opportunities) than independent companies. Therefore, most anti-avoidance rules are only applicable for controlled companies, e.g. transfer pricing, CFC legislation, and thin capitalization. Besides the anti-mismatch rules etc. enacted as part of the implementation of the EU ATA Directive,[21] rules on reverse hybrid entities and special

[20] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 12D (1).

[21] Except in regard to CFC legislation (not yet passed by the parliament), the Danish anti-avoidance rules have been amended as part of enacting the EU ATA Directive and thus, the Danish rules now follow the provisions of the directive.

anti-avoidance rules on circumventing taxable dividends to tax free capital gains also only apply in a controlled environment.

1.5.2. *Special rules for the attribution of intra-group interest*

In general, interest payments are deductible under Danish tax law regardless of intra-group or third-party interest. However, the following three interest limitation rules do apply in Denmark:
(i) a thin capitalization rule[22]
(ii) an asset-based limitation rule[23]
(iii) an EBITDA-based limitation rule[24]

Thin capitalization rule

The thin capitalization rule only applies to intra-group interest, while the asset-based rule and EBITDA-based rule apply to all interest. All three rules are applied on the group level.

The thin capitalization rule entails a disallowance of interest deduction on intra-group loans as well as capital losses on intra-group loans. The thin capitalization rule applies to intra-group loans and to loans from third parties if the loans are either directly or indirectly guaranteed by a group company for example back-to-back loans. The thin capitalization rule only applies if (i) the debt-to-equity ratio exceeds 4:1 at the end of the income year and (ii) the Danish company has controlled debt exceeding DKK 10 million.

For Danish groups these criteria are tested on the group level. Consequently, the solvency ratio and controlled debt are applied on the group level when assessing whether or not interest limitation may be imposed.[25] The group definition is not necessarily identical to the entities being subject to Danish group taxation as the thin capitalization rules are applied only to Danish group companies (more than 50% of the shares/votes) that are still considered group companies if foreign shareholders and a Danish ultimate parent company (if any) are disregarded. This to some extent ensures vertical group level application of the thin capitalization rules.

Gross interest payments and capital losses arising from the excessive part of the intra-group debt cannot be deducted. If the deductibility is denied, the limitation is allocated between the group of companies that have contributed with interest expenses and capital losses. Consequently, companies without intra-group debt and companies that are not individually thinly capitalized may be affected by the thin capitalization rule. If the company can substantiate that similar funding could have been obtained between independent parties, the limitations of deduction may be reduced or completely eliminated.

An interest-receiving Danish company is tax exempt on interest income and capital gains if the corresponding deduction of the interest payments and/or capital losses relating

[22] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11.
[23] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11B.
[24] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11C.
[25] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11(4).

to the intra-group debt has been denied according to the Danish thin capitalization rule or similar foreign thin capitalization rules.[26]

Asset-based limitation rule

The asset-based limitation rule denies interest deductions, as well as other deductions for net financing expenses, if the net financing expenses exceed the tax value of assets multiplied by a standard rate.[27] A minimum threshold of net financing expenses up to DKK 21.3 million applies.

The basis for the computation, of any limitation of deduction of net financing expenses, is the tax value of the corporations assets (not including shares, receivables, claims etc.) multiplied by a standard rate (2021: 2.3%).[28] As the tax value of the assets are used, depreciations will reduce the corporation's maximum limit for the deductibility of net financing expenses. Further, assets without a tax value or a tax value of zero will not be included in the calculation.

The net financing expenses include:

– interest payments and deductible commissions related to loan agreements;
– capital gains and losses on claims, loans and financial instruments;
– a calculated finance cost on financial lease arrangements; and
– dividends as well as capital gains and losses on shares.[29]

The net financing expenses which exceed the tax value of the assets multiplied by the standard rate cannot be deducted.

Generally, net financing expenses which cannot be deducted are not eligible to be carried forward according to the asset-based limitation rule. However, net capital losses relating to debt, including foreign exchange losses, and financial instruments may be carried forward for three tax years to offset future gains on debts, including foreign exchange gains, and financial instruments.[30] Further, it should be noted that unrealized losses on interest swaps related to debt secured in real estate can always be carried forward during the term of the interest swap to offset any future gains on the same interest swap.

The asset-based limitation rule is applied on a consolidated basis for corporate groups and permanent establishment subject to Danish joint taxation. Accordingly, the net financing expenses and assets are calculated jointly when assessing a potential interest limitation according to the asset-based limitation rule.[31] If the deductibility of net financing expenses are denied, the limitation is allocated to each individual group company that exceeds the individual asset-base, proportionally based on each group company's net finance expenses exceeding the assets multiplied by the standard interest rate (asset base).

[26] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11(6) and (7).
[27] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11 B.
[28] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11 B (2).
[29] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11 B (4).
[30] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11 B (10).
[31] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11 B (8).

EBITDA-based limitation rule

The EBITDA-based limitation rule – originally introduced in 2007 as an EBIT rule but amended following the ATAD – denies the deduction of net finance expenses not related to the generation of taxable income in Denmark.[32] Consequently, the income before net financing expenses, taxes, depreciation and amortization (EBITDA) can only be reduced by a maximum of 30% by virtue of deducting net financing expenses. Net financing expenses up to the threshold of DKK 22,313,400 (approx. EUR 3 million) are not affected.

The definition of net financing expenses in the EBITDA-based limitation rule are to a large extent similar to the definition of net financing expenses in the asset-based limitation rule, but dividends and capital gains and losses on shares are not included in the definition of net financing expenses in the EBITDA rule.[33]

A group ratio rule applies in conjunction with the EBITDA-based rule, as the ratio of net interest to third parties divided by the EBITDA of the worldwide group can replace the fixed 30% ratio in accordance with OECD BEPS Action 4 Report and ATAD article 4. Hence, corporations subject to Danish joint taxation, or which *could* be part of Danish international joint taxation, may instead of the 30% rate rely on its group's third-party net financing expenses/EBITDA ratio based on the group's consolidated financial statement.

The EBITDA-based limitation rule is – like the asset-based limitation rule – applied on a consolidated basis for corporate groups and permanent establishments subject to Danish joint taxation. If deduction of net finance expenses is limited, the limitation is allocated to each individual group company proportionately to the extent that the individual company's excess borrowing costs exceed 30% (or the percentage applied to the group) of the company's EBITDA. If the allocated limitation exceeds the actual net finance expenses in some of the companies, this excess limitation is allocated proportionally to all other group companies.

1.6. Special rules at the local or regional level for the profit allocation in groups of companies

The Danish corporate income tax is a federal tax and no state/local corporate income taxes or similar apply.

1.7. Special tax procedure rules for associated corporations and controlled groups

For Danish income tax purposes, there are no special rules for tax audit of controlled groups as such and therefore there are no formal rules on "joint" audit for group companies to be observed. However, it should be mentioned that the statute of limitations is prolonged by two years for group transactions compared to the ordinary reassessment rules.

[32] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 11.

[33] See s. 1(10) of the draft proposal on Implementing the Anti-Tax Avoidance Directive, dated 28 May 2018 (J.nr. 2017-1461).

Companies being a part of a group are in principle audited independently. However, in practice the tax authorities normally audit the entire group at the same time or at least also audit the "group tax income" when one company is subject to a tax audit.

Group companies file their own separate tax return (often administratively handled by the administration company). This separate tax return is based on the "group taxation income", i.e. potential utilization of losses between companies, but no joint or group tax return is filed. The tax return does, however, include information on controlled transactions to be filled out. In addition, group companies should, in accordance with the OECD TP Guidelines, file a country-by-country report, master file and local file within 60 days after the deadline for filing the tax return.

Part Two: Separate entity approach and group approach in cross-border situations

2.1. Taxation of a foreign corporate entity

The approach used in classifying a foreign corporate entity is crucial for the taxation of the foreign entity. In general, at least three possible approaches exist:

1. Use the foreign civil law qualification;
2. Use the foreign tax qualification; or
3. Perform an independent Danish tax law qualification (*lex fori*).

The latter approach is applied under Danish tax law. The reason for choosing this approach in Danish tax law is mainly "equal treatment" considerations as well as general inspiration from Germany.

The approach is *firstly* to assess whether the foreign entity constitutes an opaque taxable entity and, if so, *secondly* what kind of opaque taxable entity. If the foreign entity is not considered opaque, it is considered transparent for tax purposes.

There are no precisely formulated guidelines in Danish tax law. From case law the following documents and guidelines may be highlighted in determining whether an entity is considered opaque or transparent:

– Articles of associations governing the entity;
– Form of liability for the participants and entity;
– Organizational form, including management, of the entity;
– The operation and structure of the entity; and
– Profit sharing between participants.

In short, a foreign entity is classified and taxed under the same norms that apply to a (similar) Danish entity.[34]

If the foreign entity is *not* resident in Denmark, the entity is taxed in Denmark only in relation to the following income arisen in/from Denmark:[35]

[34] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 1.

[35] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 2.

a) Income allocated to a permanent establishment in Denmark (net basis)
b) Income from real estate in Denmark (net basis)
c) Dividends paid from a Danish entity, while many exemptions do apply (gross basis)
d) Interest paid from a Danish group entity (intra-group debt), while many exemptions do apply (gross basis)
e) Income from hiring-out labor (gross basis)
f) Certain service income paid to former owners/management (net basis)
g) Royalty income paid from a Danish entity, while exemptions do apply (gross basis)
h) Capital gains on intra-group claims to a Danish group entity (intra-group debt) if the capital gain has been pre-determined (gross basis)

The statutory accounts usually form the basis for taxation, but may need to be adjusted for tax purposes.

2.2. Treatment of branches (inbound and outbound)

Denmark applies the same classification and principles of allocation of profits to both inbound and outbound branches (permanent establishments).

Profits allocated to foreign entities' Danish permanent establishments are subject to normal CIT in Denmark on a net basis as mentioned in section 2.1. Profits allocated to Danish entities' foreign permanent establishments are tax exempt in Denmark and losses are non-deductible.[36] However, this does not apply to the following income:

– Income from international shipping and air transport;
– Income allocated to a permanent establishment, where the source state has waived the right to tax the income under a DTT or similar international agreement;
– Income that would have been taxable CFC income had the permanent establishment been a subsidiary.

Denmark has implemented the AOA in relation to both foreign and domestic permanent establishments.

Income is allocated to the permanent establishment as the profits it might be expected to make if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the functions performed, assets used and risks assumed by the enterprise through the permanent establishment and through the other parts of the enterprise. However, if a DTT has been concluded between Denmark and the relevant other country in question and the article on allocation of profits is based on other principles, this allocation approach is also applied for domestic tax purposes.

Denmark has entered into approx. 70 DTTs or similar treaties according to which the source state is allowed to tax income allocated to a permanent establishment and – as a main rule – the credit method is applied. The permanent establishment is not in its own right entitled to DTT benefits, as permanent establishments are not in Denmark considered a "person who is resident of one or both of the Contracting States".

Following the ECJ's decision in the Danish case C-650/16 *Bevola*, final losses in foreign permanent establishments may be deducted in Denmark under certain conditions, i.e.

[36] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 8.

some form of Danish implementation of the "final loss doctrine".

There is no separate branch profit tax in Denmark and "distributions" of profits from permanent establishments in Denmark are also not subject to branch profit tax or anything similar.

2.3. Treatment of income from foreign subsidiaries

Income from foreign subsidiaries are taxable, unless explicitly tax exempt. The same principle applies to dividends, i.e. dividends are taxable, unless specifically tax exempt. However, capital gains and losses on shares are tax exempt/non-deductible, unless explicit rules have been enacted.

Such explicit rules have been enacted and therefore several exceptions to the theoretical starting point apply, depending on the classification of the shareholding (shares):

- "Subsidiary Shares" are generally defined as shares owned by a shareholder holding at least 10% of the nominal share capital of the issuing company.[37] Further requirements apply as described in section 1.2.
- "Group Shares" are generally defined as shares in a company in which the shareholder of the company and the issuing company are subject to Danish joint taxation or fulfill the requirements for international joint taxation under Danish law (i.e., the company is controlled by the shareholder).[38]
- "Tax-Exempt Portfolio Shares" are defined as shares not admitted to trading on a regulated market owned by a shareholder holding less than 10% of the nominal share capital of the issuing company.[39]
- "Taxable Portfolio Shares" are defined as shares that do not qualify as Subsidiary Shares, Group Shares or Tax-Exempt Portfolio Shares.

Dividends from Subsidiary Shares and Group Shares are fully tax exempt.[40] Similar, capital gains and losses on these shares are tax exempt/non-deductible.[41]

Dividends from Tax-Exempt Portfolio Shares are partly taxable – that is 70% are taxable while 30% are tax exempt.[42] However, capital gains and losses on these shares are still fully taxable/deductible.[43]

Dividends from Portfolio Shares are taxable.[44] Similarly, capital gains and losses on these shares are taxable/deductible.[45]

Taxable capital gains and deductible losses on the disposal of shares are included in the taxable income according to the mark-to-market principle. Non-listed companies, however, have a possibility to opt for taxation in accordance with the "realization principle", provided that the realization principle is applied for all non-listed shares.

[37] The Danish Act On Taxation Of Capital Gain And Losses On Claim And Debt [*Kursgevinstloven*] § 4A.
[38] The Danish Act On Taxation Of Capital Gain And Losses On Claim And Debt [*Kursgevinstloven*] § 4B.
[39] The Danish Act On Taxation Of Capital Gain And Losses On Claim And Debt [*Kursgevinstloven*] § 4C.
[40] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 13.
[41] The Danish Act On Taxation Of Capital Gain And Losses On Claim And Debt [*Kursgevinstloven*] § 8.
[42] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 13.
[43] The Danish Act On Taxation Of Capital Gain And Losses On Claim And Debt [*Kursgevinstloven*] § 9.
[44] The Danish State Tax Act [*Statsskatteloven*] § 4 and The Danish Tax Assessment Act [*Ligningsloven*] § 16A.
[45] The Danish Act On Taxation Of Capital Gain And Losses On Claim And Debt [*Kursgevinstloven*] § 9.

Group companies that are part of Danish joint taxation or that qualify for international joint taxation under Danish law may make tax-exempt group contributions.[46] A group contribution is tax exempt for the recipient if:

- the grantor and the recipient are group-related and have been group-related for a continuous period of at least one year, in which period the capital contribution must take place;
- the grantor and the recipient are subject to Danish joint taxation or are eligible for international joint taxation under Danish law;
- the receipt would not be subject to Danish taxation on dividend from the grantor, had the recipient been a parent company to the grantor; *and*
- the grantor does not have the right to deduct the capital contribution from its taxable income. A group contribution is normally non-deductible under Danish tax law.

2.4. Application of group taxation regimes to cross-border groups and DTT entitlements of groups

The mandatory Danish group taxation regime applies to all group companies resident in Denmark and permanent establishments in Denmark.[47] A group exists if a company:[48]

- has the majority of the voting rights in another company;
- is a shareholder of another company and has the right to appoint or dismiss the majority of the members of that company's management;
- is a shareholder of another company and is entitled to exercise control over that company's operational and financial management on the basis of the articles of association or of an agreement with that other company;
- is a shareholder of another company and controls the majority of the voting rights in that company on the basis of a shareholder's agreement; *or*
- is a shareholder of another company and exercises control over that company's operational and financial management.

Foreign group entities and foreign permanent establishments can also participate in the group taxation should the ultimate parent company choose so.[49] However, group taxation is then required to include all group companies worldwide as well as permanent establishments and real estate for ten years, i.e. Danish taxation of the group's worldwide income for ten years. The top Danish group entity is appointed as the administration company in the tax group and responsible for administrating the payment of taxes etc.

The separate entity principle still applies and the group taxation "only" enables group companies and permanent establishments to utilize losses from other group companies/ permanent establishments (against compensation). Group taxation means inter alia that losses of one company are set off against profits of the other companies. Losses originating from tax years before the commencement of group taxation may only be set off against profits of the same company.

[46] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 31D.

[47] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 31.

[48] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 31C.

[49] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 31A.

The group is not in itself entitled to claim DTT benefits, as that would be up to each entity.

2.5. Transfer pricing rules

Danish transfer pricing legislation was reformed in 1998. The aim of the reform was to provide a clear legal basis for transfer pricing adjustments, in order to avoid erosion of the Danish tax base and to ensure equal tax treatment of Danish and foreign-owned companies. The material transfer pricing legislation has not been changed since and is therefore (still) based on a separate entity approach with the arm's length principle as the prevailing principle.

The Danish transfer pricing legislation states that controlled transactions should be entered into on the same terms and conditions as would have been entered into by independent parties. No additional guidance follows from the law. However, it follows from the preparatory work that the Danish arm's length principle should be interpreted in line with article 9(1) of the OECD Model Tax Convention on Income and on Capital and the OECD Transfer Pricing Guidelines.[50]

With regard to Action 8-10 of the BEPS Final Reports on transfer pricing (which should now be considered a part of the OECD Transfer Pricing Guidelines) as well as the other changes to the OECD Transfer Pricing Guidelines from 2017, it is the Danish tax authorities' view that these guidelines merely constitute clarifications and elaborations of the way in which the arm's length principle is applied in practice. As such, the Danish tax authorities argue that there is no need to amend Danish law, and therefore the tax authorities have already brought their own (published) transfer pricing guidelines in line with the new OECD Transfer Pricing Guidelines.

This has been criticized in the literature, where the prevailing position is that new Danish legislation should be adopted in order to transpose the result into Danish law.[51] This argument is primarily based on the opinion that the outcome of the BEPS Final Reports and the new OECD Transfer Pricing Guidelines on "*analysis of risk in commercial and financial relations*" and "*delineation of the actual transaction*" deviate significantly from the previous guidelines, and that these new guidelines therefore constitute a material change to the arm's length principle. It is yet to be seen to what extent the Danish courts will make a strict distinction between older and newer versions of the OECD Transfer Pricing Guidelines regarding these updates.

Besides the application of the updated OECD Transfer Pricing Guidelines (at least from the tax authorities' perspective), no other tendencies exist. As such, a wider application of profit split than suggested under the OECD Transfer Pricing Guidelines, including the principles discussed under OECD BEPS Pillar 1, is not (yet) seen in Denmark.

[50] This is stated in the explanatory notes to the bill that introduced the rules back in 199 (Explanatory notes to Bill L 101 (1997/1998)).

[51] J. Wittendorff, Nyt Armslængdeprincip , SR-Skat, p. 34 et seq. (2016).

2.6. CFC regimes and separate entity approach

Denmark originally introduced CFC rules in 1995, but the CFC rules have since been revised several times. The Danish CFC rules have been somewhat aligned with the ATAD, but a lot of discussion has taken place in relation to whether a controlled foreign company that carries on a substantive economic activity should be excluded from the CFC rules.

Under the Danish CFC regime, a Danish company is liable to tax on the income of a Danish or foreign subsidiary if (i) the subsidiary is directly or indirectly controlled by the Danish company and (ii) the tainted income (CFC income) of the subsidiary exceeds 1/3 of the total taxable income under Danish tax law.[52] When assessing whether the subsidiary's income exceeds 50% income from shares in (sub)-subsidiaries resident in the same country as the subsidiary in question are disregarded and the sub-subsidiaries income are instead included in the calculations. This is to ensure that local holding companies are assessed together with local subsidiaries and not *per se* constitute a CFC subsidiary.

If the CFC rules apply, the Danish parent company must include the total income of the subsidiary corresponding to the Danish parent company's average ownership, provided that the income of the subsidiary is positive, i.e. income inclusion. A tax credit is granted for taxes paid by the subsidiary. The Danish parent company may – under certain conditions – elect only to include the CFC-income of the subsidiary.

The Danish CFC rules also apply to permanent establishments.

The scope of the Danish CFC regime for companies was expanded in 2007 to also include Danish subsidiaries following the decision of the ECJ in C-196/04 *Cadbury Schweppes*. Thus, in principle, the Danish CFC rules apply to both foreign and Danish subsidiaries. However, it has been argued that different treatment still exists, as the CFC rules only entail an additional tax burden for the Danish parent company if the subsidiary is resident in another country in which the level of taxation is lower than the Danish level of taxation.[53]

2.7. Intra-group withholding taxes or non-deductibility of outbound payments (e.g. interest-/royalty capping rules)

There are no general withholding taxes on intra-group payments, but withholding taxes may be levied on royalties as well as intra-group interest.

In general, interest payments are not subject to withholding tax in Denmark. However, interest payments on intra-group debt are subject to a withholding tax of 22%, unless:[54]

1. The interest and claim are allocated to a permanent establishment in Denmark.
2. The withholding tax is to be reduced or eliminated in accordance with the interest and royalty directive or a DTT if the group companies are associated for at least one year.
3. A Danish parent company has directly or indirectly controlled the interest-receiving company for at least one year.
4. The interest-receiving company is controlled by a parent company resident in a country which has entered into a DTT with Denmark and the company may be subject to CFC legislation of the interest (if those conditions were met).

[52] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 32.

[53] Cf. P.K. Schmidt, Are the Danish CFC Rules in Conflict with the Freedom of Establishment? – An Analysis of the Danish CFC Regime for Companies in Light of ECJ Case Law, 54 Eur. Taxn. 1, pp. 3-9 (2014), Journals IBFD.

[54] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 2 (d).

5. The interest is taxed at a level corresponding to at least ¾ of the Danish taxation (3/4 of 22%) at the hands of the direct receiving group company and this company does not on-pay the interest to another company subject to a lower taxation than ¾ of the Danish taxation (minimum taxation criteria).

In general, interest payments are deductible under Danish tax law. However, the following three interest limitation rules do apply:
(i) a thin capitalization rule;
(ii) an asset-based limitation rule; and
(iii) an EBITDA-based limitation rule.

We refer to section 1.5.2 for a description hereof.

Royalties are subject to a withholding tax of 22%, unless:[55]
1. The royalties and IP are allocated to a permanent establishment in Denmark; *or*
2. The withholding tax is to be eliminated in accordance with the interest and royalty directive if the group companies are associated for at least one year.

The withholding tax applies to industrial and commercial royalties and are often eliminated or reduced under an applicable DTT.

Royalties are deductible if considered a business expense. No special regime applies.

2.8. Scope of the application of hybrid mismatch rules

Denmark had so-called linking/hybrid rules in place prior to the OECD BEPS Project and ATAD. Accordingly, Denmark had rules on hybrid entities and payments as well as reverse hybrid entities, whereby the Danish tax treatment in some situations depended on the tax treatment in another country, for example tax planning based on US check-the-box rules.

Following OECD BEPS Action 2 and ATAD the Danish hybrid rules were amended to be similar to the hybrid rules from ATAD, including in relation to non-EU countries (ATAD 2). It is specifically stated in the bill that the OECD BEPS Action 2 reports, including the examples, are relevant in the interpretation of the Danish rules and the definitions from ATAD have been directly inserted into the wording of the Danish tax law.[56]

Consequently, the Danish hybrid rules apply to intra-group situations (situations between associated enterprises) and structured arrangements if the hybrid results in double deductions, double non-taxation or deduction/no-inclusion situations.

2.9. Scope of country-by-country reporting

As of 2016, Denmark introduced country-by-country reporting based on the recommendations set out in the OECD BEPS Action 13.[57] The content of the requirements

[55] The Danish Corporate Income Tax Act [*Selskabsskatteloven*] § 2 (h).

[56] See Bill L 28 2018-19.

[57] Tax Control Act [*Skattekontrolloven*], 1946 with later amendments, § 3B (10-16). See Bill L 46 (2015/2016).

is specified in a statutory order, and the requirements apply to groups with a consolidated turnover exceeding DKK 5.6 billion.[58]

2.10. Scope of application of other instruments

Denmark has not introduced any other national special instruments for cross-border groups such as digital services tax, diverted profit tax, BEAT, GILTI or similar. Denmark awaits the work conducted in the OECD and EU.

[58] See the tax authorities' guidelines https://skat.dk/skat.aspx?oid=2254604.

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