

CJEU hands down important judgments in Danish cases on beneficial ownership

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In Brief

On 26 February 2019, the Court of Justice of the European Union (CJEU) issued its judgments in *T Denmark and Y Denmark vs. the Danish Ministry of Taxation* (Joined Cases C-116/16 and C-117/16 – “the dividend cases”) and in *N Luxembourg 1, X Denmark A/S, C Danmark I and Z Denmark ApS vs. the Danish Ministry of Taxation* (Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16 – “the interest cases”). The underlying question of the cases was whether dividend and interest payments were exempt from withholding tax, when the payments were made from a Danish company to a company resident within the EU if the payments were fully or partially passed on to an ultimate parent company resident in a third country.

Facts

In the cases, the Danish companies were all owned by a parent company resident in another EU Member State (Luxembourg, Cyprus or Sweden). The EU parent companies were all directly or indirectly owned by companies resident in third countries (e.g. Bermuda or the Cayman Islands) or by private equity funds with unknown residency of the investors. The Danish companies paid out either dividends or interest to their EU-resident parent companies, and claimed that such payments of dividend or interest was free of withholding tax in accordance with the Parent-/Subsidiary Directive (PSD) or the Interest/Royalty Directive (IRD).

The Danish tax authorities claimed that the withholding tax exemptions following from the PSD and IRD should not be granted, as the recipients were not the beneficial owners of the payments. The cases were appealed to the Danish High Court, which referred questions to the CJEU.

The referred questions in the dividend and interest cases are generally the same, but the question on beneficial ownership (see below) was only asked in the interest cases, as it is a requirement in the IRD that the recipient is the beneficial owner of the interest, whereas this is not a requirement in the PSD.

Judgments

In the interest cases, the first question was whether the recipient of the interest was the beneficial owner, and thereby could enjoy the

withholding tax exemption following from the IRD. The CJEU first stated that the term “beneficial owner” concerned not a formally identified recipient but rather the entity which benefits economically from the interest. The CJEU considered the OECD Commentary on the OECD Model Tax Convention to be relevant for interpreting the term “beneficial owner”.

In case the conditions for obtaining the withholding tax exemption in the IRD or the PSD were formally met, the Danish High Court asked if it was necessary for an EU Member State to implement an anti-abuse provision in its domestic law in order to deny any benefit following from the IRD or PSD. The CJEU stated that the general EU anti-abuse principle implied that an EU Member State has to deny such benefit if an arrangement constitutes abuse of rights irrespective of whether any specific anti avoidance legislation has been implemented in domestic law.

The CJEU provided guidance on when an arrangement constitutes abuse of rights. If the funds are passed on wholly or partially shortly after they are received, this may serve as an indication that the entity is a flow-through or conduit and this could be an indicator of abuse. It is not a requirement that there is a contractual obligation to pass on the payment. Further, an indication for abuse may be if the recipient lacks substance or has been interposed in a structure that otherwise wouldn't be covered by the IRD or PSD. The fact that the ultimate parent is resident in a third country, with which a tax treaty has been concluded, can neither prove nor disprove an abuse of rights.

Regarding the burden of proof, the CJEU stated that an EU Member State is obliged to prove that an arrangement is abusive, but if the authorities conclude that the recipient of the income is not the beneficial owner, they are not obliged to determine which entity is the actual beneficial owner.

Takeaway

It is now up to the Danish High Court to decide the final outcome of each case based on the guidance from the CJEU whether in fact the recipients are the beneficial owners and/or whether there is an abuse of rights. In the meantime, however, these judgments will be extremely important for the application of the IRD and PSD going forward and also more generally for the interpretation of terms such as “beneficial owner” or “abuse of rights”.

The cases have a significant impact on most international group structures, international real estate funds and REITs and the flow of funds from EU subsidiaries to parent companies when the ultimate parent is resident in a third country. The German Ministry has been awaiting these judgments with a view to reconsidering the wording of existing anti-treaty shopping provisions (please see previous [NewsAlert](#)).

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