Analysis: Canada – Denmark Income and Capital Treaty

See treaty text

Type of Treaty: Income and Capital
Model on which based: OECD
Signed: September 17, 1997
Entry into force: March 2, 1998
Effective date: January 1, 1999
Subsequent Protocol signed: September 17, 1997
Entry into force of Subsequent Protocol: March 2, 1998
Effective date of Subsequent Protocol: January 1, 1999
Second Protocol signed: July 7, 2009 (exchange of information)
Entry into force of Second Protocol: TBA

This Analysis was updated in August 2011 by **Arne Riis**, Partner, Bech-Bruun, Copenhagen, Denmark and in December 2011 by **Jim Wilson**, Partner, Gowling Lafleur Henderson LLP, Canada.

Article 1 Personal Scope

See treaty text

Persons who are residents of one or both States.

Article 2 Taxes covered

See treaty text

Taxes on total income, or on elements of income or capital;
Taxes on gains from alienation of movable or immovable property;
Taxes on total amounts of wages and salaries;
Capital gains taxes; and
Wealth taxes

As well as application to the taxes existing at the time the Treaty was signed there is a provision applying the Treaty to any identical or substantially similar taxes which are imposed after the date of signing of this Treaty.

Denmark

Income taxes to the state (statslig indkomstskat (bund-, mellem-, topskat));
Municipal income tax (kommunal indkomstskat);
Church Tax (kirkeskat);
Since 2008: labour market contribution (AM-bidrag)
Health contribution (sundhedsbidrag)
Share income tax (aktieindkomstskat)
CFC tax (CFC-skat);
Pension yield tax (pensionsafkastskat);
Hydrocarbon Tax (kulbrinteskat); and
Property value tax (ejendomsværdiskat).

As well as any identical or substantially similar taxes which are subsequently imposed in addition to, or in place of, the existing taxes.

Canada

In the case of Canada, the Canada-Denmark Income Tax Convention only applies to taxes imposed by the Government of Canada under the Income Tax Act and does not apply to taxes imposed by political subdivisions and local authorities. Canada's reservation on that portion of paragraph 1 of Article 2 of the OECD Model stems from the decision in Attorney-General for Canada v. Attorney-General for Ontario where the court found that the federal government has no constitutional ability to bind the legislative authority of the Canadian provinces by treaty.

However, as a practical matter, those Canadian provinces that are covered by a collection agreement" with the federal government are required to use the same income base as calculated for federal tax purposes. This means that any change to the income base of a taxpayer for federal tax purposes that occurs because of the operation of a provision of a tax treaty also results in an identical change to the income base for provincial or territorial tax purposes. As a result, Canada's tax treaties indirectly apply to the income taxes covered by collection agreements. The provinces not covered by a collection agreement often have provisions in their provincial income tax acts that generally take into account the provisions of Canada's tax treaties.

Canada does not consider social security taxes, such as Employment Insurance (EI) and Canada Pension Plan (CPP), or consumption taxes, such as the Goods and Services Tax (GST), to qualify as income taxes for purposes of the federal tax credit.

- The general income tax which applies to individuals, corporations and trusts;
- Withholding Taxes on Passive Income Paid to Non-Residents.

Article 3 General Definitions

See treaty text

"Canada": The territory of the Kingdom of Canada (see also Article 2 of the First Protocol).
"Denmark": The Kingdom of Denmark including any area outside the territorial sea of Denmark, within which Denmark may exercise, under its law and in accordance with international law, rights with respect to the exploration and exploitation of the natural resources of the Continental Shelf; the term does not include the Faroe Islands and Greenland.
"Person": An individual, company and any other body of persons, and in the case of Canada the term also includes a trust.
"Company": Any body corporate or any entity which is treated as a body corporate for tax purposes.
All terms not specifically defined take their meaning from domestic tax law.
"National": Any individual possessing the nationality of either State or any legal person, partnership and association or other entity deriving its status as such from the law in force in one of the States
"International traffic": means any transport by a ship, aircraft or vehicle operated by an enterprise in a Contracting State, except when the ship or aircraft is operated solely between places in the other Contracting State.
Any terms not defined take their meaning from the law of the State concerned at the time. Meanings specific to tax law take precedence over other meanings.

Expert Analysis:

Denmark

In Denmark "competent authority": The minister of taxation. In matter relating to international taxation, authority has been delegated to "SKAT", the Danish administrative tax authorities.

Canada

Canada's tax conventions define the Canadian Competent Authority as the Minister of National Revenue or the Minister's authorized representative. Administratively, the Canadian Competent Authority function is split between the International Tax Directorate and the Legislative Policy Directorate of the CRA. The Director, Competent Authority Services Division,
International Tax Directorate serves as the Canadian Competent Authority for resolving cases, such as the examples listed in paragraph 11, related to specific taxpayers. Requests for competent authority assistance in respect of specific cases and related enquiries may be sent to:
Canada Revenue Agency
Director, Competent Authority Services Division International Tax Directorate
Compliance Programs Branch
5th floor, 344 Slater Street
Ottawa ON K1A 0L5 T
he Director General, Legislative Policy Directorate, is the Canadian Competent Authority for issues involving general interpretation, non-discrimination, treaty shopping, double non-taxation issues, and general issues concerning the application of tax conventions where specific taxpayers are not involved. Requests for competent authority assistance in respect of these non-specific case issues may be sent to:
Canada Revenue Agency
Director General Legislative Policy
Directorate Policy and Planning Branch
22nd floor, Tower A Place de Ville
320 Queen Street
Ottawa ON K1A 0L5
"Competent Authority": Canada's domestic tax system does not define terms such as "enterprise" or "national". However, it does have a broad definition of "business" to include "a profession, calling, trade, manufacture or underrating of any kind whatever".

Article 4 Fiscal Domicile

See treaty text

"Resident" means any person who is liable to tax in one of the Contracting States by reason of his domicile, residence, place of management or any other criterion of a similar nature.
Being liable to taxation only because of a source of income or capital in a State does not by itself result in "residency".

Where by reason of the provisions of Article 4 a person other than an individual or a Company is a resident of both Contracting States, the competent authorities of the Contracting States shall by mutual agreement endeavour to settle the question and to determine the mode of application of the Convention to such person. In the absence of such agreement, such person shall not be entitled to claim any relief or exemption from tax provided by this Convention.

Canada

In order to be a "resident of a Contracting State" for the purposes of the relevant tax treaty, a person must be "liable to tax" in that State by virtue of a criterion referred to in the residence article of that treaty.

Based on the Supreme Court of Canada decision in *The Queen v. Crown Forest Industries Ltd et al* ("Crown Forest"), it is Canada's position that, to be considered "liable to tax" for the purposes of the residence article of Canada's tax treaties, a person must generally be subject to the most comprehensive form of taxation as exists in the relevant country. In the case of Canada, this generally means full tax liability on worldwide income.

Canada has adopted the view that being liable to comprehensive taxation does not necessarily mean that the person must actually pay tax to the jurisdiction in question. In situations where a person's worldwide income is subject to a Contracting State's full taxing jurisdiction but that State's domestic law does not levy tax on a person's taxable income or taxes it at low rates, Canada will generally accept that the person is a resident of the other Contracting State unless the arrangement is abusive (e.g. treaty shopping). In other words, as confirmed by the Supreme Court of Canada in Crown Forest, the determination of residency for the purposes of a tax treaty remains a question of fact.

Residence: Individuals

In the case of individuals apparently resident in both Contracting States, the usual tiebreaker tests apply:

- He will be deemed to be a resident of the State in which he has a permanent home. If he has a permanent home in both States, he will be deemed to be resident in the State with which his personal and economic relations are closer (centre of vital interests).

- If unable to determine the State where the centre of vital interests lies, then he is a resident of the State in which he has a habitual abode.

- If he has a habitual abode in both States, then he is a resident of the State of which he is a national.

- If a national of both States or of neither of them, then the competent authorities must settle the question by mutual agreement.

Expert Analysis:

Denmark

According to sec. 1(1) of the Danish Tax at Source Act (kildeskatteloven), tax liability on its global income applies to (i) persons who are resident in Denmark, (ii) persons without Danish residence who stay on Denmark for at least six months, (ii) Danish nationals employed on vessels which with home port in Denmark, unless it is substantiated that they are tax resident outside of Denmark, and (iv) Danish nationals, who are civil servants deployed for duty abroad. Tax liability under (ii) applies as of the initiation of the stay in Denmark. However, persons visiting Denmark as tourists or students, who remain liable to tax in their home State and are not carrying on business in Denmark will only be considered as tax residents if the stay exceeds 365 days within a 2 year period.

Residence in a foreign State for foreign tax purposes does not preclude residence in the Denmark for Danish tax purposes. Dual residence, often resulting in double taxation of the individual's worldwide income, is generally resolved under the terms of an applicable tax treaty. When a Danish tax resident individual moves out of Denmark, the individual will generally still under Danish domestic law be considered tax resident in Denmark as long as he/she or his/her family still has a house suitable for year-round residence. A house owned by the Danish emigrant will generally be considered as being available unless it is let out on a lease which is not terminable for at least 3 years.

Canada

A person who is resident in Canada during a taxation year is subject to Canadian income tax on his or her worldwide income from all sources.

The term "resident" is not defined in the Income Tax Act ("ITA"). However, the Canadian Courts have held "residence" to be "a matter of the degree to which a person in mind and fact settles into or

maintains or centralizes his ordinary mode of living with its accessories in social relations, interests and conveniences at or in the place in question."

Factual Residence - Subsection 250(3) of the ITA

Subsection 250(3) of the ITA provides that, "[i]n the Act, a reference to a person resident in Canada includes a person who was at the relevant time ordinarily resident in Canada." The Canadian Courts have held that an individual is "ordinarily resident" in Canada for tax purposes if Canada is the place where the individual, in the settled routine of his or her life, regularly, normally or customarily lives. In determining the residence status of an individual, all of the relevant facts in each case must be considered, including residential ties with Canada and length of time, object, intention and continuity with respect to stays in Canada and abroad.

The residential ties that will almost always be significant for the purpose of determining residence status are the individual's:

(a) dwelling place(s);
(b) spouse or common-law partner; and
(c) dependants.

Generally, secondary residential ties must be looked at collectively in order to evaluate the significance of any one such tie. Therefore, it would be unusual for a single secondary residential tie with Canada to be sufficient in and by itself to lead to a determination that an individual is factually resident in Canada. Secondary residential ties that will be taken into account in determining the residence status of an individual are:

(a) personal property in Canada (e.g. furniture, clothing, automobiles and recreational vehicles);
(b) social ties with Canada (e.g. memberships in Canadian recreational and religious organizations);
(c) economic ties with Canada (e.g. employment with a Canadian employer and active involvement in a Canadian business, and Canadian bank accounts, retirement savings plans, credit cards, and securities accounts);
(d) landed immigrant status or appropriate work permits in Canada;
(e) hospitalization and medical insurance coverage from a province or territory of Canada;
(f) a driver's license from a province or territory of Canada;
(g) a vehicle registered in a province or territory of Canada;
(h) a seasonal or leased dwelling place in Canada;
(i) a Canadian passport; and
(j) memberships in Canadian unions or professional organizations.

Other residential ties that have been considered in determining the residence status of an individual, but are generally of limited importance except when taken together with other residential ties, include:

(a) retention of a Canadian mailing address, post office box, or safety deposit box;
(b) personal stationery (including business cards) showing a Canadian address;
(c) telephone listings in Canada; and
(d) local (Canadian) newspaper and magazine subscriptions.

Deemed Residence- Subsection 250(1) of the ITA

Where an individual has not established sufficient residential ties with Canada to be considered factually resident in Canada, he or she may still be deemed to be resident in Canada for tax purposes by virtue of subsection 250(1) of the ITA.

Paragraph 250(1)(a) of the ITA deems an individual to be resident in Canada for the entire taxation year if he or she sojourned in Canada for a total of 183 days or more in the calendar year. To "sojourn" means to make a temporary stay in the sense of establishing a temporary residence, although the stay may be of very short duration. It is a question of fact whether an individual who is not resident in Canada is "sojourning" in Canada. An individual is not automatically considered to be "sojourning" in Canada for every day (or part day) that the person is present in Canada. The nature of each particular stay must be determined separately. Any part of a day is considered to be a "day" for the purpose of determining the number of days that an individual has sojourned in Canada in a calendar year.

Residence: Companies

If a company appears resident in both States, e.g. because one determines residence according to the place of legal incorporation and the other according to place of management then it will be deemed resident in the State where its place of effective management is located.

Domestic law

Denmark

All companies taxable under sec. 1 of the Danish Corporate Income Tax Act (CITA)(selskabsskatteloven) are considered as Danish taxable corporate entities. This list primarily entails, "aktieselskaber" (A/S) and "anpartselskaber" (ApS), which are required to be registered in the Danish Commerce and Companies Agency (Erhvervs- og Selskabsstyrelsen). Further, companies and cooperatives with similar corporate characteristics as the above company types and which have a Danish tax resident management will be considered as taxable in Denmark. Management will normally be considered as resident in Denmark if Denmark is the seat of the daily management. This would generally be the seat of management rather than the board of directors. However, if the board of directors take very active part in the daily management decisions, the venue of the board may depending on the circumstances be considered as the seat of management for tax purposes. In all other cases than aktieselskaber and anpartselskaber, it is recommendable to obtain local advice.
As a noticeable potential exception to the rule that the above entities are considered to be taxable entities, sec. 2A of the CITA provides that if any of the above entities are considered to be tax transparent under foreign tax law to the effect that income in such Danish entity is taken into account in foreign income, then the otherwise taxable corporate entity is for Danish tax purposes considered tax transparent and potentially not protected by the tax treaty. The reclassification rule is an anti-abuse rule aimed at the US check-the-box rules to avoid creating a possibility of double-dip of primarily financing expenses in both Denmark and the US, but it applies equally to other rules with the same effect.

Canada

Paragraph 250(4)(a) generally deems a corporation incorporated in Canada to be resident in Canada throughout a taxation year.
The Canadian courts have held that a corporation is resident where its "central management and control" is located. Central management and control usually refers to the exercise of power and control by the board of directors of a corporation. The location of central management and control is a question of fact. In determining the central management and control of a corporation, all surrounding factors must be evaluated, including the following:
(a) location of meetings of board of directors;
(b) degree of independent discretion exercised by the board of directors; and
(c) relative influence and power that its Canadian directors exercise as compared with foreign directors.
Canada has entered a reservation on paragraph 3 of Article 4 of the OECD Model, which reserves the right to resolve cases of dual residence of corporations based on the place of incorporation or organization rather than the place of effective management. Canada is of the view that there is uncertainty about the proper application of the common law concept of the place of effective management with the diversity of modern business operations because an examination of all of the relevant facts and circumstances needed to determine the place of effective management is complex and the conclusions drawn from that examination are often contentious. In Canada's view, the most serious defect of this concept is the fact that it is not difficult to shift central management and control from one jurisdiction to another.
As Canada has not been successful in negotiating a departure from the OECD formulation with Denmark, paragraph 3 does not specify a tie-breaker test for corporations and leaves the question of residence for treaty purposes up to the competent authorities to settle on a case-by-case basis.

Partnerships and fiscally transparent enterprises

There are no definitions given in the Treaty as to which bodies may be treated as transparent. Article 3 merely states that the term "company" designates any body corporate or any entity which is treated as a body corporate for tax purposes. To the extent that an entity comes under the Treaty definition of "company" its residence is to be determined in the same way as described for companies.

Domestic law

Denmark

Partnerships are not comprised by sec. 1 of the Danish CITA and therefore generally not recognised as separate taxable entities.
A partnership is either a general partnership (interessentskab (I/S), a limited partnership (kommanditselskab (K/S) or partnerselskab / kommanditaktieselskab (P/S)). The general partnership is the ordinary form of commercial partnership, all partners being jointly and severally liable for the partnerships' debts and obligations. Under current Danish law, a partnership is not a separate legal entity, but is transparent with respect to its (tax) liability. A general partnership is normally not subject to taxation; instead, the individual partners are taxable on their share of the partnership's profits.

With respect to a K/S, separate rules for the tax treatment (transparent or non-transparent) apply. A K/S generally has partners having limited liability (limited partners) and one or more partners having unlimited liability (general partners).
A limited partner (kommanditist or stille deltager) is liable only to the extent of his capital contributions or commitments. Under Danish corporate law, it is a requirement that the general partner (komplementaren) has both administrative and economical rights in the K/S.
A P/S is a limited partnership where all limited shares are divided into actual shares. The affairs of the P/S are, however, governed by the Danish Corporate Act, despite being transparent for tax purposes.
As a noticeable exception to the rule that the above entities are considered to be tax transparent, sec. 2C of the CITA provides that if there are participants in an otherwise tax transparent entity (or a permanent establishment in Denmark) which are resident in a state which considers the entity to be a taxable entity or in a state which does not have a tax treaty or information exchange treaty with Denmark, and such participants hold more that 50 percent of the votes or the capital in the entity/permanent establishment, the entity/permanent establishment will be considered a separate taxable entity for Danish tax purposes. The reclassification rule is an anti-abuse rule aimed at the US check-the-box rules to avoid creating a "reverse hybrid" and thereby the possibility of double non-taxation in a situation where Denmark would (without this rule) consider income to be earned by the partnership participants, while the jurisdiction where the partners are resident would consider the same income as earned by the partnership.
With respect to foreign entities, whether or not they are treated as taxable or transparent depends on how closely they correspond to the abovementioned Danish partnership forms. If they are significantly different then the general test is that an entity will be considered taxable if none of the participants have unlimited liability for the debts and obligations of the enterprise. In practise another significant criteria has been whether or not the entity has its own corporate bodies (board of directors or management).

Canada

In Canada's view, a partnership is not a legal entity that is separate and apart from its partners and is not treated as a separate person liable to tax under the ITA. Canada treats partnerships as "fiscally transparent" or "look-through" entities. The partnership income is first computed "as if the partnership were a separate person resident in Canada" according to paragraph 96(1)(a) of the ITA and then apportioned among the individual partners based on their shares in the partnership according to paragraph 96(1)(f) of the ITA.

Article 5 Permanent Establishment

See treaty text

This Article defines the term "permanent establishment". The profits of an enterprise of one of the Contracting States can only be taxed on an arising basis in the other Contracting State to the extent that they are attributable to a permanent establishment in that other State.
This Treaty broadly uses the OECD definitions. Two types of permanent establishment are set out: A fixed place of business and a dependent agent.
Fixed place of business
A fixed place of business through which the business of the enterprise is wholly or partly carried on will constitute a permanent establishment. The list of types of establishment particularly included are the usual ones:

- A place of management;
- A branch;
- An office;
- A factory;
- A workshop;
- A mine, an oil or gas well, a quarry or any other place of extraction of natural resources; and
- Building sites, construction, installation or assembly projects will constitute a permanent establishment if they last more than 12 months.

According to the OECD Commentary, a "fixed place of business" means to be established at a distinct place with a certain degree of permanence, however, it could be a pitch in a market place, or even part of the premises of another enterprise. There is no requirement that the premises be owned. The Commentary offers the example of an employee of Company A who is allowed to use an office at the premises of Company B. This could create a permanent establishment for Company A in the country of Company B if the arrangement persists for long enough and if the employee is carrying out activities which are more than merely "preparatory or auxiliary" (see below).
The OECD considers that to be fixed, a place of business must be at a specific geographic point. However, if the permanent establishment consists of mechanical equipment only, then there is no requirement for mechanical equipment to be fixed to the soil.
As to what constitutes a reasonable period of time to give the necessary degree of permanence, most countries will not consider a presence of less than six months to give rise to a fixed place.
The usual exclusions from the definition of permanent establishment are given so that the following will not constitute a permanent establishment:
(a) The use of facilities solely for the purposes of storage, display or delivery of goods or merchandise belonging to the enterprise;

(b) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;

(c) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

(d) The maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or for collecting information, for the enterprise; and

(e) The maintenance of a fixed place of business solely for the purpose of carrying on any other activity of a preparatory or auxiliary character.

(f) The maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

To apply this Article, it is necessary to be able to make a distinction between functions that are core to a business and those that are merely preparatory or auxiliary. What constitutes core functions will vary from one business to the next. However, any fixed place of business from which the business is partly managed will constitute a permanent establishment even if its functions otherwise appear to be preparatory or auxiliary. Also, if services are rendered to other companies within the corporate group or to third party customers then this would not be preparatory or auxiliary because activities only count as preparatory or auxiliary if they are carried on "for the enterprise" itself.

Agency permanent establishment

Dependent agents may constitute a permanent establishment. Where a person acting on behalf of a resident of a Contracting State has, and habitually exercises, in a Contracting State an authority to conclude contracts in the name of the resident, that resident is deemed to have a permanent establishment in that other State, unless the activities of the agent are limited to those listed in (a)-(f) above. Where the activities of the agent are merely preparatory or auxiliary, or where the agent is an independent agent (e.g. a general commission agent acting in the ordinary course of his business) the presence of the agent will not give rise to a permanent establishment.
The fact that a company has a subsidiary in the other Contracting State does not mean that the subsidiary is a permanent establishment of that company, unless it binds the parent company in contract as per the rule for dependent agents. This rule applies generally to groups of companies.

Domestic law

Denmark

The Danish domestic law definition of a permanent establishment is more or less identical to the definition under Article 5 of the OECD Model Tax Convention. A number of decisions have been made by the Danish tax authorities and Danish courts considering the existence of a Danish permanent establishment.
In sec. 2(5) of the CITA and sec. 2(9) of the Danish Source Tax Act (kildeskatteloven), however, a specific provision excluding the existence of a permanent establishment in the event of "distance

selling". Hereunder, a permanent establishment in Denmark shall not be deemed to exist for a foreign principal, even if a Danish tax resident representative as such has power of attorney to bind the foreign principal, when carrying out distance selling. Distance selling shall for the purpose of these provisions mean the passive receipt of orders from Danish or foreign customers via telephone, telefax, telex, EDI, internet, mail or similar. However, it is further a condition that (i) the representative is not employed with the principal and that (ii) neither the foreign principal not any of his/her close relatives or a group related entity of the principal carries out business activities which has ties to the activities of the representative.

Canada

The term "permanent establishment" is defined in the Income Tax Act strictly for provincial income tax purposes. Otherwise the term has no relevance for federal tax purposes. Accordingly, Canada's domestic definition of "permanent establishment", as that term is found in Canada's tax treaties, is based on the OECD Model Commentary and Canadian jurisprudence.

The official CRA views on PE determinations are generally consistent with the OECD Model Treaty and its Commentary on Article 5, which, as per the general rule in paragraph 1 of Article 5 ("General PE Rule"), establishes three key conditions:

i) There must be a place of business ("1st PE criteria").

ii) The place of business must be fixed ("2nd PE criteria").

iii) The non-resident must be carrying on his business wholly or partly through this fixed place of business ("3rd PE criteria").

There have been several Canadian court cases dealing with the meaning of a "permanent establishment" under one of Canada's tax treaties, but the following analysis examines recent Canadian jurisprudence.

Recent Canadian Jurisprudence

In 2008, the Tax Court of Canada ("TCC") simultaneously released the decisions of *Knights of Columbus v. The Queen* ("Knights of Columbus") and *American Income Life Insurance Co. v. Canada* ("American Income Life Insurance"). Both cases dealt with a determination of whether the appellant had a permanent establishment (PE) in Canada as a result of carrying on its business through a fixed place of business in Canada and the TCC's decision in both cases was highly dependent on whether the place of business was "at the disposal" of the enterprise. In both cases, the TCC held that the non-resident company did not have a PE in Canada.

In *Knights of Columbus*, the issue of the General PE Rule was to be determined by considering the 3rd PE criteria relating to whether the business of the parent was being carried on through this fixed place of business (i.e. in the context of this article, the subsidiary's office). The Knights of Columbus' insurance business was handled through agents. In Canada, there were general agents who were not actively involved in selling insurance products to members of the Knights of Columbus; instead, they earned income from a commission override from the field agents and were responsible for recruiting, training, and managing the field agents. The field agents did the front-line work of soliciting applications for sales of Knights of Columbus' insurance products from members. The field agents typically conducted business from their home offices but usually met with clients at the clients' homes. The Knights of Columbus had no access to their home office nor was there anything there that would indicate a connection with the Knights of Columbus.

Justice Miller concluded the following in response to expert testimony:

For the Field Agents' residences to be considered fixed places of business of the Knights of Columbus, the Knights of Columbus must have a right of disposition over these premises. A right of disposition is not a right of the Knights of Columbus to sell an agents' house out from under him. The Knights of Columbus might be viewed as having the agents' premises at its disposal, for example, if the Knights of Columbus paid for all expenses in connection with the premises, required that the agents have that home office and stipulate what it must contain, and further required that clients were to be met at the home office and in fact the Knights of Columbus' members were met there.

And later, at paragraph 80:

The Knights of Columbus make no operational decisions at the Field Agent's premises. The Knights of Columbus had no officers, directors or employees even visit the agents' home offices, let alone have any regular access. All risks connected with carrying on business at the home offices are borne by the agents themselves. The agents are not carrying on the Knights of Columbus' core business from these premises. Their premises cannot therefore be found to be a fixed place of business permanent establishment.

In *American Income Life Insurance*, Justice Miller provided the following list of factors to be considered in determining whether the parent's business was being carried on from the fixed place of business:

- Use of premises by parent;
- Control by parent over premises;
- Legal right to exercise control over premises;
- Degree to which premises identified with parent business;
- Who paid for expenses of premises;
- Who paid for equipment used at premises;
- Who made management decisions;
- What contracts were concluded from premises;
- What parent products were kept on premises;
- Did parent have any Canadian employees;
- Who bore the risk of the operation from premises;
- How many principals were represented by the agent; and
- Were agents subject to detailed instructions or comprehensive control.

Article 6 Income from immovable property

See treaty text

The general rule is that income derived by a resident of a Contracting State from immovable property in the other State may be taxed in that other State. Thus, for instance, if a resident of one State owns a building in the other State and receives rent, that rent may be taxable in the other State.

This treatment also applies to income from immovable property used by an enterprise and to income from immovable property used for the performance of independent personal services.

Immovable property is defined as per the domestic law of the State in which the property is located but it will include livestock and equipment used in agriculture, forestry, general property rights and rights for the working of natural resources.

Expert Analysis:

Denmark

Under Danish domestic law, profits from sale of real estate specifically comprises capital gains under the Danish Capital Gains on Property Tax Act (ejendomsavancebeskatningsloven) and recaptured tax depreciation under the Danish Tax Depreciation Act.

Danish tax law generally provides for possibility of deducting financing costs on real estate/property under the same circumstances in income and profit thereon as Danish owners of property/real estate. However, in administrative practise it has been determined that for tax purposes it is only possible to allocate financing costs corresponding to debt financing of 80 percent of the value of the real estate to the Danish real estate for Danish tax purposes. Further, foreign currency exchange gains and losses on real estate financing are not deemed to be allocable to the Danish real estate for Danish tax purposes.

Canada

Under subsection 212(1) in Part XIII of the Income Tax Act ("ITA"), every non-resident must pay a 25% withholding tax on every amount, such as rental income from immovable property, that a resident pays or credits to the non-resident. However, under section 216 of the ITA, the non-resident can elect to file a income tax return under Part I instead of paying the Part XIII withholding tax. Part I income will be net income as opposed to gross income to which Part XIII applies, such that expenses like financing costs and property taxes can be deducted from the rental income from immovable property when the section 216 election is made.

Article 7 Business profits

See treaty text

Only profits actually arising from a permanent establishment may be taxed by the source State. If an enterprise has both a permanent establishment in a State and also derives other income, say,

dividends, royalties or interest unconnected with the permanent establishment, then the dividends or interest may only be taxed in accordance with Articles 10 and 11 of the Treaty and not this Article.
"In the case of permanent establishment consisting of construction or assembly sites, only the profits which result from the actual construction or assembly activities are taxable by the State in which the permanent establishment is located. That State is not permitted to attribute additional profits to the permanent establishment on the basis of delivery of merchandise or equipment, whether by the head office or a different permanent establishment of the enterprise."
Generally, the profits to be attributed to the permanent establishment are the profits that would be expected if the permanent establishment was a distinct and separate enterprise. The starting point for the computation of profits will be the branch accounts, assuming they exist.
The OECD, in 2008, published its final report on the attribution of profits to permanent establishments (July 17, 2008) and updated the Commentary on Article 7 of the Model Treaty. When interpreting a tax treaty, it is generally agreed that the latest version of the OECD's Commentary on the Model Treaty should be used. These notes follow the 2008 version of the Commentary. The "authorised OECD approach" to attributing profits to a permanent establishment now requires that there is a two step process.
Firstly, a functional and factual analysis should be carried out, along the lines set out in the OECD's transfer pricing guidelines, to establish the economically significant activities and responsibilities undertaken by the permanent establishment. This will involve establishing the rights and obligations arising out of transactions between the permanent establishment and third parties, e.g. the sales revenue arising from independent customers generated by the permanent establishment as opposed to by the head office. If the permanent establishment takes the form of a factory, then it would assume the obligation to pay for the raw materials which it uses. The OECD then recommends that "significant people functions" relevant to the attribution of economic ownership of assets are identified to support the attribution of economic ownership of assets of the enterprise to the permanent establishment. Economic ownership is defined as the right to income from an asset or the right to depreciate it. Tangible property should be attributed to the location where it is in use. Economic ownership of intangibles rests with the location in which the risks associated with the intangibles is borne: For instance, if an enterprise owns a patent for a particular drug which is sold by distributor companies in many countries, the economic ownership would rest in that part of the enterprise responsible for commissioning the research to develop the drug and which would bear the losses if medical trials failed. A further set of "significant people functions" are then to be identified: this time, those relevant to the assumption of risks so that an allocation of risks borne by the enterprise can be made to the permanent establishment. For instance, road building equipment may be economically owned by a permanent establishment in Country A but the head office, located in Country B, may have the power to determine on which road building projects the equipment is used and hence the head office bears the risk associated with profits or losses arising from the equipment. The more risks that are managed by the permanent establishment, the higher the share of the profit of the enterprise to be attributed to it. The OECD's 2008 Report looks for the place of active decision taking rather than mere "rubber stamping". Note that no such distinction between asset management and risk assumption functions are required in the case of enterprises in the financial sector, because it is considered highly likely that these functions would be carried out by the same people.
Secondly, taking into account the picture built up in the functional and factual analysis, the profits of the permanent establishment must be determined. Although this is relatively simple in the case of transactions with third parties, transactions and dealings with other parts of the enterprise must be determined using the rules laid down in the OECD's Transfer Pricing Guidelines. This means that goods and services provided by head office must carry an arm's length mark up. Pricing policies should be properly documented, which in practice may prove troublesome as firms may not take the same care in documenting the terms of transactions within the firm as they would with third parties. In determining the profits attributable to the permanent establishment, part of the enterprise's interest costs on its borrowings should be allocated to the permanent establishment. The amount of capital needed to support to functions carried out by the permanent establishment on the assumption that it is a separate entity must be calculated. Then, this total theoretical capital must be broken down into debt and equity (or "free capital" in OECD terms). The greater the risks undertaken by the permanent establishment, the higher the proportion of its notional capital that will be regarded as "free capital". Several methods of establishing the split between "free capital" and debt capital are suggested, including the use of thin capitalisation practices in the State in which the permanent establishment is located. Once the amount of notional debt capital has been determined, an allocation of the enterprise's interest liabilities can be made to the permanent establishment. Note that only actual

interest liabilities can be allocated. If the enterprise as a whole has paid no interest to external lenders, then there can be no allocation of interest liability to the permanent establishment. The only exception to this rule is where the permanent establishment is involved in treasury dealings with other parts of the enterprise. Whilst this may well be the case in banking enterprises, it would be unusual in other enterprises. Generally, the interest rates used and the terms of the notional loans to the permanent establishment must be such as would be found between parties dealing at arm's length.
When deciding what transactions should be recognised between the permanent establishment and other parts of the enterprise, the OECD recommends that the only internal transactions which can be recognised in arriving at the permanent establishment's profits are those which relate to real and identifiable events. These would include the physical transfer of goods, the provision of services, the use of intangibles and the transfer of financial assets. Whilst the internal records (e.g. the branch accounts) are the starting point for identifying these transactions, the true test is whether there has been an internal dealing of economic significance. The OECD's 2008 report suggests the following tests are used when considering whether an internal dealing should have any effect on the profits of a permanent establishment:

- Is the documentation consistent with the economic substance of the internal dealings?

- Are the arrangements such that they are not too different from dealing which one group company might have with a fellow group company? For instance, credit periods should be similar in similar circumstances.

- Are the dealings consistent with the OECD principles for attributing profits to permanent establishments?

Allocations of head office expenses, e.g. for strategic management or centrally managed support functions such as payroll may be set against the profits of the permanent establishment, but the arm's length principle must be observed.

The allocation of profits to dependent agent permanent establishments

A dependent agent is not part of the taxpayer enterprise and will file his tax returns independently. Normally the enterprise will make payments to the agent for his services. The question is: Should the host State merely tax the profits of the agent (the "single taxpayer approach") or should there be an additional charge on the enterprise which is using the services of the agent? The amount of the charge would depend on the excess of the enterprise's profits over the amount paid to the agent which was attributable to the activities of the agent. For instance, a dependent agent may be paid for the sales he procures on a commission bases, but the selling enterprise may make a profit on those sales even after taking into account the (arm's length) commission paid to the agent. The OECD recommends that States should always consider whether the enterprise has made a profit in respect of business transacted via the agent which is in excess of amounts paid to the agent. Hence the host State may tax both the dependent agent and the foreign enterprise.
As is usual, no profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.
The same method of attribution is to be used year by year unless there is good and sufficient reason to the contrary.

Domestic law

Denmark

The definition of a PE for Danish domestic law purposes as well as the allocation of profits thereto generally follows that of the OECD Tax Model Convention. A number of decisions consider the existence of a PE and allocation of profits thereto for Danish tax purposes, most of which are based on actual circumstances. Sec. 2 of the Danish Corporate Income Tax Act (selskabsskatteloven) specifically states (i) that permanent establishment building and construction sites which constitute a permanent establishment are considered as established on the first day thereof (ii) that shares can be allocated to a permanent establishment if such shares constitute a part of the core capital of the PE (iii) that profits and losses as well as recaptured depreciation on the sale of goods allocable to the PE is taxable in Denmark. As a significant exception to the main rule that a PE is from a Danish tax perspective considered to be a separate entity, a Danish supreme court ruling from 1993 determined that "interest" payments from a Danish PE to its head office on a "loan" granted to the PE would not be tax deductible for the PE.
Sec. 8 of the Danish Corporate Income Tax Act lies down a territorial principle for certain corporate activities as it states that if a Danish enterprise has a permanent establishment abroad Denmark will

exempt income allocable to such permanent establishment abroad, unless (i) the state in which the PE is located waive its right of taxation under a tax treaty with Denmark or other international agreement, (ii) income in the PE would have been taxable under Danish CFC tax rules if the PE had been a company, or (iii) the income in the PE is income from the operation of ships or aircraft in international traffic.

Canada

Canada does not have any reservations or observations on Article 7 of the OECD Model and generally abides by the OECD Model Commentary to Article 7. Canada does not apply a "force of attraction" principle in attributing income to a permanent establishment (PE) (i.e. the right to tax of the Source State does not extend to profits that the enterprise may derive from the State otherwise than through the PE.) Under the Canadian tax system, non-residents are generally liable for Canadian tax and must file tax returns in Canada if they carry on business in Canada, subject of course to treaty relief under Article 7. A non-resident generally carries on business in Canada if he or she engages in any business activity, solicits orders, or offers anything for sale in Canada.

Article 8 Shipping and air transport

See treaty text

This provision relates to income derived from the operation of ships, aircrafts or vehicles in international traffic. The Treaty provides that profits derived by an enterprise of a Contracting State from the operation of ships or aircraft in international traffic shall be taxable only in that State The terms "transport by a ship" or "operation of ships" means the operation of a ship on a voyage by voyage basis. The same applies where the enterprise has an agency in the other State for the transportation of goods or persons, but only in direct connection with shipping, aircraft or road-transportation. For purposes of the Treaty, the term "international traffic" is defined in Article 3, par 1(h).

Notwithstanding the provisions of paragraphs l and 2 and of Article 7, profits derived from the operation of ships used principally to transport passengers or goods exclusively between places in a Contracting State may be taxed in that State.

With respect to profits derived by the Danish, Norwegian and Swedish air transport consortium, known as the Scandinavian Airlines System (SAS), the provisions of paragraphs 1 and 3 shall only apply to such part of the profits as corresponds to the shareholding in the consortium held by SAS Denmark A/S, the Danish partner of Scandinavian Airlines System (SAS).

Article 9 Associated enterprises

See treaty text

This Article contains the usual OECD provisions regarding transfer pricing. Associated enterprises must adopt the arm's length principle in their dealings with each other, and to the extent that they do not, a Contracting State may make an upwards adjustment to taxable profits.

There is no specific provision for the other State to make a corresponding downwards adjustment in taxable profits.

The position regarding "secondary adjustments" is not dealt with. If one State makes an upwards adjustment of taxable profits and the other makes an exactly equal corresponding downwards adjustment, then the tax revenues of the two States might still be different to what they would have been had arm's length pricing been applied in the first place. This is because higher profits in the State where the upwards adjustment took place might well have given rise to higher dividends or interest payments, on which withholding taxes might have been chargeable. So even though the State making the upwards adjustment has retrieved the tax deficit on the enterprise resident there, it has still not retrieved any deficit in withholding taxes. Whether it makes a secondary upwards adjustment to make good this deficit in withholding tax receipts depends on whether this is provided for in domestic law. If it does so, then double taxation will be the result which will not necessarily be relieved by the normal treaty Article on elimination of double taxation and it may be necessary to invoke the mutual agreement procedure.

According to article 9 (3) a Contracting State shall not change the income or profits of an enterprise in the circumstances referred to in paragraph l after the expiry of the time limits provided in its national laws and, in any case, after six years from the end of the year in which the income or profits which would be subject to such change would have accrued to an enterprise of that State. And the provisions of paragraphs 2 and 3 shall not apply in the case of fraud, wilful default or neglect.

Denmark

Under Danish domestic law, transfer pricing rules as well as transfer pricing documentation rules apply which provide that Danish taxable persons and PEs in Denmark which carry out business transactions

with group related entities are treated for tax purposes as if such transactions are carried out at arm's length. The definition of group related transactions is relatively wide under Danish tax law as it applies to transactions with a party, which controls or is controlled by another party. “Control” means direct or indirect legal ownership of more than 50 % of the shares or legal control over more than 50 % of the voting rights. Ownership or control has not been conferred from a pledgor to a pledgee solely as a result of a pledge over shares.
When determining whether a party controls the Danish borrower (or vice versa), votes and shares held by group-related entities are considered. Votes and shares held by non-related shareholders may also be considered if an agreement has been made between a party and non-related shareholders for the purpose of “exercising a common controlling influence” over the Danish borrower. A shareholders agreement may in this context constitute an agreement to “exercise common controlling influence” over the other party.
Not only taxable legal entities are considered as entities for purposes of control; also fiscally transparent entities may be considered if they are “are governed by rules of corporate law, a corporate law agreement or Articles of association”.
“Group related” means two or more entities which (i) directly or indirectly are controlled by the same group of shareholders or (ii) which are under common management.
Two parties may be considered to be group related by virtue of common management if they have the same manager or if they have different managers that have entered into an agreement providing for a common management of the lender and the borrower.
In determining an arm's length price the approach taken in the OECD transfer pricing guidelines is generally applied.

Canada

Canada's domestic tax laws have a comprehensive transfer pricing regime that abides by the arm's length principle and applies to transactions between non-arm's length persons.
Canada's treaty policy is to attempt to negotiate a time limit to raise upward transfer pricing adjustments (e.g. see article 9(3)). The reason behind this policy is that Canada has books and records retention laws that are not indefinite and Canada will not be on the hook to provide correlative relief for an open-ended time period. See Canada's reservation on Article 25 of the OECD Model.

Article 10 Dividends

See treaty text

This Treaty provides for rates of withholding tax on dividends below those which may be charged in the absence of any agreement between the two countries.
This Treaty in Paragraph 2, provides that maximum withholding tax rates are to be:
5% where the recipient owns at least 25% of the paying company's share capital; and
10% where the gross amount of the dividends if the dividends are paid by a non-resident owned investment corporation that is a resident of Canada to a beneficial owner that is a resident of Denmark and that holds directly or indirectly at least 25 per cent of the capital of the Company paying the dividends; and
15% in other cases.
To enjoy the Treaty rates of withholding tax the recipient must also be the beneficial owner of the dividends. This is an anti-treaty shopping measure.
Paragraph 3 defines the term “dividends” to include income from shares, jouissance shares or jouissance rights, mining shares, founders' shares or other rights to participate in profits. Also included is other income subjected to the same tax treatment as income from shares under the domestic laws of a State. Jouissance shares or rights are financial instruments which grant rights of the types enjoyed by shareholders but which, in some jurisdictions, are viewed as debt rather than equity.
Paragraph 4 provides that where, say, a Canadian company receives a dividend from a Danish company, and that dividend is effectively connected with a permanent establishment which the Canadian company has in Denmark, then the dividend income will be deemed to be part of the income of the permanent establishment and the provisions of Article 7 and Article 14 will apply.
Paragraph 5 contains the usual provision that a State does not have the right to levy any tax on a dividend unless either the dividend is paid by a resident company or received by a resident shareholder. Thus the fact that a dividend paid by, say, a Canadian company may be sourced from profits earned by a permanent establishment which that Canadian company has in Canada, does not give Canada any taxing rights over that dividend, unless of course, it is received by Canadian shareholders.

Paragraph 6 provides that any provision of this Convention, a Company which is a resident of a Contracting State and which has a permanent establishment in the other Contracting State shall, in accordance with the provisions of the law of that other State, remain subject to the additional tax on companies other than corporations of that other State, but the rate of such tax shall not exceed 5 per cent.

Domestic law

Denmark

Individuals

The distribution of dividends from a Danish company to a non-resident individual is generally subject to withholding tax at the rate of 28% (27% as of 2012). The shareholder may seek a refund from the Danish tax authorities of the tax withheld in excess of 15%. In practise this is done by completing and filing ready print reclaim form 06.003 (available online at www.skat.dk) with the Danish tax authorities (Skattecenter Ballerup), which must contain a statement from the Canadian tax authorities that the beneficial owner of the payment is resident in Canada.

If the shareholder (in aggregate with shareholders group related to the shareholder) holds less than 10% of the nominal share capital in the Company and the shareholder is tax resident in Canada, the final tax rate is 15%.

In addition it is possible for the Danish Securities Centre or the dividend distributing company to enter into an arrangement with the Danish tax authorities according to which the obligation to withhold tax is reduced to the tax rate stipulated in the double taxation treaty with the relevant State.

Companies, etc.

Dividends from subsidiary shares (i.e. shares which constitute at least 10% of the share capital in the issuing company) are exempt from Danish withholding tax provided the taxation of dividends is to be waived or reduced in accordance with the Parent-Subsidiary Directive (90/435/EEC) or in accordance with the Treaty. Further, dividends from Group Shares (i.e. share in a company in which the shareholder of the company and the issuing company are subject to Danish tax consolidation or fulfill the requirements for international tax consolidation under Danish law) are exempt from Danish withholding tax provided the company investor is a resident of the European Union or the European Economic Area and provided the taxation of dividends should have been waived or reduced in accordance with the Parent-Subsidiary Directive (90/435/EEC) or in accordance with a tax treaty with the State in which the company investor is resident had the shares been Subsidiary Shares.

Dividends from Portfolio Shares (i.e. shares which are not Group Shares or Subsidiary Shares) will be subject to taxation irrespective of ownership period.

Dividend payments on Portfolio Shares will be subject to a withholding tax of 28% (27% as of 2012) irrespective of ownership period. The final tax may be reduced pursuant to the Treaty. If the shareholder holds less than 10% of the nominal share capital in the Company and the shareholder is tax resident in Canada, the final tax rate is 15%, also under Danish domestic law. In practise reclaim of Danish withholding tax is done by completing and filing ready print reclaim form 06.003 (available online at www.skat.dk) with the Danish tax authorities (Skattecenter Ballerup), which must contain statement from the Canadian tax authorities that the beneficial owner of the payment is resident in Canada. According to a statement from the Danish ministry of taxation in 2000 the Danish tax authorities will confirm that also pension funds and investment funds are considered as tax residents in Denmark, irrespective of the fact that they do not pay corporate tax on their income.

Beneficial ownership

Until recently, the requirement of beneficial ownership (and the content of this term) - although formally existing under the Danish withholding tax rules - has not been subject to real attention from the Danish tax authorities and still no clear guidance on the application thereof by the Danish tax authorities currently exist. However, the Danish Supreme Court has confirmed that specific provisions of Danish tax treaties should generally be interpreted in accordance with the OECD Commentary (to the extent applicable). The tax authorities have also referred to the OECD Commentary whenever (vaguely) commenting on the concept of beneficial ownership.

Relief under EU law (the EU directives 90/435 and 03/49)

The parent/subsidiary directive does not contain any beneficial ownership provisions. Instead, Article 1 of the parent/subsidiary directive contains a general abuse exception according to which protection under the Dividend Directive may be denied pursuant to domestic or agreement-based (e.g. treaty-based) anti-abuse provisions. We believe that the general anti-abuse exception in Article 1 with almost certainty will be held to reflect the general principle in EU law that abuse of rights is prohibited and that instruments of EU law cannot be extended to cover abusive practices.

Article 1 of the interest and royalty directive sets out a beneficial owner condition. Article 1(4) explains that the receiving company shall be treated as the beneficial owner only if it "receives those interest payments for its own benefit and not as an intermediary, such as an agent, trustee or authorised signatory, for some other person." Beyond this, the interest and royalty directive contains no definition of the concept of beneficial ownership and we have not identified any instruments of EU law which operate with the concept in any way that seems relevant to the interest and royalty directive. It would seem that beneficial ownership is a novel concept in EU law. Thus, the specific meaning of the concept of beneficial ownership in the context of the interest and royalty directive must be held to be uncertain. It will be for the European Court of Justice (ECJ) to determine specifically what it means.
It is conceivable that the ECJ would interpret both the beneficial owner condition and the general anti-abuse exception in light of its extensive case law dealing with abusive practices. Further, it is conceivable, based on the abuse test as it stands after Cadbury Schweppes, that the ECJ would not accept an allegation of abuse under the parent/subsidiary directive or the interest and royalty directive unless it can be established by objective verifiable factors that :
1. The structure has only been established for the purpose of escaping Danish dividend withholding tax; and
2. the establishment of the structure constitutes a "wholly artificial arrangement" which does not reflect a "genuine economic activity" carried out in the residence State of the shareholder.
On 16 March 2010 the Danish Tax Tribunal (Landsskatteretten) published a long awaited ruling on beneficial ownership which found in favour of the tax payer in a structure put in place by certain non-Danish private equity funds which had acquired a Danish company by using a Danish-Luxembourg acquisition structure with a Luxembourg top holding company. On distributing dividends to the Luxembourg no Danish tax was withheld on dividends. The dividends were subsequently reinvested by the Luxembourg company by extending a loan to the dividend distributing company, which was ultimately reinvested into the Danish company acquired. The Tax Tribunal stated that the requirement of beneficial ownership is from a Danish perspective applied as an anti-abuse measure. However, as the dividend payment to the Luxembourg company was in the case At hand not paid on to the shareholders therein, the company could not be considered as a flow-through entity and as such would qualify as the beneficial owner of the dividend. As a result, the dividend distributing company was correct in not withholding tax on the dividend paid to the Luxembourg company.

Canada

Paragraph 2 of the OECD Model provides for a lower rate of tax if the beneficial owner is a company that directly holds at least 25% of the capital of the company paying the dividends. However, the OECD Commentary expressly allows Contracting States to agree to a lower holding percentage in cases where the parent company's State of residence grants exemption to a company for dividends derived from a holding of less than 25%. This is the case in Canada as the foreign affiliate rules in the Income Tax Act apply where there is a holding of 10% or more. Accordingly, a large number of Canada's tax treaties contain a minimum 10% holding.
Canada reserves the rights to expand the definition of "dividends" in paragraph 3 of the OECD Model to cover certain interest payments which are treated as distributions under its domestic law.
Canada also entered a reservation on paragraph 5 of Article 10 of the OECD Model, which reserves the right to impose its branch tax on the earnings of a company attributed to a permanent establishment situated in these countries and also reserves the right to impose this tax on profits attributable to the alienation of immovable property situated in Canada by a company carrying on a trade in immovable property.

Individuals, Corporations and Trusts

All dividends paid by a corporation resident in Canada to a non-resident of Canada, whether the non-resident shareholder is an individual, corporation or trust, is subject to a Part XIII withholding tax of 25%, on the gross dividend, subject to tax treaty relief.

Beneficial ownership

The Canada Revenue Agency (CRA) has found that it can sometimes be difficult to determine who the true beneficial owner is, particularly in complex scenarios where the transactions are largely motivated by tax planning.
Prevost Car Inc. v. The Queen was the first Canadian tax case on beneficial ownership in the context of a treaty shopping scenario using a conduit company. In this case, the Canada Revenue Agency (CRA) took the position that a Netherlands holding company was not the "beneficial owner" of dividends paid to it by its Canadian subsidiary for purposes of the reduced rate of withholding under the Canada-Netherlands tax treaty. The Court found in favour of the taxpayer being the "beneficial owner".

Article 11 Interest

See treaty text

This Article deviates from the OECD Model Convention.

Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

According to Article 11(2) such interest may also be taxed in the Contracting State in which it arises and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed 10 per cent of the gross amount of the interest.

Notwithstanding the provisions of paragraph 2:

(1) Interest arising in a Contracting State and paid to a resident of the other Contracting State who is the beneficial owner thereof shall be taxable only in that other State to the extent that such interest:

(a) Is a penalty charge for late payment;

(b) Is paid by the central bank of a Contracting State to the central bank of the other Contracting State; (

c) Is paid with respect to indebtedness in connection with the sale on credit by a resident of that other State of any equipment, merchandise or services, except where the sale or indebtedness was between associated enterprises within the meaning of Article 9, paragraph l a) or b); or

(d) Is paid to a person which was constituted and is operated exclusively to administer or provide benefits under one or more pension, retirement or other employee benefits plans provided that:

(i) Such person is generally exempt from tax in the other State; and

(ii) The interest is not derived from carrying on a trade or a business or from a related person.

(2) Interest arising in a Contracting State and paid in respect of indebtedness of the government of that Contracting State or of a political subdivision or local authority thereof shall, provided that the interest is beneficially owned by a resident of the other Contracting State, be taxable only in that other State.

(3) Interest arising in Denmark and paid to a resident of Canada shall be taxable only in Canada if it is paid in respect of a loan made, guaranteed or insured, or a credit extended, guaranteed or insured by the Export Development Corporation; and

(4) interest arising in Canada and paid to a resident of Denmark shall be taxable only in Denmark if it is paid in respect of a loan made, guaranteed or insured, or a credit extended, guaranteed or insured by the Eksportkreditrådet or by such lending institution as is specified and agreed in letters exchanged between the Contracting States. Interest is defined as debt-claims of every kind that are not classed as dividends by virtue of Article 10, whether or not secured by mortgage and whether or not carrying the right to participate in the debtor's profits. The term includes income from government securities, bonds and debentures and premiums and prizes attaching to these securities as well as other bonds and debentures. It includes almost all items treated as interest under a State's domestic law. The term “interest” does not include income dealt with in Article 10. There are the usual provisions such that interest received by a non-resident but which relates to a permanent establishment, which that non-resident has in the other Contracting State, is taxed under Article 7 and thus escapes withholding tax. Also, interest paid by an enterprise, which is borne by a permanent establishment, is deemed to arise in the State in which the permanent establishment is situated. Hence, if the permanent establishment and the recipient are in the same State, no withholding tax can arise.

As is usual under the Model Conventions, there is a provision limiting the treaty benefit to an arm's length amount of interest where there is a special relationship between the payer and the beneficial owner.

Domestic law

Denmark

No withholding tax applies to interest paid to individuals whether resident inside or outside EU/EEA.

No Danish withholding tax will apply on interest paid from a Danish corporate entity to a person or entity which does not qualify as a controlling or group related entity foreign lender (subject to definition, cf. below).

Interest paid from a Danish corporate entity to a controlling or group related entity foreign lender will be subject to Danish withholding tax, unless:

a) the foreign controlling or group related lender has a permanent establishment in Denmark to which such interest income is attributed (in this case the interest is subject to normal corporate tax in Denmark - also at 25 percent) or

b) the foreign controlling or group related lender is entitled to claim reduction or elimination of Danish withholding tax under the Interest and Royalty Directive (no tax is levied and no withholding tax applies) and the relationship with the Danish borrower is upheld for an minimum period of 1 year, or
c) the foreign controlling or group related lender is protected under a tax treaty with Denmark (irrespective of treaty rate) and the relationship with the Danish borrower is upheld for an minimum period of 1 year, or
d) the foreign controlling or group related lender is controlled (as defined under the Danish tax consolidation rules) by a Danish entity, or
e) the foreign controlling or group related lender is controlled by a party resident in a State that has concluded a tax treaty with Denmark, and further that such State may tax the related foreign lender (specifically defined) on such interest payments pursuant to CFC taxation rules of that State, or
f) the foreign controlling or group related lender can demonstrate that it has paid foreign income tax on the interest received at a rate of at least 18.75 percent (2011) and further provided that it has not entered into a back-to-back loan with an entity that has paid foreign income tax on the interest received at a rate of less than 18.75 percent (2011)
In order to qualify for reduction or elimination of withholding tax under a tax treaty or the Interest and Royalties Directive, it is a general requirement that the recipient qualifies as beneficial owner of the interest. Reference is made to the specific comments made on the Danish interpretation of this term under Article 10, above.
For purposes of the Danish interest withholding tax rules, "control" means direct or indirect legal ownership of more than 50% of the shares or legal control over more than 50% of the voting rights. Ownership or control has not been conferred from a pledgor to a pledgee solely as a result of a pledge over shares.
When determining whether the lender controls the Danish borrower (or vice versa), votes and shares held by group-related entities are considered. Votes and shares held by non-related shareholders may also be considered if an agreement has been made between the lender and the non-related shareholders for the purpose of "exercising a common controlling influence" over the Danish borrower. A shareholders agreement may constitute an agreement to "exercise common controlling influence" over the Danish borrower.
Not only taxable legal entities are considered as entities for purposes of control; also fiscally transparent entities may be considered if they are "are governed by rules of corporate law, a corporate law agreement or Articles of association".
"Group related" means two or more entities which (i) directly or indirectly are controlled by the same group of shareholders or (ii) which are under common management.
The lender and the Danish borrower may be considered to be group related by virtue of common management if they have the same manager or if they have different managers that have entered into an agreement providing for a common management of the lender and the borrower.
Not only taxable legal entities are considered as entities for purposes of group relation; also fiscally transparent entities may be considered if they are "are governed by rules of corporate law, a corporate law agreement or Articles of association".
In practise, no filing claims apply to be exempt from withholding tax if the recipient is not group related with the borrower or if the recipient can claim exemption pursuant to b) or c), above. In the cases d)-f) a 25 percent tax is to be withheld at source and the recipient will need to reclaim the withholding tax by completing reclaim form 06.026 with the tax authorities enclosed with such documentation which substantiates eligibility for exemption under the relevant exception.. According to a statement from the Danish ministry of taxation in 2000 the Danish tax authorities will confirm that also pension funds and investment funds are considered as tax residents in Denmark, irrespective of the fact that they do not pay corporate tax on their income.

Canada

Canada's Part XIII withholding tax regime (i.e. 25% withholding on passive income) was recently amended to exempt all arm's length interest paid to non-residents from withholding tax (i.e. it is now 0%). In Canada's tax treaty network, Canada was initially one of the States that sought a maximum withholding tax rate of 15% or higher and many of Canada's older tax treaties provide for a maximum rate of 15%. Canada's more recent treaties include a 10% maximum rate.
However, as a consequence of the 5th Protocol, the Canada-US Treaty now has a 0% withholding tax rate on arm's length and non-arm's length interest. However, there is no indication that Canada intends to modify its other treaties to reduce the current 10% withholding rate, which is currently only applicable to non-arm's length interest, to 0%.

Canada has entered two reservations on paragraph 3 of the OECD Model, which reserves the following rights:

- To amend the definition of "interest" so as to secure that interest payments treated as distributions under their domestic law fall within Article 10; and

- To delete the reference to debt-claims carrying the right to participate in the debtor's profits in the definition of "interest".

In addition, Canada requires the words "income assimilated to income from money lent by the taxation law of the State in which the income arises" in the definition of "interest" in order to tax certain payments to non-residents, such as standby charges and guarantee fees which are deemed to be interest under Part XIII of the Income Tax Act.
Canada has also chosen to omit the sentence which states that the definition of "interest" excludes penalty charges for late payments, which is permitted by the OECD Commentary. The result of this omission is that penalty charges will be treated in accordance with the domestic laws of the source State.

Article 12 Royalties

See treaty text

Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. However, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed 10 per cent of the gross amount of the royalties.
Some royalties arising in a Contracting State and paid to a resident of the other Contracting State who is the beneficial owner thereof shall be taxable only in that other State:
(a) Copyright royalties and other like payments in respect of the production or reproduction of any literary, dramatic, musical or other artistic work (but not including royalties in respect of motion picture films nor royalties in respect of works on film or videotape or other means of reproduction for use in connection with television broadcasting); and
(b) Royalties for the use of, or the right to use, computer software or any patent or for information concerning industrial, commercial or scientific experience (but not including any such information provided under a rental or franchise agreement), Royalties are defined as payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including cinematograph films and films or tapes for television or radio broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience. It also includes payments for the use of, or the right to use industrial, commercial or scientific equipment, i.e. leasing payments.
There are the usual provisions such that royalties received by a non resident but which relate to a permanent establishment which that non-resident has in the other Contracting State are taxed under Article 7 and thus escape withholding tax.
Where the payer and beneficial owner are connected and the amount of royalties exceeds an arm's length amount, the excess amount paid will not enjoy the treaty benefits and will be liable to tax in the payer's State at the normal domestic rate of withholding tax.

Domestic law

Denmark

Danish withholding tax applies to payments (i) qualifying as royalties for Danish tax purposes, (ii) which are not exempt under the EU interest/royalty directive or a tax treaty. If applicable, royalties paid from a Danish company to a foreign company is subject to 25% withholding tax. The tax is withheld at source by the Danish company and settled with the tax authorities.
In relation to (i), it is noticeable that the term "royalties" according to Danish law is narrower than the definition applied in both Article 12 of the OECD Model Tax Convention and the Interest and Royalties Directive. Indeed, the Danish royalty definition only includes industrial and commercial royalties (i.e. mainly payments for use or right to use patents, trademarks, patterns or models, drawings, secret formulas or production methods information on industrial, commercial or scientific knowhow) and does not include "artistic" royalties. Artistic royalties are described as payments for using or buying the right to use copyrights to literary work, artistic work or scientific work, e.g. author royalties or royalties for the use of music, films, etc.
In relation to (ii) in order to qualify for reduction or elimination of withholding tax under a tax treaty or the Interest and Royalties Directive, it is a general requirement that the recipient qualifies as

beneficial owner of the royalty. Reference is made to the specific comments made on the Danish interpretation of this term under Article 10, above.
In practise, if the payment is a royalty, a 25 percent tax is to be withheld at source and the recipient will need to reclaim the withholding tax by completing reclaim form 06.015 with the tax authorities including a statement from the Canadian tax authorities that the beneficial owner of the payment is resident in Canada. According to a statement from the Danish ministry of taxation in 2000 the Danish tax authorities will confirm that also pension funds and investment funds are considered as tax residents in Denmark, irrespective of the fact that they do not pay corporate tax on their income.
Canada
Royalty type payments paid to non-residents of Canada are generally subject to Part XIII withholding tax of 25%, subject to relief under a tax treaty. There are several categories of royalties that are exempted from Canadian Part XIII withholding tax, the main one being "a royalty or similar payment on or in respect of the production or reproduction of any literary, dramatic, musical or artistic work". Also, the types of transactions that are subject to withholding taxes for royalty type payments is broader under the Canadian Part XIII withholding tax regime because it includes any payment for the use of, or for the right to use in Canada, "any property.... or other thing whatever".
Canada's tax treaties contain the following two departures from Article 12 of the OECD Model:
- Canada reserves its right to add the words "for the use of, or the right to use, industrial, commercial or scientific equipment" to the definition of "royalties" in paragraph 2 of the OECD Model.

- Canada reserves its right, in order to fill what it considers as a gap in the Article, to propose a provision defining the source of royalties by analogy with the provisions of paragraph 5 of Article 11, which deals with the same problem in the case of interest.

Article 13 Capital Gains

See treaty text

The usual rule that gains derived by a resident of a Contracting State from the alienation of immovable property as defined in Article 6 and situated in the other Contracting State may be taxed by that State applies under this Treaty. In other words, the Contracting State where the property is situated may tax the capital gain. The term "alienation" is used in connection with events giving rise to capital gains. This will include normal disposals of assets and also events such as exchange of assets, expropriation, gifts and the passing of assets to another on death. Not all States levy tax in all these situations, but the meaning of the term "alienation" is sufficiently wide to give them the right to do so if their domestic law provides for a charge to tax in a particular situation.
As with all treaty provisions, this Article does not impose a requirement upon either State to tax a capital gain; it merely allocates taxing rights so that the relevant State can tax a gain if it chooses.
The usual rule is present: that gains on alienation of movable property forming part of the assets of a permanent establishment may be taxed by the Contracting State where the permanent establishment is situated, including gains from the alienation of the permanent establishment, whether or not as part of the alienation of the whole enterprise. Thus, for example, the sale of a wholly owned company resident in State A and owned by a resident of State A could give rise to a tax charge in State B if that company has a permanent establishment in State B. This does not include gains on ships and aircraft operated in international traffic nor to other movable property used in such a trade.
Apart from some special rules for international transport assets, all other gains are taxable only in the State where the person making the disposal is tax resident. Article 13(4) provides that gains derived directly or indirectly by a resident of a Contracting State from the alienation of shares of a Company which is a resident of the other Contracting State and of which the first-mentioned resident owns at least 25 per cent of the value of the capital stock, or, in the case of Canada, of an interest in a partnership or trust established under the law of that other State and of which the first-mentioned resident's total interest was at least 25 per cent of the value of all such interests, may be taxed in that other State if at least 50 per cent of the value of the share or interest, as the case may be, is derived from immovable property situated in that other State.
The Contracting States has the right to levy, according to its law, a tax on gains from the alienation of any property derived by an individual who is a resident of the other Contracting State and has been a resident of the first-mentioned State at any time during the 6 years immediately preceding the alienation of the property.
Domestic law
Denmark

Under Danish law, only alienation of real estate as well as assets or liabilities attributable to a permanent establishment in Denmark are subject to Danish taxation if the alienator is not a Danish tax resident person. Shares, receivables and intellectual property rights are generally exempted from Danish capital gains tax under Danish domestic law when not attributable to a permanent establishment in Denmark (as Denmark would normally also be prevented from taxing such income under its tax treaties). However, as a very narrow definition of interest applies under Danish domestic law, a specific provision applies according to which any capital gains on receivables in the form of a difference between the nominal amount of the receivable and the amount actually borrowed which is agreed in advance between the debtor and the borrower will be subject to tax in the hands of a non-Danish creditor, if such payment would also be taxable in Denmark to the creditor if it had been an interest.

Canada

Under the Canadian tax system, residents of Canada are taxed on world income which includes all capital gains on the disposition of property. However, only 50% of the capital gain (i.e. the "taxable capital gain") is included in income. Non-residents of Canada are also subject to tax in Canada on the taxable capital gains (i.e. 50% of the capital gain) on the disposition of taxable Canadian property ("TCP"). TCP is a defined term under the Canadian tax laws and includes real property situated in Canada, Canadian resource properties and, generally, any interest in an entity that principally derives its value from such property. Non-residents of Canada realizing capital gains on the disposition of TCP will generally be required to file Canadian tax returns to compute its ultimate Canadian Part I tax liability. To protect the Canadian government from non-residents not complying with its tax laws and filing Canadian tax returns, there is a withholding tax system (on obligation that passes on to the purchaser) that requires the purchaser to withhold 25% of the proceeds of disposition in the absence of a waiver from the Canada Revenue Agency.

Article 14 Independent personal services

See treaty text

Article 14 was taken out of the OECD model in its 2000 revision as a separate provision as it was generally deemed not to be different in substance than Article 7. However, this Treaty still has separate Articles governing the taxation of income from permanent establishments (see Articles 5 and 7) and income from professional services. This Article provides that where a resident of one of the States has a "fixed base" in the other State, income in respect of professional services attributable to that fixed base may be taxed in the country in which it is situated. Thus an Canadian accountant with an office in Denmark will be taxable in Denmark on profits attributable to the Danish office. The attribution of profits is dealt with in the same way as for other business profits under the provisions of Article 7.

The term "professional services" is defined to include especially independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants.

Denmark

Reference is generally made to Article 7, above.

Canada

The Denmark-Canada Convention still includes Article 14 that was deleted from the OECD Model on April 29, 2000. This deletion reflects the fact that there were no intended differences between the concepts of "permanent establishment" in Article 7 and "fixed base" in Article 14 or between how profits and tax were calculated according to Article 7 or 14. In addition, it was not clear which activities fell within Article 7 as opposed to Article 14. Canada would generally view professional services as business profits that would be covered under Article 7 if not for this more specific provision.

Article 15 Dependent personal services

See treaty text

This equates to the "Income from Employment" (Article 15) of the OECD Model and does almost follow the OECD provisions. Salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of employment are taxable only in that State unless the employment is exercised in the other State. If so, remuneration derived from the other State is taxable in the other State.

However, the other State (the source State) will not tax provided:

- The recipient is present in the other State for no more than 183 days during any calendar year; and

- The remuneration is paid by, or on behalf of, an employer not resident in the other State; and

- The remuneration is not borne by a permanent establishment or a fixed base which the employer has in the other State.

Where a resident of Denmark derives remuneration in respect of an employment exercised aboard an aircraft operated in international traffic by the Scandinavian Airlines System (SAS) consortium, such remuneration shall be taxable only in Denmark.
The purpose of this Article is to ensure symmetry in taxation. If the employer is not taxable in a State, because it is neither resident there nor has a permanent establishment there then it will not receive any tax deduction in that State for wages and salaries paid. Wages and salaries paid by the employer in respect of short term employment postings of employees to that State are correspondingly exempted from tax in that State in the hands of the employees.
The treatment of employee stock options is not expressly dealt with and can be difficult as entitlement to the benefit taxable as a result of the option may have accrued partly whilst the employee was working temporarily in one of the States but there may be no taxable event, such as exercise of the option until the employee returns to the other State. A State is permitted to tax that part of the taxable benefit that can be related to the portion of the entitlement period spent working in that State.
Determining the extent to which an employee stock option benefit is derived from employment exercised in a particular State has to be done on a case by case basis, taking into account all relevant facts and circumstances. Whether a period of employment would be considered in allocating taxing rights between two States would depend on whether the entitlement to exercise the stock option was contingent upon continuing employment during that period. If an option was granted with a right to exercise, say, in three years' time, regardless of continuing employment then time elapsing between grant and exercise would not count towards an apportionment of the taxing rights over the benefit in the absence of any other factors.
Periods of employment before the option was granted may be considered in the apportionment of taxing rights if the grant of the option was contingent upon a minimum period of employment or attainment of performance objectives.
Once the option is exercised, any further benefit to the employee, normally in the form of a capital gain on a disposal of the shares at a profit, will be dealt with under Article 13 and so probably only taxable in the State where he is resident.
If the shares do not vest irrevocably on exercise of the option (e.g. because they are liable to forfeiture upon certain conditions) then the increase in value of the shares until they do vest irrevocably will also be dealt with as employment income and subject to the same considerations as the benefit arising between grant and exercise.
The method of apportioning stock option benefits recommended by the OECD is by reference to the proportion of the number of days during which the employment was exercised in one State to the total number of days of employment from which the entitlement to the stock option benefits were derived. Thus if an employee was required to work for an employer for 520 days in total during a particular time period to qualify for the benefits of the stock option and was sent to work in the other State for 260 days out of that period, then half of the stock option benefits would be taxable in each State.
Article 15 should be interpreted in combination with Articles 16, 18, 19 and 20 and the principle behind it is that income derived from an employment is taxed under Article 15 if it does not qualify as income as mentioned under Articles 16, 18, 19 and 20.

Domestic law

Both States have special regimes for expatriate workers: these apply where an individual from one State works in the other State such that he does not qualify for the exclusion from taxation in the State where he is working under the provisions of this Treaty.

Denmark

Under Danish domestic rules, Denmark can tax non-resident employees on income from employment when work is carried out in Denmark. The Danish domestic rules apply to all forms of payment and irrespective of when payment is made. The provision specifically includes severance payments and payment during a termination period when such payments attributable to employment in Denmark. Further, the Danish domestic law provides for a 30 percent tax on hiring out of labour when work is carried out in Denmark.

In a ruling from 2006 by the Danish Tax Council (Skatterådet) the Danish tax authorities confirms that it considers stock options granted as remuneration for employment was comprised by Article 15 of the Denmark-UK tax treaty, which in this respect is similar to Article 15 of the Treaty.
When taxable in Denmark, a person will generally be taxable pursuant to the same rules as a Danish tax resident employee. When only working in Denmark for part of the income year (normally the calendar year for individuals), specific calculation rules apply to ensure that the progressive Danish tax system applies to the income from Denmark. In very general terms, the marginal tax rate, including labour market contributions (AM-bidrag) of 8 percent, applicable to personal income (such as salaries, etc.), is approx. 56 percent. This rate applies to annual income in excess of DKK 389,900 (about. EUR 52,400) per income year. Salary income lower than this amount is taxable between 0-41 percent. Specific rules on aggregate taxation of income apply to married couples.
Denmark operates a specific expatriation tax regime which provides the possibility of taxation at a flat rate of 25 percent (not including AM-bidrag) for a 3-year period or a flat rate of 30 percent (not including AM-bidrag) for a 5 year period., when certain specific criteria are met. When applying either regime, no deductions are allowed.

Canada

Under Canadian domestic tax laws, non-residents of Canada are liable to Canadian tax for any employment income earned in respect of duties of an office or employment performed in Canada. There is no "minimum" period of time that a non-resident employee has to spend in Canada in order to be taxable (and therefore required to file Canadian tax returns). Accordingly, it is of utmost importance that non-residents who physically exercise a portion of their employment duties in Canada understand their treaty entitlements under Article 15 and that their employees understand their Canadian payroll withholding obligations.

Article 16 Directors' fees

See treaty text

These fees may be taxable in the country in which the company is resident as well as that in which the director is resident. This treatment extends not only to directors' fees but also to similar payments deriving from duties as an administrator, manager, liquidator or other duties which are considered analogous by the paying State.

Expert Analysis:

Denmark

Under Danish domestic rules, Denmark can tax fees paid for membership a board of directors, a commission, a committee, a council or similar when payment is made from a Danish company or entity. The payment is taxable as personal income, cf. in further detail 15, above.

Canada

In Canada, a director is considered an employee for the purposes of the Income Tax Act (ITA) and, since remuneration of a director is considered as income from an office, it is included in income by virtue of subsection 5(1) of the ITA.

Article 17 Artists and Athletes

See treaty text

Income derived by a resident of one State as an entertainer, such as a theatre, motion picture, radio or television artist, or a musician, or as an athlete, from their personal activities as such exercised in the other State may be taxed in the other State. This also applies where the income accrues not to the entertainer or athlete himself, but to another person, e.g. a management company or a troupe, team or orchestra forming a legal entity or to an artist company. However this provision shall not apply if it is established that neither the entertainer or the sportsman nor persons related thereto, participate directly or indirectly in the profits of the person referred to in that paragraph.
If the performance in question is supported to a significant extent out of public funds or if it is carried out within the framework of a programme of cultural exchange between the two States, then the income will be taxable only where the performer is resident.

Expert Analysis:

Denmark

Denmark has - in practise - limited access to tax such income as Danish domestic tax law does not have specific provisions on this type of income and therefore only allows taxation when the nature of the payment is payment from employment in Denmark, cf. also Article 15, above.

Canada

According to subsection 212(5.1) of the Income Tax Act, a 23% tax must be withheld on the gross income earned by non-resident actors in a film or video production. However, where subsection

212(5.1) of the Act does not apply, non-resident artists and athletes are taxed in Canada on the same basis as regular business profits or employment income, depending on the nature of the non-resident's services or activities performed in Canada. Please see Article 7 and 15 for general comments on Canada's tax system for non-residents carrying on business in Canada or employed in Canada.

Article 18 Pensions

See treaty text

The main rule in article 18 is that any pension paid to a resident of a Contracting State shall be shall be taxable only in the State in which they arise. Alimony and other similar payments arising in a Contracting State and paid to a resident of the other Contracting State who is subject to tax therein in respect thereof, shall be taxable only in that other State.

Denmark

Under Danish domestic law, Denmark is entitled to tax payments from Danish pension schemes to non-resident persons. The Danish pension tax system is relatively complex and a detailed description thereof is not made herein. Generally, tax deductibility for pension contributions is allowed irrespective of whether the pension scheme is established in Denmark or elsewhere in the EU when certain criteria are met. The deductible annual amount depends on the type of pension scheme. During the life of the pension scheme, an annual mark-to-market pension yield tax of 15 percent applies. When the pension is ultimately paid to the pensioner (or beneficiaries) such payments are taxable as personal income (cf. Article 14, above). However, payments from a capital pension scheme are taxable at a flat rate of 40 percent.

In 1998, the Danish ministry of taxation issued a statement regarding the application of the Danish tax treaties to payments under the Danish social legislation, which contains guidance on how to apply the Danish tax treaty to various types of payments under the Danish social legislation.

Canada

Under the domestic tax laws of Canada, tax is generally totally or partially deferred on contributions to, and earnings in, pension schemes or on the accrual of pension rights, but is recovered when pension benefits are paid. Canada considers that a deduction for pension contributions is a deferral of tax on the part of the employment income that is saved towards retirement.

When pension payments are made to non-residents of Canada, such amounts are generally subject to a 25% Part XIII withholding tax, subject to any reduced treaty rates. However, because pensions are commonly dealing with smaller overall income figures, Canada's tax system does allow non-resident pensioners to make a section 217 election and file a Canadian tax return reporting their Canadian pension income. This election generally results in a lower overall Canadian tax liability than a withholding tax on gross pension payments, particularly since Canada's tax rates for individuals is on a progressive basis and pensions are commonly lower income amounts.

Article 19 Governmental Payments

See treaty text

This Article contains rules for the taxation of a remuneration paid in respect of government service. Remunerations paid by a country or one of its political subdivisions or local authorities will generally be taxable only in that State. However, such remuneration will be taxable only in the other country if the services are rendered by a national of that other country who is a resident there, or by a resident of that country, who, although not one of its nationals, did not become a resident solely to render the services.

The Article does not include any pension where Article 18 will apply.

Article 19(2) determines that Article 19(1) does not apply to salaries, wages and other similar remuneration in respect of services rendered in connection with a business carried on by a Contracting State or a political subdivision or a local authority thereof. Such income will be dealt with under Articles 15, 16.

Article 20 Students

See treaty text

Where a student, or business apprentice who is, or was immediately before visiting a Contracting State, a resident of the other Contracting State and is present in the visited State solely for the purpose of his education or training for no more than two years, receives for the purpose of his maintenance, education or training will not be taxed in the visited State provided that the payments arises from sources outside the visited State.

Students or apprentices can work in the visited State without being taxed provided the work is in connection with the education or training, or the remuneration earned is needed to support the student's living expenses.
Receipts of grants, scholarships or prizes from scientific, educational or charitable organisations are tax-free in the visited State no matter where they arise.

Article 21 Other Income

See treaty text

Any income not dealt with in the preceding Articles is taxable only in the State of residence, provided that the income is subject to tax in that state (subject-to-tax-test). However, if such income is derived by a resident of a Contracting State from sources in the other Contracting State, such income may also be taxed in the State in which it arises, and according to the law of that State. Where such income is income from an estate or a trust, other than a trust to which contributions were deductible, the tax so charged shall, provided that the income is taxable in the Contracting State in which the beneficial owner is a resident, not exceed 15 % of the gross amount of the income.

Expert Analysis:

Denmark

The provision is deemed to have only very little practical impact. Taxation hereunder requires - similar as the other provisions of the Treaty - that Danish domestic law contains a right to tax income hereunder. This would only exceptionally be the case.

Canada

Canada has entered a reservation on Article 21 of the OECD Model, which maintains Canada's right to tax income arising from sources in its own country that have not been dealt with by other Articles in the Treaty.
Types of income covered under Article 21 may include the following:

- income from an estate or trust;
- currency gains or losses;
- annuities and income under certain life insurance policies (if not dealt with in Article 18);
- non-employee retirement income (if not dealt with in Article 18);
- income from certain distributions to taxpayers that do not fit into any of the other tax treaty categories;
- child support payments (if not dealt with in Article 18);
- damages and other income under certain severance arrangements; or
- income from certain non-traditional financial instruments.

Article 22 Capital

See treaty text

Wealth taxes may be imposed on:

- Immovable property according to the State where the property is located; and
- Movable property used by a permanent establishment may be subject to wealth tax in the State where the permanent establishment is located.

Apart from these items and some rules in connection with international transport assets, all other elements of capital may only be subject to wealth taxes in the State where the owner is resident.

Expert Analysis:

Denmark

Denmark does not levy general wealth taxes. However, a partial wealth tax applies in the form of property value tax which is levied at the value of real estate which is the domicile of the owner and/or his family or the summer residence of the owner and/or his family. The tax rates are 1 percent up to a value of DKK 3,040,000 (2011) and 3 percent of values in excess thereof. The value is generally determined as the so-called publicly assessed value, but certain modifications may apply. For Danish tax resident individuals the domestic tax rules apply both to real estate situated in Denmark and

abroad. For non-resident individuals, the tax applies to real estate situated in Denmark (in practise primarily Danish summer houses or apartments).

Canada

The federal Large Corporations Tax, which was imposed on corporations with capital in excess of $10 million, was eliminated as of January 1, 2006. The provinces of Nova Scotia, Quebec and Manitoba still levy a tax on the capital of most active business corporations, including mining. Generally, provincial capital taxes are in the process of being reduced or phased out.

Article 23 Methods for the Elimination of Double Taxation

See treaty text

Canada

Canada will use the exemption method. The method is exemption with progression so that the amount of exempt income will be taken into accounting determining the tax rates to be applied to income remaining in charge to tax in the State of residence.

However, for dividend and interest income the credit method will be used. No credit is given for corporation tax underlying a dividend.

Denmark

Denmark generally applies the tax credit method under its domestic rules, unless another method follows from a tax treaty or is specifically provided for under domestic law. The credit is the lesser of either (a) the foreign tax actually paid on the income, and (b) the proportionate amount of the overall Danish tax payable which can be allocated to the foreign income. However, according to the Danish Tax Assessment Act (ligningsloven), a net income calculation principle applies in internal Danish law when determining the amount of tax credit available. Under this principle any expenses directly relating to foreign source income initially eligible for a tax credit ("related expenses") should be deducted from such income when computing the Danish tax credit. Further, when calculating the Danish tax credit any expenses which are not immediately allocable either to the taxpayer's foreign source income or Danish source income (unallocated expenses) should be allocated proportionally (pro rata) to the foreign and Danish source income (i.e. in proportion to the foreign and Danish gross income). To which extent an expense is a related expense or a general expense must be determined on a case by case basis.

As regards participants in partnerships, Denmark allows Danish partners therein a tax credit, also for tax levied on the partnership as such when the partnership is considered tax transparent in Denmark.

An exemption method applies pursuant to sec. 33A of the Danish Tax Assessment Act to income from employment abroad when the employment exceeds 6 months and the employee only has limited stays in Denmark during the foreign employment period as further specified therein.

Further, Sec. 8 of the Danish Corporate Income Tax Act lies down a territorial principle for certain corporate activities as it states that if a Danish enterprise has a permanent establishment abroad Denmark will exempt income allocable to such permanent establishment abroad, unless (i) the state in which the PE is located waive its right of taxation under a tax treaty with Denmark or other international agreement, (ii) income in the PE would have been taxable under Danish CFC tax rules if the PE had been a company, or (iii) the income in the PE is income from the operation of ships or aircraft in international traffic.

Domestic law

Denmark

Denmark's participation exemption can reduce tax payable where a resident company or permanent establishment of a foreign company receives dividends, currency gains and capital gains on shares. These are exempt from Danish taxation if they arise from a minimum shareholding of 10% in a directly owner subsidiary located within another EU Member State or a state with which Denmark has a tax treaty, provided the tax treaty between Denmark and that state provides for a reduction in the rate of withholding tax. Thus dividends received by a Danish company from an Canadian subsidiary in which there was a minimum shareholding of 10% would be exempt from Danish taxation, although if not covered by the Parent-Subsidiary Directive, they may have suffered Austrian withholding tax.

Canada

Canada, which taxes its residents on worldwide income, already has an extensive foreign tax credit system to alleviate double tax on non-Canadian source income, Therefore, the benefits of Article 23 of the Canada-Denmark Treaty are rather limited.

Furthermore, Canada also adopts the exemption method system for certain qualified dividends arising outside Canada. The exemption system usually applies to active business profits (i.e. exempt surplus) earned by a foreign affiliate (i.e. a non-resident corporation in which the Canadian corporate shareholder owns more than 10% interest.)

Article 24 Non-discrimination

See treaty text

Nationals of one of the States are not be subjected in the other State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of the other State in the same circumstances are or may be subjected.

The usual OECD provisions provide that individuals who are nationals of one State do not have the same status as individuals who are nationals of the other State when they are not residents of that State. Hence they need not be granted the personal allowances and similar deductions which are available to residents.

Each State will grant to nationals of the other the same exemptions and personal allowances as it grants to its own nationals. The non-discrimination principle applies to all taxes, not just those covered by this Treaty.

Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned Contracting State to any taxation, or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprises of that first-mentioned State are or may be subjected.

Canada

Canada has entered a reservation on Article 24 of the OECD Model. Nonetheless, Canada does accept the general principle of non-discrimination on the basis of nationality that is proposed by the OECD Model in this Article. Accordingly, most of Canada's treaties do include this Article with the exception of a few of the principle's extensions as found in the OECD Model.

Paragraph 1 of the Non-Discrimination Article of Canada's tax treaties does not normally contain the last sentence of paragraph 1 of Article 24 of the OECD Model. It is Canada's view that this Article should only apply to nationals covered by a particular treaty as it would be inappropriate to give a taxpayer the benefit of a Canadian treaty with a country in which the taxpayer is not a resident. Presumably, this is a bigger concern to Canada where the national is resident in a non-treaty country.

Saipem UK Limited v. The Queen ("Saipem") is the first Canadian court decision dealing with the substance of the Non-Discrimination Article in Canada's tax treaties. Prior to Saipem, the Canadian courts in cases like *Crawford v. The Queen* and *Ramada Ontario Ltd v. The Queen* only ruled on minor issues regarding the Non-Discrimination Article. In Saipem, the issue was whether the restriction in subsection 88(1.1) of the Income Tax Act (Canada) ("ITA") pertaining to "Canadian corporations" violated the taxpayer's rights to non-discriminatory treatment under Article 22 of the Canada-United Kingdom Tax Convention. The appellant ("Saipem UK") was a UK resident that carried on business in Canada through a permanent establishment ("PE") from 2004 to 2006. Saipem UK's subsidiary, Saipem Energy International Limited ("SEI"), was also a UK resident that carried on business in Canada through a PE from 2001 to 2003. In 2003, SEI was wound up into its parent company. In computing its income from its Canadian business for the 2004 to 2006 years, Saipem UK claimed deductions for the losses incurred by SEI in prior years. With respect to paragraph 1 of the Non-Discrimination Article, the Tax Court of Canada ("TCC") concluded that Saipem UK was not being treated "less favourably" and that subsection 88(1.1) does not discriminate based strictly on nationality. However, in applying and interpreting the expression "in the same circumstances", the TCC confirmed that the residence of the taxpayers is one of the factors that must be taken into account when determining whether the taxpayers are placed in similar circumstances for the non-discrimination provision to apply. With respect to paragraph 2 of the Non-Discrimination Article, the TCC also concluded that the "equal treatment principle only applies to the taxation of the PE's own activities and does not therefore extend to provisions that take into account the relationship between an enterprise and other enterprises and that allow the transfer of losses." The Federal Court of Appeal recently upheld this decision by the TCC.

Most of Canada's tax treaties do not contain paragraph 2 of the OECD Model as this provision deals with an obscure situation.

Canada's tax treaties do not generally include a provision equivalent to paragraph 4 of Article 24 of the OECD Model because Canada is not prepared to give up its thin capitalization regime.

Paragraph 5 of Article 24 of the OECD Model also provides that an entity of one of the Contracting States which is owned or controlled by residents of the other Contracting State may be treated no less favourably than entities owned or controlled by residents of the first-mentioned State. In other words, the OECD Model requires national treatment for foreign?owned entities. Again, based on Canada's existing treaty network, it would appear that Canada is only prepared to accept a most-favoured

nation rule. That is, the provision seen in many of Canada's tax treaties provides only that entities owned by residents of the treaty partner will be treated the same as any other foreign?owned entities. The intention is most likely to protect Canada's special tax regimes pertaining to small businesses in Canada and Canadian-controlled private corporations.

Article 25 Mutual agreement

See treaty text

The usual provision found in the OECD Model is used. Where a person considers that the actions of one or both of the States will lead to taxation in conflict with the provisions of this Treaty, the person may present his case to the competent authority of the State of which the person is resident. This is so irrespective of the remedies provided by domestic law. The Treaty does not include a time limit for presenting the case. A Contracting State shall not, after the expiry of the time limits provided in its national laws and, in any case, after six years from the end of the taxable period in which the income concerned has accrued, increase the tax base of a resident of either of the Contracting States by including therein items of income which have also been charged to tax in the other Contracting State. This paragraph shall not apply in the case of fraud, wilful default or neglect. The tax authorities of the two States will try to resolve the case by mutual agreement. They will also try to agree on definitions of terms not specifically defined in the treaty and on general matters of interpretation of the Treaty. Thus, this Article removes the need for the tax authorities in each State to go through diplomatic channels, they may simply contact each other directly. The mutual agreement procedure is commonly used to decide matters concerning income and expense allocations and transfer pricing.

Domestic law

Denmark

The competent authority in Denmark on matters of tax treaties is SKAT (Legal Center), which is resident on Østbanegade 123, DK-2100 Copenhagen. On issues on relation to transfer pricing and the EU Arbitration Convention, the competent authority is SKAT (Store selskaber), which is resident on the same address.

Canada

Canada's tax conventions define the Canadian Competent Authority as the Minister of National Revenue or the Minister's authorized representative. Administratively, the Canadian Competent Authority function is split between the International Tax Directorate and the Legislative Policy Directorate of the CRA. The Director, Competent Authority Services Division,
International Tax Directorate serves as the Canadian Competent Authority for resolving cases, such as the examples listed in paragraph 11, related to specific taxpayers. Requests for competent authority assistance in respect of specific cases and related enquiries may be sent to:
Canada Revenue Agency
Director, Competent Authority Services Division International Tax Directorate
Compliance Programs Branch
5th floor, 344 Slater Street
Ottawa ON K1A 0L5 T
he Director General, Legislative Policy Directorate, is the Canadian Competent Authority for issues involving general interpretation, non-discrimination, treaty shopping, double non-taxation issues, and general issues concerning the application of tax conventions where specific taxpayers are not involved. Requests for competent authority assistance in respect of these non-specific case issues may be sent to:
Canada Revenue Agency
Director General Legislative Policy
Directorate Policy and Planning Branch
22nd floor, Tower A Place de Ville
320 Queen Street
Ottawa ON K1A 0L5
“Competent Authority”: Canada's domestic tax system does not define terms such as “enterprise” or “national”. However, it does have a broad definition of “business” to include “a profession, calling, trade, manufacture or underrating of any kind whatever”.

Article 26 Exchange of information

See treaty text

This Article is almost identical to Article 26 of the OECD Model Convention. Article 26 of the Convention has been extended to apply to Greenland.

The scope of this Article is limited in that it only provides for exchange of such information as is "foreseeably for carrying out the provisions of this Convention and of the domestic laws of the States concerning taxes covered by the Convention insofar as the taxation thereunder is in accordance with the Convention." Exchange of information is not limited only to residents of the two States.
The article includes the usual provisos relieving the States from any obligation to:

- Carry out administrative measures at variance with the laws or administrative practices of either State;

- Supply information which is not obtainable under the laws or in the normal course of the administration of either State; and

- Supply information which would disclose any trade, business, industrial commercial or professional secret or trade process, or information the disclosure of which would be contrary to public policy (ordre public).

Article 27 Activities in Connection with Preliminary Surveys, Exploration or Extraction of Hydrocarbons

See treaty text

Notwithstanding the provisions of Article 5 and Article 14, shall a person who is a resident of a Contracting State and carries on activities in connection with preliminary surveys, exploration or extraction of hydrocarbons situated in the other Contracting State be deemed to be carrying on in respect of those activities a business in that other Contracting State through a permanent establishment or fixed base situated therein, if the activities are carried on for a period or periods exceeding 30 days in the aggregate in any 12 month period.
Drilling rig activities carried on off-shore constitutes a permanent establishment only if the activities are carried on for a period or periods exceeding 90 days in the aggregate in any 12 month period.

Article 28 Diplomatic Agents and Consular Officials

See treaty text

Nothing in this Convention shall affect the fiscal privileges of diplomatic or consular officials under the general rules of international law of under the provisions of special agreements.

Article 29 Territorial Extension

See treaty text

The article provides that this Treaty may be extended either in its entirety or with any necessary modifications to any part of the territory of Denmark which is not included in the scope of the Treaty and which imposes taxes substantially similar in character to those to which the Treaty applies. Any such extension shall take effect from such date and subject to such modifications and conditions - including conditions as to termination - as may be specified and agreed between the Contracting States in notes to be exchanged through diplomatic channels or in any other manner in accordance with their constitutional procedure.

Domestic law

Denmark

For Denmark, this would only be relevant if it were decided to include Greenland and/or the Faroe Islands hereunder.

Canada

This provision on territorial coverage is not necessary for Canada as every part of Canada is covered by its tax treaties (see definition of "Canada" in Article 3). However, Canada likely has agreed to include this Article in the Canada-Denmark Income Tax Convention due to the reasons noted by Denmark above.

Article 30 Miscellaneous Rules

See treaty text

An Article like this does not exist in the regular OECD model.
Paragraph 1 and 2 stipulates that the Convention are not construed to restrict in any manner any exclusion, exemption, deduction, credit or other allowance now or hereafter accorded by the laws of a Contracting State in the determination of the tax imposed by that State and the Convention shall not be construed as preventing a Contracting State from imposing a tax on amounts included in the income of a resident of that State with respect to a partnership, trust or controlled foreign affiliate, in which he has an interest.

Paragraph 3 stipulates that dividends paid to an organisation that was constituted exclusively to administer or provide benefits under one or more pension, retirement or other employee benefits plans shall be exempt from tax in the source state provided that:
(a) the organisation is the beneficial owner of the shares on which the dividends are paid, holds those shares as an investment and is generally exempt from tax in the other State;
(b) the organisation does not own directly or indirectly more than 5 per cent of the capital or 5 per cent of the voting stock of the company paying the dividends; and
(c) the class of shares of the Company on which the dividends are paid is regularly traded on an approved stock exchange.
Paragraph 5 stipulates that any dispute between the Contracting States related to the General Agreement on Trade in Services, paragraph 3 of Article XXII (Consultation), whether a measure falls within the scope of this Convention, may be brought before the Council for Trade in Services.

Article 31 Entry into Force

See treaty text

The Treaty entered into force as per the income year 1999.

Article 32 Termination

See treaty text

The Treaty can be terminated with a notice of 6 months. In case of such termination, the Treaty will cease to have effect from the following income year.