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DANISH TAX AND VAT NEWS IN ENGLISH

Foreign source income and relief for double taxation

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A recent verdict by the High Court may result in an increased total tax burden for some taxpayers earning foreign source income.

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The case before the High Court concerned the attribution of expenses to Danish and foreign source income respectively, thus influencing the maximum amount of foreign taxes to be offset against Danish taxes.

Background

When a Danish resident taxpayer earns income from foreign sources, this income may be taxable in the country of source as well as in the country of residence, Denmark.

In order to avoid double taxation, often, the Danish taxes on the foreign source income shall be reduced by an amount equal to the foreign taxes paid. However, the Danish taxes cannot be reduced by more than the Danish taxes attributable to the foreign source income.

Hence, if the calculated Danish taxes on the foreign source income are lower than the foreign paid taxes on said income, the foreign taxes cannot be fully offset against the calculated Danish taxes.

The law stipulates that deductible expenses directly referable to the foreign source income shall be deducted in the foreign source income as opposed to income from Danish sources. This entails a reduction of the Danish taxes attributable to the foreign source income.

Deductible expenses not directly referable to either Danish or foreign source income shall be divided between the Danish and foreign source income based on the ratio between the Danish and foreign source gross income.

Consequently, the Danish taxes attributable to the foreign source income may be the limiting factor for reduction of Danish taxes in order to avoid double taxation.

In other words, the foreign taxes may exceed the Danish taxes attributable to the foreign source income thereby preventing complete offset of foreign taxes.

Naturally, taxpayers would prefer to fully offset the foreign taxes. Hence, it will be preferable to be able to refer deductible expenses to Danish source income to the largest extent possible in order to attribute a larger part of the total Danish taxes to the foreign source income thereby raising the threshold for offsetting foreign taxes.

However, according to a recent case, the High Court ruled in favour of the Danish tax authorities in this respect.

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Consequently, certain deductible expenses of a Danish company were divided between the Danish and foreign source income instead of being referred entirely to the Danish source income.

According to the High Court, an individual assessment must be made in reference to each deductible expense in order to determine whether the expense should be attributable entirely to either foreign or Danish source income. In lack hereof, the expense must be divided between the foreign and Danish source income as described above.

Offhand, the verdict seems rather harsh, as the company appeared to have solid arguments that the expenses in question could be referred to the Danish source income instead of being divided proportionately between the Danish and foreign source income.

If the Danish company does not appeal the verdict to the Supreme Court, or if the Supreme Court upholds the verdict of the High Court, taxpayers may experience increased difficulties in referring expenses solely to Danish source income and additional effort may be required to provide solid arguments that expenses can indeed be attributed the way the taxpayer wants.

Tax exemption when working abroad

An employee paid by the hour for work performed abroad including transportation time to and from his home in Denmark was granted tax exemption on the salary.

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A special Danish tax provision allows employees to be tax free in Denmark on salary for work performed abroad under certain conditions.

The conditions entail that the employee must stay abroad for at least 6 months.

During any 6-month period of the stay abroad, the employee may only visit Denmark for a maximum of 42 days. Travel days where the employee spends part of a day in Denmark count as whole days in Denmark in this respect.

When the employee visits Denmark, it must as a main rule be for holiday purposes etc. only. The employee may only perform work in Denmark if it can be substantiated that the work relates directly to his work abroad and it is necessary that he performs this work in Denmark.

This last condition was the subject of a recent ruling by the National Tax Tribunal. The case concerned an employee working in Sweden. The employee was remunerated by the hour and was paid for the travel time between his country of work, Sweden, and his home in Denmark.

The Danish tax authorities argued that the travel time - for which the employee was remunerated - did not constitute necessary work performed in Denmark. For that reason, the conditions for utilizing the tax exemption rule were not met in the opinion of the Danish tax authorities.

The National Tax Tribunal was of another opinion and ruled in favour of the employee. The transportation time in Denmark was not considered work. Hence, the remuneration for the transportation time did not constitute salary for work performed in Denmark meaning that the employee met the conditions for tax exemption on his salary.

The ruling by the National Tax Tribunal seems fair. Had the employee been paid by the month, there would likely not have been an issue to begin with which makes it difficult to understand that remuneration by the hour in itself should disqualify for tax exemption.