Analysis: Denmark – United Kingdom Income and Capital Treaty

See treaty text

Type of Treaty: Income and Capital
Model on which based: OECD
Signed: November 11, 1980
Entry into force: December 17, 1980
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First Protocol signed: July 1, 1991
Entry into force of First Protocol: December 19, 1991
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Article 1 Personal Scope

See treaty text

Persons who are residents of one or both States.

Article 2 Taxes covered

See treaty text

Denmark

- Income taxes to the state (statslig indkomstskat (bund-, mellem-, topskat));
- Municipal income tax (kommunal indkomstskat);
- Since 2008: labour market contribution (AM-bidrag)

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

This agreement does not apply to certain charges ("afgifter") levied under The Danish Pension Tax Act (Pensionsbeskatningsloven).

United Kingdom

- Income tax;
- Corporation tax;
- Capital gains tax;
- Petroleum revenue tax; and
- Development land tax.

Article 3 General Definitions

See treaty text

"United Kingdom": The territory of the Kingdom of United Kingdom (see also Article 2 of the First Protocol).

"Denmark": The Kingdom of Denmark, including any area outside the territorial sea of Denmark which in accordance with international law has been or may hereafter be designated under Danish laws as an area within which Denmark may exercise sovereign rights with respect to the exploration and exploitation of the natural resources of the sea-bed or its subsoil; the term does not comprise the Faroe Islands and Greenland, but the Convention can, pursuant Article 29 be extended to cover the Faroe Islands and Greenland.

"National": In relation to the UK the term "national" has been amended by the 1991 protocol: All British citizens or any subject not possessing the citizenship of any other Commonwealth country or territory, provided he has the right of abode in the UK. Any legal person, partnership, association or other entity deriving its status as such from UK law. In relation to Denmark, any individual possessing the nationality of Denmark and any legal person, partnership or association deriving its status as such from the law in force in Denmark.

"Competent authority" is in the Convention stated to be the minister of taxation. In matters relating to international taxation, authority has been delegated to "SKAT", the Danish administrative tax authorities.
"Person": An individual, company and any other body of persons.
"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": The term has been amended by the 1996 protocol. It means any transport by ship or aircraft operated by an enterprise of either Denmark or the United Kingdom, except when the operation is solely between places in the other Contracting State. The main rule is that the place of residence - not the place of effective management - is relevant.
"United Kingdom": Great Britain and Northern Ireland, including any area outside the territorial sea of the United Kingdom which in accordance with international law has been or may hereafter be designated, under the laws of the United Kingdom concerning the Continental Shelf, as an area within which the rights of the United Kingdom with respect to the seabed and subsoil and their natural resources may be exercised. Jersey, Guernsey, the Isle of Man and Gibraltar are not covered by this Treaty.
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.

Article 4 Fiscal Domicile

See treaty text

"Resident": 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. It does not include a person liable to tax in a State only in respect of income from sources of income situated in that State.

Residence: Individuals

In the case of individuals apparently resident in both Contracting States, the usual OECD Model 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 section 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.

United Kingdom

There is no statutory definition of "residence". Individuals who are present in the UK for 183 days or more in a fiscal year or, on average, at least 91 days (tested over the last three complete tax years; residence applying from the fourth) are generally treated resident in the UK. Although once considered "resident" this applies for the entire fiscal year in which residence arises, the fiscal authority, by concession, will permit the residency to commence or cease on the day of arrival or departure, respectively, to the UK where the move to/from the UK has a degree of permanency. Note that these presence based tests are not statutory but reflect the normal practice of the UK tax authorities: although they can and do have regard to other relevant factors in particular circumstances.
The tax law of the UK also has a concept of "ordinary residence", arising broadly from two years' residency (ordinary residence applying from the second year); residency in the four years preceding the previous year to that being considered; or, intentions to reside or actual residence in the UK for three years. Ordinary residence is a more adhesive quality than simple residence so that a person wishing to change his residence will find this harder if he is ordinarily resident. Working abroad under a contract of employment for an entire fiscal year is one way of shedding ordinary residence.

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 of the State in which its place of effective management of its business is situated.

Domestic law

Denmark

All companies taxable under section 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, section 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.

United Kingdom

The UK's domestic law states that companies incorporated in the UK are resident there. Other companies are resident in the UK if their central management and control is located in the UK. This test focuses on where the board meets and company policy decisions are made, not where day-to-day management takes place. In the face of conflict between questions of residence arising from UK domestic law and treaty provisions, the treaty provisions prevail: the "central management and control" domestic law test is generally understood to be similar to the "place of effective management" test found in the OECD model treaty, but HM Revenue & Customs and the Courts have both suggested that the two tests may in certain circumstances produce different results.

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 section 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).

United Kingdom

Unlimited partnerships are treated as transparent entities, as are Limited Partnerships and Limited Liability Partnerships. The following types of entities are taxed as corporations:

- Unincorporated associations;
- Building societies;
- Mutual insurance societies;
- State-owned industries;
- Public utility companies;
- Crown corporations; and
- Permanent establishments of non-resident companies.

Charities are generally exempt from corporation tax, unless they are trading and the trade is not exercised in the course of carrying out the primary purpose of the charity, or is carried out mainly by its beneficiaries.

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. Types of establishment particularly included involve the following::

- A place of management;
- A branch;
- An office;
- A factory;
- A workshop;
- ? A mine, a quarry or any other place of extraction of natural resources; and
- A construction or assembly project which exists for a period of more than 12 months. By the 1991 protocol, Paragraphs 3A and 3B had been added, which state that certain construction projects and activities concerning oil and gas shall constitute a permanent establishment from the first day.

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) (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 (including advertising and scientific research).

(f) (f) The maintenance of a fixed place of business for any combination of the above, so long as the overall activity remains preparatory or auxiliary.

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 the purchase of goods or merchandise for the enterprise. Where the activities of the agent are limited to the purchase of goods for the enterprise, 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.

Other Provisions

Concerning some offshore activities as permanent establishments see Article 28A.

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 section 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.

United Kingdom

Under UK domestic law, a person who carries on a trade, profession or vocation wholly or partly in the UK is liable to income tax on the profits attributable to that trade, whether or not a permanent establishment exists. There is extensive case law on the question of what constitutes "trading in" (as opposed to merely "trading with") the UK. Where a tax treaty exists, it will normally override the income tax charge in the absence of a permanent establishment. Where a company carries on a trade in the UK through a permanent establishment, the income tax charge is superseded by a charge to corporation tax. The UK domestic law definition of "permanent establishment" closely follows that in the OECD model treaty, with a few minor variations.

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.

When Denmark is the source state, which it is when the immovable property is located in Denmark, there is legal basis in national tax law for taxing operating profits relating to the property in the Danish Tax at Source Act (*kildeskatteloven*), section 1, (1), (5) and in the CITA section 2, (1), (b).

Since the Convention does not cover wealth taxes, property value tax (*ejendomsværdiskat*), which is considered a partial wealth tax, is not within the scope of the Convention.

United Kingdom

Non-UK resident individuals and companies are chargeable to income tax on the profits from a UK property business, which will normally comprise rental income less any deductible expenses. Where a non-resident company's UK property business is carried on through a permanent establishment, the income tax charge is superseded by a charge to corporation tax.

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.

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.

Deviation from OECD

The Treaty largely follows the 1977 OECD Model, but does not permit allocation of profits by means of unitary apportionment. It also does not include the corresponding adjustment mechanism that later became part of the model.

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.

United Kingdom

The UK uses the “distinct and separate enterprise approach” in its domestic law. Both income arising directly or indirectly from a permanent establishment, including income from property used by the permanent establishment are taxable as well as chargeable gains on assets used by the permanent establishment for the purposes of its trade.
Specifically, the UK allocates the profits of the entity on the assumption that the permanent establishment has the same credit rating as the Head Office and has the capital structure that an independent enterprise in similar circumstances would be expected to have. Transactions between the permanent establishment and other parts of the enterprise are valued on the arm's length basis, but no deduction is allowed for payments to any other part of the same company in respect of intangibles, interest or other financing costs. An apportionment of executive and general administration expenses is permitted whether or not the permanent establishment has borne or incurred such expenses providing these would have been deductible if borne by a UK resident company.

Article 8 Shipping and air transport

See treaty text

This provision relates to income derived from the operation of ships or aircrafts in international traffic. The Treaty provides that such income shall only be taxable in the state in which the seat place of effective management of the enterprise is situated.
For purposes of the Treaty, the term “international traffic” is defined in Article 3, par 1(i).

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. However, as Member States of the European Union, both States are bound by the provisions of the EU Arbitration Convention (see below) and can use the mutual agreement procedure provided for in this Treaty.
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.

Effect of the EU Arbitration Convention

The EU Arbitration Convention re-entered into force retroactively from January 1, 2000. Its main purpose is to assist the working of the European Single Market by achieving the elimination of double taxation which may result from one Member State making an upwards adjustment in taxable profits which is not matched by an equivalent downwards adjustment to taxable profits in the other State(s) concerned in the transactions in question. As Member States of the European Union, both United Kingdom and Denmark are bound by the provisions of the EU Arbitration Convention (90/436/ EEC of July 23, 1990). Both States have also ratified the EU Code of Conduct for the effective implementation of double taxation in connection with the adjustment of profits of associated enterprises. Under the

Arbitration Convention and the Code of Conduct, a taxpayer company disagreeing with the amount of a transfer pricing agreement or suffering double taxation as a result of an upwards transfer pricing adjustment has three years in which to present its case to the tax administration of the State making the upwards adjustment. Under the Code of Conduct (2006/C176/02) the three years runs from the date of first notification of the transfer pricing adjustment. The two Member States involved then have two years in which to reach an agreement which eliminates the double taxation resulting from the upwards transfer pricing adjustment. If they cannot reach agreement within this period then they must set up an advisory commission consisting of representatives of each tax authority and independent persons. This body then has six months to deliver its opinion.

Domestic law:

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.

United Kingdom

Part 4 of the Taxation (International and Other Provisions) Act 2010 (TIOPA 2010) contains the UK's transfer pricing code, which applies to the arm's length standard to most dealings between parties if one of them directly controls the other, or the same person controls both. The rules also apply to dealings between joint venture vehicles and their participants in situations where two participants have 40% interests in the joint venture, and also where a number of people "act together" in connection with financing arrangements (thus catching many leveraged private equity structures). The legislation provides that it is to be interpreted in accordance with OECD principles. A corresponding adjustment for transfer pricing purposes pursuant to a treaty is given effect under section 124 TIOPA 2010.

Article 10 Dividends

See treaty text

This Article was rewritten by the 1996-protocol. The new version is more or less in accordance with the OECD Model Convention. It 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

- 0% where the recipient owns at least 25% of the paying company's share capital; and
- 15 % in other cases.

The dividend withholding tax rates of par. 2 do not apply if an exemption exists under the EU Parent-Subsidiary Directive.

Other points of this Article

Paragraph 3 defines the term “dividends” to include income from shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident and also includes any other item (other than interest relieved from tax under the provisions of Article 11) which, under the law of the Contracting State of which the company paying the dividend is a resident, is treated as a dividend or distribution of a company.
Paragraph 4 provides that where, say, a United Kingdom company receives a dividend from a Danish company, and that dividend is effectively connected with a permanent establishment which the United Kingdom 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 dealing with the attribution of business profits will apply.
Paragraph 6 contains a special anti-abuse provision. The Contacting States shall inform each other if this provision is applied.

Effect of EU Parent-Subsidiary Directive

Although this Treaty provides that the Member State from which the dividend is paid may tax the dividend, domestic law of the two States as amended in line with the EU Parent-Subsidiary Directive (90/435/EEC) may override this aspect of the Treaty.
Dividends or other profit distributions paid to a shareholder where both are resident in the EU are not to be subject to withholding taxes. This treatment also applies to dividends received by permanent establishments.
To qualify for this treatment both States require that the shareholding must amount to a minimum holding of 15% of the capital (reducing to 10% from January 1, 2009). Previous limits were 25% (from 2003 - December 31, 2004) and 20% (from January 1, 2005 - December 31, 2006).
Member States may impose a two-year minimum ownership period before the exemption provided for in the Directive is granted. However, in its 2009 tax reforms, Denmark has abolished the statutory holding period (previously enacted as 12 months).
The business entities covered by the Directive are:

Denmark

- Aktieselskab;
- Anpartselskab; and
- Other companies constituted under Danish law subject to Danish corporate tax.

United Kingdom

- Companies incorporated under the law of the UK.

The parent company must be subject to tax in its own Member State. Recognised taxes for this purpose are:

Denmark

Selskabsskat.
Denmark will exempt dividends from withholding tax under the Parent-Subsidiary Directive without any minimum holding period for the shares in respect of which it is paid. The minimum shareholding is 10% of the paying company's capital.

United Kingdom

Corporation tax

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 27%. The shareholder may seek a refund from the Danish tax authorities of the tax withheld in excess of 10%. 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 United Kingdom tax authorities that the beneficial owner of the payment is resident in United Kingdom.
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 27% 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 United Kingdom, 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 United Kingdom tax authorities that the beneficial owner of the payment is resident in United Kingdom. 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.

United Kingdom

There are no withholding taxes on dividends payable to non-resident shareholders other dividends paid by Real Estate Investment Trusts, which are subject to a withholding tax at a rate of 20%.

Article 11 Interest

See treaty text

No withholding tax may be levied provided the interest is beneficially owned by a resident of the State to which it is paid.

"Interest" is widely defined to mean income from government securities, bonds or debentures, other debt claims of every kind but excluding income covered by Article 10.

There is the usual provision such that interest received by a non-resident but which relates to a permanent establishment or fixed base which that non-resident has in the other Contracting State is taxed under Article 7 or 14.

Where the payer and recipient 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.

Paragraph 6 contains a special anti-abuse provision. The Contacting States shall inform each other if this provision is applied.

Effect of the EU Interest and Royalties Directive

The EU Interest and Royalties Directive (2003/49/ EEC) provides that interest and royalty payments from a company in one Member State to a shareholder in another Member State may be exempt from withholding tax providing certain conditions are met. This has been adopted into UK law, with the relevant provisions now contained in sections 757 to 767 of the Income Tax (Trading and Other Income) Act 2005.

As Denmark did not apply withholding tax on interest when the Interest and Royalties Directive was adopted, Denmark did not amend Danish tax law to implement the directive. Subsequently, Denmark as introduced withholding tax interest, however, specifically exempting inter alia interest payments eligible for protection under the Interest and Royalties Directive, cf. "Denmark", below.

In practice, the advent of the Directive did not change the position in relation to interest payments between the UK and Denmark as the Treaty already offered more generous relief. Interest recipients qualifying for relief under the Directive may elect to claim under either the Treaty or the Directive.

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 25% 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 (2013) 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 (2013).
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.

United Kingdom

Interest paid to companies: Withholding tax of 20% except on quoted Eurobonds. Certain bank interest may be paid gross on filing of a declaration
. Interest paid to individuals: 20%.
A claim must be made in order to obtain relief under the Treaty or the Directive. On approval of a claim, HMRC will issue a direction to the paying party to make payment of interest without deduction of tax.

Article 12 Royalties

See treaty text

This Convention provides for elimination of withholding tax on royalties when paid from a resident in one state to a resident in the other state.
To benefit from these provisions, the royalties must be derived and beneficially owned by a resident of the State to which they are paid.
In paragraph (3) "royalties" is defined to include payments of any kind received as consideration for the use of, or right to use:

- Copyright of literary, artistic or scientific works including film and films or tapes for radio or television broadcasting;

- Any patent or trademark, design or model, plan, secret formula or process;

- Any industrial, commercial or scientific equipment (i.e. leasing payments); and

- Any information concerning industrial, commercial or scientific experience.

Where royalties or fees are effectively earned by a permanent establishment or fixed base (see independent personal services) they will be taxed as part of the profits of that permanent establishment (i.e. in the State in which they arise) (Article 7 or 14 applying).
Where the payer and recipient 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.
Similar to Article 10 and 11, this Article also contains a special anti-abuse provision. The Contacting States shall inform each other if this provision is applied

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 United Kingdom tax authorities that the beneficial owner of the payment is resident in United Kingdom. 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.

United Kingdom

Withholding tax at 20% on certain specified classes of royalties and on other royalties that represent "annual payments" (i.e. regular periodic payments that represent pure income profit in the hands of the recipient). Royalties can be paid without deduction of tax where the paying party reasonably believes that a Treaty applies.

Effect of the Interest and Royalties Directive

See above under Article 11.

Article 13 Capital Gains

See treaty text

The usual rule that gains derived by a resident of a Contracting State from the disposal (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.
The general principle is that gains, other than those relating to immovable property and relating to assets which belong to a permanent establishment, are taxable only in the State where the seller is resident. There are the usual special provisions for ships, boats and aircraft.
Also applicable is the usual rule is 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.

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.

United Kingdom

The UK does not tax chargeable gains of non-residents except assets used for the trade of a non-resident in a UK permanent establishment. This applies both to permanent establishments of a non-resident company and of a non-resident unincorporated business.

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 from 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 a United Kingdom 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, and accountants.

Domestic law:

Denmark

Reference is generally made to Article 7, above.

United Kingdom

A non-resident individual will be taxable in the UK if he/she is trading in the UK (see Article 5 above).

Article 15 Dependent personal services

See treaty text

This equates to the "Income from Employment" (Article 15) of the OECD Model and follows 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 in aggregate in a 12-month period; 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.

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.
Special rules apply to employees in international transport industries.

Treatment of stock options

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

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 this 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 421,000 (about. EUR 56,440) per income year. Salary income lower than this amount is taxable between 0-44 percent. Specific rules on aggregate taxation of income apply to married couples.
Denmark offers a special tax regime to highly paid inbound expatriates and researchers recruited from abroad (subject to criteria). Employees may elect to be taxed at a rate of 26% in up to 60 months. All other income, including benefits-in-kind other than company car and free telephone, are taxed at the

ordinary rates. Such income includes any private income received by the expatriate from outside Denmark. In addition to the 26% tax, AM-contribution of 8 % must be paid.
Outbound expatriates are generally not taxed by Denmark on the salary, when the expatriation extends to more than 6 months.

United Kingdom

Any income from employment carried on in the UK is taxable in the UK unless the UK duties are incidental to the duties of a non-UK employment.
Inward expatriates to the UK do not receive any special allowances, although an expatriate receiving a salary from a non-resident employer may claim a deduction for items that would receive a deduction if a corresponding item payable in the UK would have been deductible. Expatriates may also receive limited non-taxable relocation costs and travel expenses from a UK or non-resident employer for himself and his family for journeys between home and his place of UK employment.
If an individual is present in the UK for more than 183 days in a tax year, technically he is considered tax resident, and therefore liable on his worldwide income and gains in the UK for the whole of the tax year. However, inward and outward expatriates from the UK may claim the so-called 'split year' treatment, which is a concession of the UK fiscal authority and not part of domestic law. To qualify, inward expatriates must arrive with the intention of staying for at least two years. Under the concession, an outward expatriate can claim to be treated as non-resident from the day following the day of departure provided that his absence from the UK is for a complete year of assessment, for the purpose of a full time contract of employment and his visits to the UK during the period amount to less than 183 days in any tax year and average less than 91 days a tax year over a maximum period of four years.
An individual who leaves the UK for the purpose of taking up full-time employment abroad will generally be regarded as ceasing to be resident from the date of departure.
Domicile, distinguished from residence has a special significance: an individual who is domiciled abroad, while being resident in the UK is taxed on the remittance basis in respect of foreign income and capital gains so that only income and gains from UK sources, or from non-UK sources but brought into the UK are taxed.

Article 16 Directors' fees

See treaty text

Directors' fees and other similar payments received as a resident of one State in a capacity as a member of a board of directors of a company resident in the other State may be taxed in that other 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.

United Kingdom

Directors' fees are regarded in the UK as remuneration for an office, and are taxed in the same way as employment income. They will therefore be taxable in the UK if and to the extent that the director performs the functions of his directorship (such as attending board meetings) in the UK.

Article 17 Artists and Athletes

See treaty text

The usual OECD Model rule is followed: 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.

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.

United Kingdom

Payments received by non-resident entertainers and sportsmen/women in respect of such activities in the UK are treated as deriving from a UK trade and are taxable accordingly. Payments made to other persons in respect of such activities are treated as being made to the relevant performer. All such

payments are subject to withholding tax, but this does not absolve the individual of his/her obligation to file a tax return and to pay any additional tax due.

Article 18 Pensions

See treaty text

The main rule in article 18 is that any pension or annuity paid to a resident of a Contracting State shall be taxable only in that State. However, the main rule is subject to the exception thereto in Article 19, par. 1 (see below) and par. 2-3 of this Article.

Par. 2 provides that in the case of an individual who was resident of one of the Contracting States and has become resident in the other, the first-mentioned State has the right to tax pension, annuities and other similar remuneration arising from that State. For instance if a Danish resident moves and become resident of the UK, then Denmark has the right to tax pension payments arising from Denmark to the (now) UK resident.

According to par. 3 pensions paid under the social security legislation of one of the Contracting States, are taxable in that same State.

Expert Analysis:

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 15, above). However, payments from a capital pension scheme are taxable at a flat rate of 40 percent. This tax is not covered by this Treaty.

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.

United Kingdom

Income from pensions and social security benefits is generally taxed in the same fashion as employment income, subject to certain specified exemptions.

Article 19 Governmental Payments

See treaty text

This Article contains rules for the taxation of a remuneration paid in respect of government service. Based on par. 1, salaries, wages and other similar remunerations, except pension payments, paid by a State 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 State if the services are performed in that other State by a resident who is also a national or not just became resident solely for the purpose of rendering the services.

Par. 1(c) was added by the 1991-protocol, and concerns embassy employees.

Pension payments to such employees are only taxable in the paying state. However, the other pension payments are only taxable in the other state, if the recipient is resident and a national of that other state.

Par. 3 determines that par. 1 of Article 19 do not apply to remuneration for services rendered in connection with the carrying on of a business. Such income will be dealt with under Articles 15, 16, 17 and 18.

Article 20 Students

See treaty text

Payments which a student or business apprentice who is, or was immediately before visiting a Contracting State, a resident of the other Contracting State and who is present in the visited State solely for the purpose of his education or training, receives for the purpose of his maintenance, education or training shall not be taxed in the visited State, provided the payments arise from sources outside that State.

Scientists are not covered by this article.

Denmark

The student allowance, which is the amount deemed by the tax authorities to be necessary for the maintenance and education of the foreign student is fixed at DKK 42,000 in 2013.

Article 21 Other Income

See treaty text
Any income not dealt with in the preceding Articles is taxable only in the State of residence, unless it is effectively connected with a permanent establishment or fixed base in the other state. .
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.
United Kingdom
This article will have limited effect as there are few categories of income taxed in the UK by reference to their source that have not been addressed in the preceding articles.

Article 22 Methods for the Elimination of Double Taxation

See treaty text
As main rule the tax credit method is applied to avoid double taxation. In cases where an income is subject to taxation only in UK, Denmark should apply the exemption-method.
By the latest protocol, a provision concerning taxation on profit paid from a UK subsidiary to a Danish parent (owning at least 25 percent). In this case, Denmark should avoid taxation provided the conditions set forth in art. 22(2)(d) is fulfilled.
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 United Kingdom 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 United Kingdom withholding tax.
United Kingdom
The UK historically generally relieved foreign tax by means of the credit method under its domestic law. However, from July 2009 a corporation tax exemption was introduced for most foreign dividends

received by UK companies, and the Government intends to introduce an elective exemption regime for the profits of foreign branches of UK companies from a date to be confirmed in 2011.

Article 23 Non-discrimination

See treaty text

The usual OECD provisions apply; that nationals of one of the States shall 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.

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.

Article 24 Mutual agreement

See treaty text

The provision is more or less identical to the non-discrimination provision in art. 24 of the OECD Model Tax Convention provision.

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 time limit for presenting the case is restricted to the usual three years from the first notification of the action resulting in taxation not in accordance with the provisions of the Treaty.

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.

United Kingdom

HM Revenue & Customs constitutes the competent authority for tax treaty purposes.

Article 25 Exchange of information

See treaty text

This Article provides for the exchange of such information "as is necessary" for carrying out the provisions of this Treaty or of the domestic laws of the two countries and is not restricted by Art. 1 (Personal scope) of this Treaty, but is restricted by art. 2 (Taxes Covered).

Article 26 includes the usual exemptions from the information exchange obligation, thus 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 of either State (although the obligation may go beyond information available in the normal course of administration); 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.

In February 2009, the EU adopted proposals for two new Directives: on mutual assistance in the assessment and recovery of taxes and on administrative cooperation in the field of taxation. The draft Directive on administrative cooperation will cover all taxes except VAT and excise duties and will

improve upon the current Mutual Assistance Directive by setting up common procedures, forms, formats of claims and channels for exchange of information. Tax officials of the requesting state will be permitted active participation in inspections and administrative enquiries. Importantly, banking secrecy may not be invoked as a reason for failing to supply information.

Article 26 Diplomatic Agents and Consular Officials

See treaty text

This Article follows Article 28 of the OECD Model Convention. 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 27 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.

Expert Analysis:

For Denmark, this would only be relevant if it were decided to include Greenland and/or the Faroe Islands hereunder. The UK has a separate tax treaty with the Faroe Islands.

Article 28 Miscellaneous Rules

See treaty text

This provision does not exist in the OECD Model Convention. The provision was more or less rewritten by the 1996-protocol.

Para. 1 provides Denmark with a secondary right to levy tax on individuals resident in the United Kingdom in receipt of income taxed on the remittance basis. This, broadly speaking, applies to individuals who are either not ordinarily resident or not domiciled in the UK, and provides that certain foreign source income is not taxed in the UK unless or until it is remitted to the UK. Article 28(1) provides that relief is only allowed in Denmark under the treaty in respect of income that is actually taxed in the United Kingdom. Thus, the amount that is not subject to tax in the United Kingdom, remains taxable in Denmark to the extent that domestic law so provides.

Article 28A Miscellaneous Rules Applicable to Certain Offshore Activities

See treaty text

This provision does not exist in the OECD Model Convention. It was added due to the 1991-protocol. Offshore activities situated in the other state constitute a permanent establishment/fixed base, if the activities are carried out in connection with the exploration for or exploitation of oil and gas in the sea-bed and subsoil,

Salaries, wages and similar remuneration are taxable in only in the state wherein the services was provided. There is a secondary right, for the other Contacting State to tax such remuneration. This is the case where documentary evidence for the tax payments cannot be produced.

Article 29 Entry into Force

See treaty text

The Treaty entered into force as per income year 1978. The protocol of 1 July 1991 entered into force as per 1 January 1992 in Denmark and in UK as per income year starting 6 May 1992. The protocol of 15 October 1996 entered into force as per 1 January 1998 in Denmark and in UK as per income year starting 6 May 1998.

Article 30 Termination

See treaty text

In the event of the Treaty being denounced before 1 July in any year, the Treaty will be terminated as per the following income year.