Tax Planning Under Pressure
22 June 2018

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General limits for tax planning

International Tax Planning

Background:

- Increasing pressure on the limits for tax planning.
  - International tendencies – BEPS, ATA etc.
  - Domestic tendencies – continuous attempts to narrow the scope of tax planning.

What is international tax planning?

- *”International tax planning is a multifaced discipline and may be defined as the lawful structuring (through the legally acceptable use of domestic tax law and tax treaties) of cross-border investments or activities with the objective of optimizing the overall tax burden and maximizing net income.”*

Includes optimization of effective tax rate (ETR) and mitigation of risks and uncertainty.

What is aggressive international tax planning?

- *”Taking advantage of the technicalities of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability.”*
- *See Commission Recommendation of 6.12. 2012 on Aggressive Tax Planning.*

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International Tax Planning

Nothing wrong in carrying out tax planning:

- Avoid double taxation
- Direct opportunities in existing tax legislation (e.g. depreciations)
- Succession on business transactions
- Effective Tax Rate in competition

This presentation excludes tax evasion and illegal tax avoidance.

Tax planning in Danish law

First lets take a look at Danish law in the context of tax planning.

- Is tax planning accepted in Danish law?
  - Clearly yes!
  - Minimizing taxes is a part of doing business.
  - Although the public opinion may suggest otherwise and although the tax authorities constantly try to limit the possibilities.
  - Taxpayers may choose among different options available and are not obliged to choose the most tax inefficient approach.

- Does a doctrine on abuse or circumvention exist?
  - This is hard to say:
    - In a few cases the principles of abuse or circumvention have been mentioned by the Supreme court.

- The doctrines of substance over form and the principle of rightful recipient do exist.
  - Difficult to distinguish and delineate.

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Tax planning in Danish law

The significance of transactions being mainly or substantially tax motivated.

- Starting point: Intent not important for tax purposes.
- Tax authorities will often try to argue that a tax motive may lead to a transaction being disregarded.
- Not supported by case law as a single criterion (SKM 2017.276 V tax motive cannot lead to reclassification).
- Thus tax motives cannot lead to reclassification but may be included in the overall analysis of the transaction at hand.

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Tax planning in Danish law

Business purpose requirement?

- Required that business reality and economic reality exists.
- Tax saving motive intensify the substance test and is a prerequisite to carry out a substance over form adjustment.
- Tax saving motive establish a presumption for tax avoidance.

Danish Supreme court approach:

- Guiding principles:
  - Legal certainty, equality, predictability and legality.
- Bona fide business transaction?
  - If yes: nothing further to scrutinize.
  - If no: substance or unintended tax benefit?
  - Official guidance on legality (1998):
    - Restrictive provisions cannot be interpreted beyond the wording or clear preparatory work.
      - If no clear statutory authority exists – this is clearly the problem of the tax authorities.
    - Is the result reasonable and expressing common sense?

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Tax planning in Danish law

Acceptable measures according to case law:

- Intra group agreements are equally justified as third-party agreements.
- Sale of shares and repurchase 2.5 months later – loss deduction accepted if real risk of value fluctuations.
- Establishment of companies in low tax countries is accepted.
- Formal company law transactions by nature express the substance of a transaction.

Tax planning in Danish law

GAAR vs. SAAR:

- Acceptable to rely on existing anti abuse provisions.
- Decisive that the legislator has determined the boundaries of what is acceptable and what is not.
- No basis to diminish the room to maneuver for tax payers even further.
  - SKM2003.482.H (Over Hold)
    - Losses carried forward – capital increase in a loss-making company in order to produce income through a loan.
    - Supreme court: Legitimate use of existing exemption in the rules regarding LCF.
  - SKM2010.26.H (Feri-lux)
    - Transfer of advertisement activity within group related parties without a written agreement.
    - Partly motivated by business reasons partly motivated by tax reasons – utilizing losses carried forward.
    - Accepted by Supreme Court.

Tax planning in Danish law

Does recent case law change the overall understanding of current law?

- SKM2016.16.H (TAKS)
  - The shareholders of a Faroese holding company (no. 1), sold all their shares in holding company no. 1 to a newly established holding company (no. 2), which they owned by the same ownership as in holding company no. 1.
  - One year later: merger.
  - Establishing the exact same structure as before with ownership of holding company no 1 – but with the shareholders having being paid for the sale of the shares in holding company no. 1.
- Supreme Court:
  - The establishment of holding company no. 2 and the transfer of the shares had no business justification.
  - Instead, the purpose was tax avoidance.
  - Based on all the facts and circumstances the Supreme Court found that the sale of the shares should be treated as taxable dividends and not as a tax exempt capital gain.

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Background and introduction

Comments:

- Danish tax authorities try to broaden the scope of the decision.
- Concerns Faroese law.
- No specific anti abuse provisions exist in the Faroe Islands.
- Clearly trying to circumvent tax legislation without changing the end-result.
- Decision seems to be written backwards.

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Generally Applicable Anti-abuse Rule (GAAR)

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EU ATAD GAAR and OECD PPT

Does the ATAD GAAR and OECD PPT change the legal situation in Denmark?

"1. For the purposes of calculating the corporate tax liability, a Member State shall ignore an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the applicable tax law, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one step or part. 2. For the purposes of paragraph 1, an arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality. 3. Where arrangements or a series thereof are ignored in accordance with paragraph 1, the tax liability shall be calculated in accordance with national law."	*"Not withstanding the other provisions of the Convention, a benefit under this Convention shall not be granted in respect of any item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provision of this Convention."*

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EU ATAD GAAR and OECD PPT

Two significant anti abuse provisions have been introduced – which are largely similar.

- EU ATAD GAAR
  - For the first time a real GAAR has been introduced aiming at all non-genuine arrangements ***domestically and in cross border situations.***
    - Applies to all taxpayers that are subject to corporate tax in one or more MS, including PEs in an EU MS.
  - Function: "to fill in gaps which should not affect the applicability of specific anti-abuse rules".

- OECD Principle Purpose Test (PPT)
  - PPT applicable when determining access to tax treaty benefits.
  - Applicable through the MLI – the most important measure in the MLI.
  - Currently 60 countries have opted for the PPT only while 12 have opted for the simplified LOB + PPT.

EU ATAD GAAR and OECD PPT

Implementation of EU ATAD GAAR:

- Legislation or doctrine (several countries will need actual implementation).
- ECJ interpretation.
- Enactment of more stringent GAAR in cross border situations may violate fundamental freedoms.

Cumulative requirements:

- *Arrangement or series thereof.*
- *Having been put in place for the main purpose or one of the main purposes (subjective).*
- *Of obtaining a tax advantage (objective).*
- *That defeats the purpose or object of the otherwise applicable tax provision.*
- *Non-genuine.*

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EU ATAD GAAR and OECD PPT

Legal effect:

- EU ATAD GAAR
  - Arrangements etc. shall be ignored for the purposes of calculating the corporate tax.
  - What does "*ignored*" mean?
    - Fully set aside, but not re-classification? – "*disregard, refuse to recognize – abusive transactions must simply be left out.*"
    - Tax liability should be calculated in a way that is in accordance with the object and purpose of the provision that was circumvented.

- OECD PPT:
  - A benefit under a tax treaty shall not be granted.

EU ATAD GAAR and OECD PPT

Arrangement or series thereof (similar)

- Broadly defined: transaction, plan, action, operation, agreement, understanding, promise, understanding or undertaking.
- Arrangements regarding: establishment, acquisition or maintenance of a person who derives the income, including the qualification of that person as a resident of one of the Contracting States, and includes steps that persons may take themselves in order to establish residence.

Having been put in place for the main purpose or one of the main purposes (subjective)

- EU ATAD GAAR:
  - Not required that sole purpose. Not even a *"dominant, principal, essential or main purpose".* Instead sufficient that one of the main purposes was to obtain a tax benefit.
  - No guidance regarding main and partial purpose.
    - *"a given purpose is to be considered essential where any other purpose that is or could be attributed to the arrangement or series of arrangements appears at most negligible, in view of all the circumstances of the case."*
- OECD PPT:
  - Seemingly identical interpretation.
  - Includes situations where different objectives arise- as long as the tax motive was a significant purpose.
- Rather low threshold

EU ATAD GAAR and OECD PPT

Of obtaining a tax advantage (objective).

- Tax advantage: comparison of tax payable without the arrangement in place.
- Obtaining a tax advantage is not per se non-genuine – taxpayer has the right to choose the most efficient structure for its commercial affairs.

That defeats the purpose or object of the otherwise applicable tax provision.

- Reference to domestic law and the purpose and object of the part of domestic law in question.
- Not always easy to determine (unclear or ambiguous purpose).

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EU ATAD GAAR and OECD PPT

"Non-genuine"

- Not put into place for valid commercial reasons, which reflect economic reality.
- Preamble: *"GAARs should be applied to arrangements that are not genuine:* ***otherwise the taxpayer should have the right to choose the most efficient structure for its commercial affairs".***
- **Not genuine = artificial?**
  - Possibly to be interpreted with a reference to domestic tax law on substance over form.
- Valid commercial reasons: concept involving more than the attainment of a purely fiscal advantage (Leur Bloem).
- Having regard to all facts and circumstances.
  - What are relevant facts and circumstances?

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EU ATAD GAAR and OECD PPT

Tax authorities should carry the burden of proof in applying both provisions

- Impression that this will be somewhat underemphasized.
- Unfortunate that tax administrations should make such assessments on the basis of unclear notions.
- Risk of arbitrary and varying practices among MS.

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Limitations from ECJ case law

In recent case the ECJ has interpreted the previous PSD anti abuse provision, which set up general guidelines for the EU MS to follow.

Case C-06/16 (Eqiom)

- French implementation rule regarding PSD Art. 1(2), denied access to the PSD is the ultimate parent was a resident outside the EU.
- ECJ: The actual French rules was not in accordance with Art. 1(2) or the freedom of establishment.
  - The French rule introduced a general presumption of abuse when the ultimate parent company was resident outside the EU
  - Unproportional
  - Restriction which could not be justified

C-504/16 (Deister Holding) and C-613/16 (Juhler Holding)

- German rule somewhat similar the French rule in Eqiom.
- EStG § 50d (3): objective requirements => if not fulfilled then no access to reduction or reclaim of German WHT on dividends.
  - ECJ: In conflict with EU law to deny benefits without the authorities having to demonstrate any proof of abuse.
  - The objective German requirements could not lead to a presumption of abuse.

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Limitations from ECJ case law

Cadbury-Schweppes is still the leading case to determine abuse:

- *"purely artificial arrangement, which does not reflect the economic reality"*

In particular on holding companies:

- Holding activities per se do not support that abuse takes place.
- The abuse test requires that a concrete total assessment is made of the situation at hand, concerning the organizational, economic and other features of the group to which the parent company belongs, and this structure and strategy of this group.

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Mandatory Intermediary Reporting

The European Commission's proposal on mandatory intermediary reporting was adopted by the EU on 13 March.

A new era of enhanced corporation regarding aggressive tax planning.

- Reporting by taxpayers or their advisors is mandatory from 1 June 2019
  - Under the Directive, the advisor providing the reportable tax advice must disclose the arrangement.
    - NB! If the advisors are bound by confidentiality or is located outside the EU the reporting obligation shifts unto the taxpayer.

The Directive is based on BEPS Action 12 and as such ensures a compatible implementation of the envisioned BEPS initiative on a EU-wide basis.

What must be reported?

The Directive sets forth certain conditions as to what and when arrangements must be reported:

- Terminologically the Commission have settled on ”hallmarks” the presence of which triggers mandatory reporting.
- Significant hallmarks include:
  - Acquiring loss making companies – using losses in order to reduce tax liability
  - Cross-border payments to a recipient resident in a no-tax or low-tax country;
  - Jurisdictions involved with inadequate or weakly enforced anti-money laundering legislation;
  - Setups aiming to avoid reporting income as required under EU transparency rules;
  - Direct correlation between the fee charged by the intermediary and what the taxpayer will save in tax avoidance;
  - Deductions for the same depreciation on an asset are claimed in more than one jurisdiction (“Double Dips”);
  - Relief from double taxation obtained for the same income or capital in more than one jurisdiction.

Timing and sanctions

”Hallmark” arrangements must be reported at the earliest of:

- thirty days after the day that the arrangement is made available,
- when the arrangement is ready for implementation, or
- after the first step of the arrangement has been implemented.

To the extent reporting is not done, the entity responsible for reporting the arrangement will be met with sanctions.

- Sanctions are as of yet unclear, and will be determined by the individual Member States.
  - However: *”Member States must ensure that effective and dissuasive penalties are put in place for intermediaries who fail to meet these reporting requirements.”*

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Final Remarks

1. Tax planning is definitely under pressure and the limits are being pushed.

2. GAARs will change existing principles and broaden the scope.

3. Review of MNE’s tax strategies.

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Overview of tax treatment of capital gains vs. dividends

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Capital gains vs. dividends

Type of share	Danish investor companies		Foreign investor companies	
	Capital Gains	Dividends	Capital Gains	Dividends
Shares acquired in a trade or business	Taxable	Taxable unless Group- or Subsidiary Shares	Tax exempt	Taxable unless Group- or Subsidiary Shares
Subsidiary Shares	Tax exempt	Tax exempt	Tax exempt	Tax exempt if covered by PSD/DTA
Group Shares	Tax exempt	Tax exempt	Tax exempt	Tax exempt if covered by PSD/DTA and recipient is resident in the EU/EEA
Tax exempt portfolio shares	Tax exempt	Taxable on 70% of gross amount	Tax exempt	Taxable
Portfolio shares	Taxable	Taxable	Tax exempt	Taxable

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Liquidation proceeds (sec. 16 A)

- Main rule (capital gains):
  - Taxed as sale of shares.

- Relevant exceptions (dividends):
  - If the recipient owns at least 10 % of the share capital and is taxable on dividend payments (SEL § 2).
    - Residents in a non-EU/EEA and a non-DTA country.

  - If the recipient has less than 10% ownership but controlling influence (LL § 2) and is taxable on dividend payments (SEL § 2)
    - Does not encompass situations in which the recipient is resident in the EU/EEA and withholding tax is reduced or waived as a result of the PSD or a DTA (to the extent the shares had been Subsidiary Shares).

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Liquidation proceeds (sec. 16 A)

Relevant exceptions (dividends) - continued:

- The shareholder owns tax exempt portfolio shares in the company under liquidation, *and*
  - at least 50% of the assets in the liquidated company consists either directly or indirectly of Subsidiary-/Group Shares, or
  - Within three years preceding the liquidation, Subsidiary- or Group Shares have been transferred to the direct or indirect shareholders or to another Group company.

- Liquidation proceeds received in the income year prior to the calendar year in which the company is ultimately dissolved.
  - Possible to obtain a dispensation.
  - Shareholders engaged in trading, which meet the requirements for receiving tax exempt dividends (Subsidiary- and Group Shares) -> capital gains.

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Capital reduction (sec. 16 A)

Main rule (dividend):

- Distributions correlated with a capital reduction is taxable as a dividend payment if the company is not under liquidation.
  - Background: To secure tax neutrality in relation to dividend taxation.

Exceptions (capital gains):

- Permission (Only in correlation with a decrease in activity, i.e. narrow scope).
- Trading shareholders which meet the criteria for receiving tax exempt dividends (Subsidiary- and Group Shares).

Sale to the distributing company (sec. 16 B)

Main rule (dividend):

- Background:
  - To secure tax neutrality in relation to dividend taxation.

Relevant exceptions (capital gains):

- Employee shares (conditional on sale to the employer company)
- Share buy-backs by companies under liquidation in the year it is ultimately dissolved, unless:
  - Same exemptions as under liquidation proceeds apply.
- Dispensation

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Sale to the distributing company (sec. 16 B)

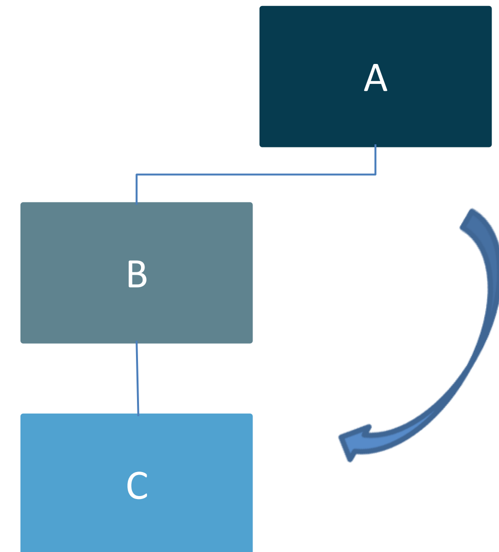
Share buy-backs

- The definition of dividends furthermore encompasses the situation in which the company buying back the shares is a subsidiary of the distributing company.

- Subsidiary:
  - Controlling influence, cf. Sec. 2(2) of the Tax Assessment Act, and
  - Directly or indirectly owns more than 10% of the shares.

- The following is thus encompassed:
  - Company A sell shares in B to another company C
  - If B has controlling influence on C

- The purchase price is treated as dividend
  - Regardless of the place of residence of the seller
  - Regardless of whether the subsidiary is Danish or foreign



Sale and re-purchase

Sale and re-purchase (”dividend stripping”)

- The difference between the sale and re-purchase price is taxable as dividends if:
  - Sale of tax exempt portfolio shares.
  - The sale price is higher than the re-purchase price.
  - Additional tax exempt portfolio shares are acquired within 6 months after selling shares in the same company.
  - The company has distributed dividend during the ”non-ownership” period.

- Example (Bill 49)
  - Portfolio shares acquired at price 100. Value of the shares before the distribution of dividends is 150 and the shares are sold at 150. Dividends of 50 are distributed (to the new shareholder), after which the shares are re-purchased at 100.
  - Taxable dividend of 50.

- Problems with the rule (NB! Only unlisted shares)
  - Wide scope
  - Is not limited to the distributed dividend
  - Is not limited to Danish residents for tax purposes

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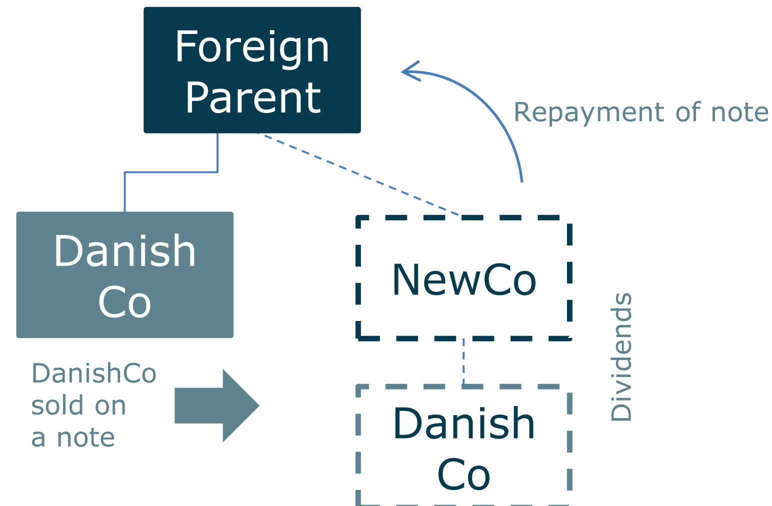
Overview - SEL § 2 D

Anti-avoidance rule *intended* to prevent circumvention of WHT on dividends.

- Scope much broader…



- Transfer of shares.
  - Intra-group transfer
  - Transfer to an ”empty” company
  - Restructurering

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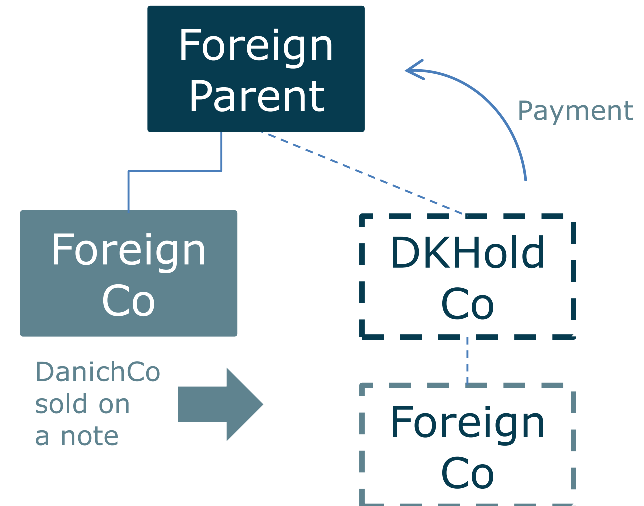
Intra-group transfer

Requirements:

1. A legal person transfers
2. shares in a group company (prior and after)
3. to a group company (after)
4. and the remuneration fully or partly consists of anything other than shares in the buyer or a group company of the buyer.



Consequence:

- The non-share remuneration is reclassified to a dividend distribution.

Does not apply if:

- The seller could receive tax exempt dividends from target prior to transfer according to Danish tax rules (SEL § 2/13)

Transfer to an ”empty” company

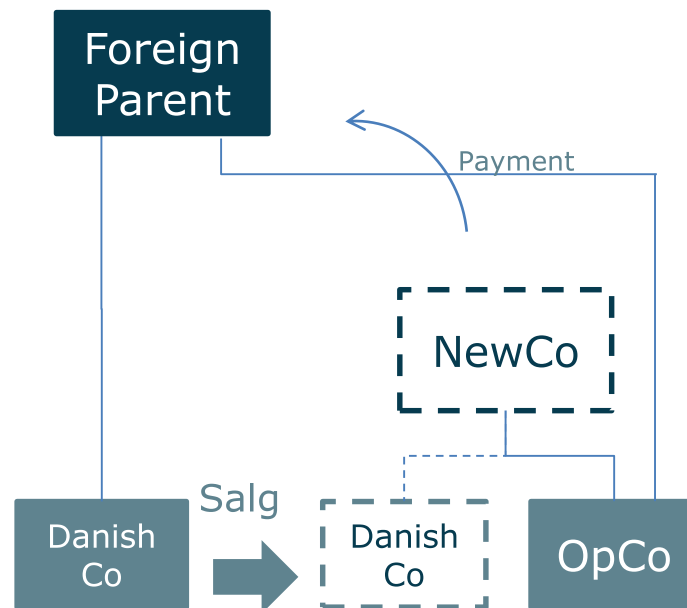
To prevent minority shareholders to circumvent Danish WHT on dividends….

Requirements:

1. A legal person transfer shares in a company
2. to a company without any commercial activities *and*
3. the remuneration:
   - partly consists of anything other than shares in the buyer or a group company of the buyer *or*
   - fully consists of anything other than shares in the buyer or a group company of the buyer, but the seller owns shares in the buyer or a group company of the buyer

Consequence:

- The non-share remuneration is reclassed to a dividend distribution.



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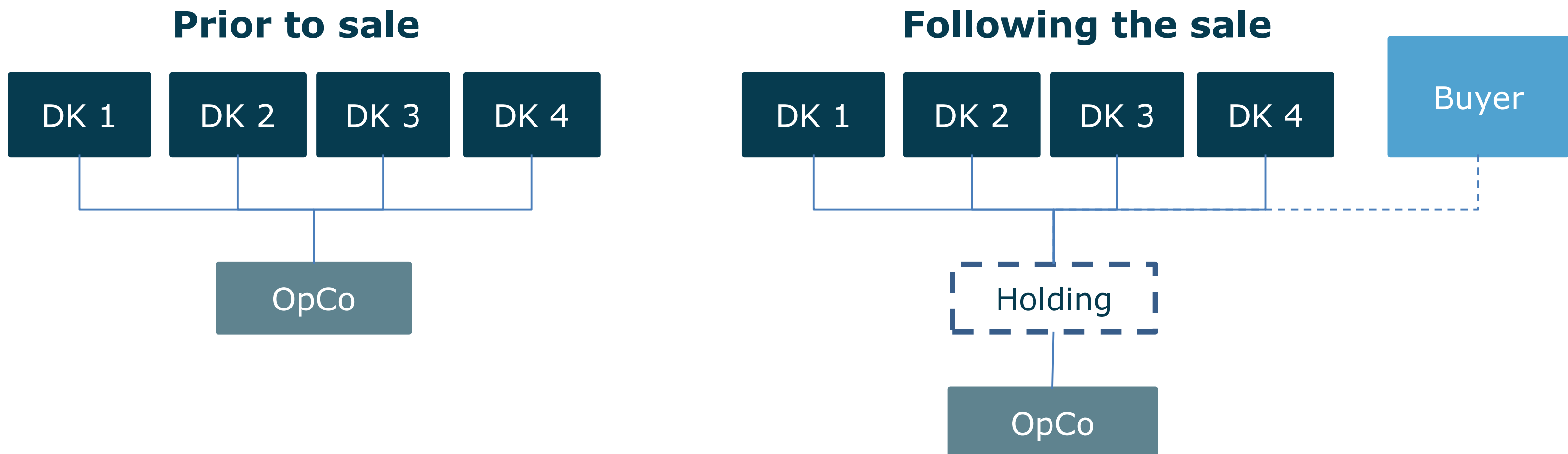
Example

OpCo is to be sold and the buyer establishes a holding company to debt finance etc.

The buyer wants the original owners to re-invest some/a small part of the sales proceeds to share the risk and therefore receives shares in Holding.



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Restructuring

”2 D” situations in certain restructurings…

- Cash payments in taxable mergers and divisions.
  - If the shareholder owns shares in the transferring company or a group company hereof.

- Cash payments in non-taxable mergers, divisions and exchange of shares (incl. cross-border).
  - If the shareholder owns shares in the transferring company or a group company hereof.

Taxation and Withholding Obligation?

”Dividend” from buyer to seller.

- Buyer must be liable to tax in Denmark to be liable to withhold taxes.
- Seller must also be liable to tax in Denmark (resident/source)
  - SEL § 2 D only reclassify the payment
  - SEL § 2 refer to LL § 16 A (regular dividend definition) – not SEL § 2 D…
  - The withholding obligation in KSL § 65 does not refer to SEL § 2 D…

What would the Supreme Court say…

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Tax Treaty Issues

OECD MC

- *Income can only be taxed in the state of residence, unless specifically mentioned in other provinsions.*

- *Capital gains can only be taxed in the state of residence.*

- *Dividends can also be taxed in the source state.*
  - *The buyer is the source*
  - *Is it dividends according to OECD MC?*

The term "dividends" as used in this Article means income from shares, "jouissance" shares or "jouissance" rights, mining shares, founders' shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident.

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Thank you for the attention!

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