



TAX:WATCH

The National Tax Tribunal rules against the taxpayer in TP case

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The National Tax Tribunal agreed with the Danish tax authorities that, in determining the group settlement prices of a production company, the return requirements for financial investments cannot be taken into consideration.

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Although the Danish tax authorities have been defeated in several major transfer pricing cases in recent years, some cases concerning transfer pricing - typically in slightly larger groups - have been decided in favour of the tax authorities.

This is exemplified well by a recent publicised ruling from the National Tax Tribunal.

The foreign production company

The case concerned a Danish group, which in 2006 invested more than DKK 100,000,000 in establishing a production company in another jurisdiction featuring a significantly lower wage level than the Danish wage level.

The purpose was to expand the production capacity at a lower cost level.

The foreign subsidiary was rated as contract manufacturer for the Danish parent company.

This meant that the subsidiary only produced for the parent company and did not sell to others, as the parent company itself was responsible for product development, procurement of raw materials and production planning.

The pricing of inter-group sales from the production company to the parent company was based on the cost-plus-profit method with a mark-up of 10 %, aiming for an EBIT margin of 9.1 % at the production company.

In the opinion of the Danish tax authorities, this was much too high.

Consequently, the Danish tax authorities increased the taxable income of the Danish parent company by an amount in the multi million DKK range.

In the case before the National Tax Tribunal, the company argued that in assessing the pricing, not only the actual value of the production should be taken into consideration.

Additionally, the production company should receive a return corresponding to the risk-free interest plus a risk premium.

However, the National Tax Tribunal disagreed. In the ruling, the National Tax Tribunal sided with the Danish tax authorities and stated, that the OECD Transfer Pricing Guidelines do not support, that the pricing can be based on assessments of return on investment requirements.

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A major clean-up work is waiting

Whether the ruling will be brought before the courts remains to be seen. If not, the group can expect a major clean-up work.

Initially, for the years 2009-2012, which the case concerned, a correction of the tax assessment for the foreign subsidiary can likely be claimed, corresponding to the amounts that are taxed in Denmark as a consequence of the ruling by the National Tax Tribunal.

Subsequently, and in close cooperation with the tax authorities of the two countries, awaits correction of the tax assessment of both the Danish parent company and the foreign subsidiary for the years 2013-2017 as well as determination of the future group pricing.

The case is also a good example of the time required when dealing with tax cases.

The ruling by the Danish tax authorities was brought before the National Tax Tribunal in October 2015, where it was pending for two and a half years.

Before then, the case had likely also been pending before the Danish tax authorities for at least a couple of years.

The lengthy casework times combined with the significant costs involved, often lead companies to seek a settlement with the Danish tax authorities in cases concerning transfer pricing.

New rules on Danish tax residence for individuals are postponed

Non-resident individuals owning real property located in Denmark must wait a bit longer before knowing, how their Danish tax position will be in the future.

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As described in the March 2018 issue of tax:watch, the government recently proposed new rules on Danish tax residence for individuals.

Originally, the plan was for the bill to be proposed to and adopted by the Danish parliament before the end of session of the parliament this summer.

However, due to the many comments and objections received by the Minister of Taxation concerning the draft bill, the Minister of Taxation has decided to postpone the bill until autumn, when the Danish parliament reconvenes.

The objections have mainly focused on non-resident individuals living in low or zero tax jurisdictions owning a second home in Denmark.

According to the proposed draft bill, such individuals could suddenly risk exposure to Danish tax on their global income regardless of the length of their stay in Denmark.

In connection with the postponement, the Minister of Taxation expressed that he expects the final bill will be amended in order to better accommodate companies expatriating employees to work abroad.

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