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FS Newsflash

Danish Supreme Court rejects Fidelity Funds' withholding tax reclaim on Danish sourced dividends (Fokus Bank Claim)

Introduction

On 24 June 2021, the Danish Supreme Court denied the refund of withholding tax on Danish sourced dividends suffered by non-resident investment funds.

The investment funds are resident in the United Kingdom and Luxembourg and qualify as Undertakings for the Collective Investment of Transferable Securities ("UCITS") (hereafter "the Funds" or "the Claimants"). The Funds invested in Danish shares and received dividends in the period 2000-2009, which were subject to Danish withholding tax ("WHT").

The main question in the cases concerned was whether non-resident investment funds could be subject to WHT on dividends received from their Danish shares while resident investment funds in Denmark that have elected status as an investment fund with minimum taxation are tax exempt on Danish sourced dividends.

The Danish Supreme Court's judgement

Previously, the Danish Eastern High Court had referred the question of compatibility of the Danish tax rules on WHT for investment funds to the Court of Justice of the European Union ("CJEU") (Fidelity Funds (C-480/16)).

The CJEU stated in its preliminary ruling from June 2018 that Article 63 TFEU must be interpreted as precluding legislation of a Member State, such as that at issue in the main proceedings, under which the dividends distributed by a company resident in that Member State to a non-resident UCITS are subject to WHT, while dividends distributed to a UCITS resident in that same Member State are exempt from such tax, provided that the undertaking makes a minimum distribution to its members, or technically calculates a minimum distribution, and withholds on that actual or notional distribution the tax payable by its members.

Surprisingly, on 2 April 2019 the Eastern High Court ruled against the CJEU ruling in favour of the Danish government. The Claimants appealed the ruling to the Danish Supreme Court.

The Danish Supreme Court outlined in its judgement that there are two conditions that must be met for a non-resident UCITS to receive Danish sourced dividends tax-free; (i) they are domiciled in Denmark and (ii) they have elected the status as an investment fund with minimum taxation for the relevant years.

The Danish Supreme Court opined that the CJEU in its Judgement had ruled that only the Danish domicile criterion was ruled out as a breach of EU law while the remaining part of the Danish tax scheme for investment funds was maintained. Based on that, the Danish Supreme Court opined that a foreign UCITS must have tax status as an investment fund with minimum taxation for the relevant income years in question in order to be entitled to a refund of the Danish dividend WHT. Hence, the Danish Supreme Court rejected the Fidelity Funds' WHT reclaim based on the fact that none of the Claimants had elected the status as a Danish investment fund with minimum taxation.

The Danish Supreme Court argued that section 16 C in the Danish Tax Assessment Act (in Danish “ligningsloven”) was justified in the need to ensure the coherence of the Danish tax system and to ensure an effective control. This result is surprising, as the CJEU reached the complete opposite result in paragraph 86 of their judgement, where the CJEU opined that the restriction resulting from the application of the tax legislation to issue in the main proceedings cannot be justified by the need to safeguard the coherence of the Danish tax system.

The Danish Supreme Court very surprisingly also disregarded the fact that even if the non-resident investment funds had elected the Danish status as a investment fund with minimum taxation in the relevant years, the investment funds would not have been able to benefit from the tax exemption due to the Danish domicile criterion. Moreover, the Danish Supreme Court disregarded the fact that an obligation to calculate a minimum income would probably also be an unlawful discrimination of non-resident investment funds, since those rules most likely constitute a discriminating technical trade barrier themselves.

Takeaway

The Danish Supreme Court’s judgement cannot be appealed to a higher court in Denmark.

On one hand, it will generally be possible to argue in pending cases that the Danish Supreme Court judgement is not in line with CJEU Judgement. On the other hand, it should be considered whether the client is able to document that the fund has been covered by foreign tax regimes, where the investment fund calculates income components that are distributed or reported to the investors annually. The aim is to show that the client has been in a comparable situation with investment funds that have the Danish tax status as investment fund with minimum taxation.

It is expected that the reclaims in all pending cases before the Danish Tax Agency and National Tax Tribunal will most likely be denied. A decision from the National Tax Tribunal can be brought before the Danish courts, but it might be difficult to convince the Danish courts that additional questions should be referred to the CJEU. At the end the result might be, that the judgement from the Danish Supreme Court will remain unquestioned.

At this moment there should most likely be no basis for filing new reclaims with the Danish Tax Agency. Also please note that as of 1 January 2022, the Danish tax legislation has been amended by imposing a 15% WHT on Danish sourced dividends received by Danish investment funds with minimum taxation status. Consequently, non-resident investment funds are no longer subject to discrimination.

The judgement clearly shows that the legal framework where national courts refer questions to the CJEU for preliminary rulings might not always be a sufficient remedy to secure fundamental rights under the TFEU especially in complex cases like the Fidelity Funds case. The correct outcome is among others highly dependent on all relevant questions being referred to the CJEU by the national courts in the first place.

PwC Denmark

Anne Cathrine Primdal Allentoft	Partner	+45 51 38 47 86	anne.cathrine.primdal.allentoft@pwc.com
Søren Jesper Hansen	Partner	+45 20 30 47 94	soren.jesper.hansen@pwc.com
Susanna f. Bjerrum Poulsen	Partner	+45 51 38 49 54	susanne.f.bjerrum.poulsen@pwc.com
Morten Bang Mikkelsen	Director	+45 29 60 40 55	morten.bang@pwc.com
Henrik Laust Poulsen	Director	+45 52 19 03 41	henrik.poulsen@pwc.com