Direct Tax News Alert

Future dividend tax regime in Denmark from 2023 will be based on a relief-at-source mechanism

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The Danish Minister of Taxation has recently stated in a press release that the Ministry of Taxation has entered into an agreement with Finance Denmark (The Danish Banking Association) regarding new principles for taxation of dividends paid to foreign investors.

The current regime

Under the current regime, 27% tax on dividends is withheld at source when the dividend is distributed to foreign shareholders. The foreign shareholders can reclaim the part of the dividend tax which exceeds the rate according to the relevant double taxation agreements, etc. which is typically 15%. Applying for a refund requires the shareholder to provide the tax authorities with relevant documentation after the dividend distribution. It is an administratively heavy regime that involves the risk of errors and fraud.

The new regime

The new regime is a relief-at-source regime where the dividend tax is withheld at the correct rate at the time of distribution i.e. down to the tax rate according to the double taxation agreement, etc. The relief-at-source will by default make reclaims of dividend tax obsolete. The new relief-at-source regime requires the foreign shareholders to be registered with the Danish tax authorities prior to the dividend payment to obtain a unique identification number, which is used to identify the shareholder's shares and tax rate.

Registration must be made via the shareholder's custodian bank and the shareholder must declare that the beneficial owner requirements in relation to the shares and the dividend are fulfilled under Danish tax law. The declaration describes the situations in which the immediate recipient of the dividend under Danish tax rules cannot be regarded as the beneficial owner, for example for certain types of security lending. However, institutional investors, such as pension funds, that are entitled to a particularly low dividend tax rate must go through a pre-approval procedure with the Danish tax authorities to obtain the low rate.

By the agreement, the banks are responsible for errors if it subsequently turns out that the dividend tax has been withheld at a too low rate. The banks' liability covers situations where errors have been revealed in samples, for example when applying the wrong tax rate or the recipient is not the beneficial owner of the dividend. However, this does not apply to institutional shareholders who must be pre-approved by the Danish tax authorities.

According to the agreement, an explicit premise for the participation of the Danish banks in the new regime is that they will be able to make recourse claims against the foreign banks which have contributed to the incorrect registration. However, it has not yet been determined how such mechanisms will be implemented in practice

The bill to introduce the new regime has been postponed several times. The Ministry of Taxation has recently announced that the bill is expected to be put forward in the parliamentary year 2020/2021. This means that the new regime will probably not come into effect until 2023 as the regime requires significant IT system customization, etc.

Limited possibility for reclaims

In the interests of shareholders who have not been able to obtain an identification number from the tax administration yet, it is under the new regime possible for the shareholder to reclaim excess tax withheld from the tax administration within a short period. The recovery requires the shareholder to register with the tax administration via the custodian bank and be issued an identification number.

Takeaways

The background to the new regime is the desire for administrative simplification and that future fraud should be avoided. However, the result may be that foreign investors lose appetite for Danish equities if, for some reason, it turns out that foreign banks do not wish to join the new regime. Hence, PwC Denmark recommends that the new regime be implemented as flexible as possible, or alternatively that the implementation of the similar OECD relief-at-source model (OECD TRACE) is awaited which is at the moment considered implemented in the OECD Member Countries.