
Chapter 12

Australia: Transfer Pricing*

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12.1. Introduction

The edifice that is the lore of transfer pricing often seems to outsiders to lack the kinds of rigours that are associated with more traditional cross-border tax issues. It seems to be a sealed box filled with obscure contents, where practitioners speak a special dialect, communicate only with each other and use methods of analysis that are arcane and entirely fictional. There is much writing and deep theory, but it seems so abstruse and artificial that it ceases to be convincing.

Occasionally, however, transfer pricing must emerge into the real world and be tested under the scrutiny and by the standards of judges who are expecting something rigorous.

In Australia, very few transfer pricing cases have ever been litigated,¹ and when they have, the results have not been what the tax authorities had hoped. *Commissioner of Taxation v. SNF (Australia) Pty. Ltd*² is a prime example. The failure in Australia to produce a deep and rich body of jurisprudence on substantive transfer pricing law means that any new case will likely throw up some novel and unexpected learning.

* AU: Full Federal Court (FFC), 1 June 2011, *Commissioner of Taxation v. SNF (Australia) Pty. Ltd.* [2011] FCAFC 74, Tax Treaty Case Law IBFD.

1. The few examples of substantive transfer pricing issues being litigated are *Roche Products*, [2008] AATA 639; *SNF (Australia)* [2011] FCAFC 74; and the so-called “oil industry case” “in the 1960s, case N69 (1963) 13 TBRD 270. On the other hand, there have been many procedural skirmishes; see e.g. *Commonwealth Aluminium Corporation*, [1980] HCA 28; *WR Carpenter Holdings*, [2008] HCA 33; *Daihatsu Australia*, [2000] FCA 1718; *Daihatsu Australia*, [2001] FCA 588; *Syngenta Crop Protection Pty Ltd (ACN 002 933 717)*, [2005] FCA 1646; *FH Faulding & Co.*, [1994] FCA 1492; *San Remo Macaroni*, [1998] FCA 610; *San Remo Macaroni*, [1998] FCA 634; and *San Remo Macaroni*, [1999] FCA 1468.

2. AU: Full Federal Court (FFC), 1 June 2011, *Commissioner of Taxation v. SNF (Australia) Pty. Ltd.* [2011] FCAFC 74, Tax Treaty Case Law IBFD.

The lesson of *SNF* is that when someone from outside the transfer pricing world examines the lore that has been developed, the edifice seems to be a house of cards.

12.2. Facts of the case

SNF was a French-based multinational group in the chemicals industry. The taxpayer was an Australian resident distributor of chemicals which it purchased from related offshore suppliers in France, the United States and China. Intra-group prices were determined by the holding company, SNF France.

The Australian subsidiary suffered operating losses every year from 1998-2004. The Commissioner apparently viewed the continuing losses as incontrovertible evidence that the prices paid by the Australian subsidiary for supplies were higher than arm's length prices: "The Commissioner contended that these losses, which the trial judge found [...] would have forced an independent operator from the market, provided powerful support for his case".³ The Commissioner issued assessments claiming AUD 2 million in additional tax, penalties and interest, relying on the domestic transfer pricing provisions.

Far from conceding the point, the taxpayer argued that it was in fact underpaying for the chemicals it purchased: "The taxpayer's case was that it had generally paid less for the polyacrylamides it had purchased from the suppliers than independent third party purchasers had".⁴

Domestic law. The case was argued on the basis that the Commissioner had the power to adjust the prices for the purchases of chemicals by relying on the domestic transfer pricing rule:

Section 136AD. Arm's length consideration deemed to be received or given

(3) Where:

- (a) a taxpayer has acquired property under an international agreement;
- (b) the Commissioner, having regard to any connection between any 2 or more of the parties to the agreement or to any other relevant circumstances, is satisfied that the parties to the agreement, or any 2 or more of those parties, were not dealing at arm's length with each other in relation to the acquisition;

3. Id. at para. 6.

4. Id. at para. 12.

- (c) the taxpayer gave or agreed to give consideration in respect of the acquisition and the amount of that consideration exceeded the arm's length consideration in respect of the acquisition; and
 - (d) the Commissioner determines that this subsection should apply in relation to the taxpayer in relation to the acquisition;
- then, for all purposes of the application of this Act in relation to the taxpayer, consideration equal to the arm's length consideration in respect of the acquisition shall be deemed to be the consideration given or agreed to be given by the taxpayer in respect of the acquisition.⁵

Because the case was lost under the domestic law – the claim to tax under domestic law could not be sustained – the Court never had to consider the treaty issues which the case raised.

Nevertheless, the Court did examine – and make some startling comments on – the OECD Transfer Pricing Guidelines and their usefulness in interpreting domestic law and treaty provisions.

12.3. The Court's decision

At first instance, the Court was unpersuaded by the Commissioner's analysis:

the Commissioner was wholly unsuccessful in persuading the trial judge to the view that the taxpayer's persistent losses were caused by the prices it was paying to its suppliers. Instead, and to the contrary, the trial judge found [...] that the losses were caused by a congeries of factors – unreasonably low sales per salesperson resulting in higher levels of commercial costs expressed as a percentage of sales; competition in the Australian market; excessive stock levels; poor management – none of which included the Commissioner's contention that the losses had arisen from the transfer of 'profits' to the suppliers.⁶

The Commissioner lost the appeal to the Full Federal Court.

The appeal court's reasoning necessarily addresses the arguments put to it which, in an appeal, typically focus on particular failings said to be evident in the lower Court's judgment. Because the appeal was mostly directed to alleged problems in the lower Court, the focus on the substantive issues was often less than comprehensive. Nevertheless, the judgment of the appeal court does address issues of process (issues of evidence and proof), as well as substantive issues (choice of method, meaning of comparability, accept-

5. Sec. 136AD Income Tax Assessment Act 1936 (Cth) (Australia).

6. *Commissioner of Taxation v. SNF (Australia) Pty. Ltd.*, supra n. 2, at para. 7.

able adjustments and so on), while finding few of the faults claimed by the tax authorities to be evident in the lower court's judgment.

12.4. Comments on the Court's reasoning

The decision of the appeal court revolved around three principal issues:

- whether the trial judge had erred in the findings of fact. The arguments were that evidence was led by the taxpayer which was not admissible, and that the admissible evidence was not sufficient to support the conclusion that the transactions relied on by the taxpayer were comparable;
- the trial judge should not have accepted evidence from one of the suppliers that it suffered losses on the sales to the taxpayer; and
- the trial judge inappropriately viewed some transactions as comparable.

Evidence and proof in transfer pricing disputes. On appeal, much of the case argued by the tax authorities revolved around disputes about evidence and proof – what evidence is acceptable in a court, how facts are proved in this type of litigation and what that evidence must prove. The report of the case spares the reader much of the detail of the comparability assessments and pricing adjustments which must have occurred, and the evidence which had been led, although some of that information in summary form is appended to the judgment.

At trial, the taxpayer presented three sets of data to support its argument that it was paying less than the arm's length price:

- Data Set 1: details provided by executives of the French supplier of the prices it charged on sales of products in the same family of chemical products to five specified unrelated foreign companies and their subsidiaries. This data set was limited just to:
 - buyers of similar quantities to the taxpayer; and
 - customers who were viewed by the person who prepared the list as “suppliers” rather than users of the chemicals.Only one customer in this group of companies operated in Australia.
- Data Set 2: details provided by same executives of the prices charged on sales of seven named products, but limited just to sales to three companies operating in Australian and New Zealand.

- Data Set 3: prepared by the taxpayer's expert, details of sales by the French supplier of individual products (not product groups) to a larger set of 21 companies.

As the Court observed, this evidence was all presented on the assumption that these sales to third-party purchasers reflected an arm's length price, and that the taxpayer was paying less than this price.

The validity and reliability of the data being presented were the subject of much dispute in the case. Indeed, Data Set 2 was prepared by the taxpayer in response to claimed deficiencies in Data Set 1, and Data Set 3 was prepared by the taxpayer in response to claimed deficiencies in Data Set 2. According to the taxpayer, each Data Set simply confirmed the basic story. According to the Commissioner, the deficiencies of each Data Set were so large that these prices could not be used, and a profit-based method had to be adopted instead.

The criticisms of the data which emerged during the trial were many:

- Data Set 1 and Data Set 2 presented the prices charged for groups of chemical products, not for individual products – hence Data Set 3;
- sales to buyers that were not in Australia should be rejected;
- the Data Sets focussed on sales made just by the French supplier, not all suppliers – and SNF had purchased from related sellers in China and the United States, as well;
- there was no admissible evidence to show that the judgment made about which customers were also distributors, was reliable;
- there was no evidence to show that these distributors were placed in a similar place in the supply chain – they may have resold to users, or resold to suppliers; and
- the methodology behind the adjustments that were made to the raw prices to make them more comparable was unproven, particularly the adjustments that ought to be made for the contract terms the customers had negotiated which differed from the terms for sales to the taxpayer:
 - time for payment: the taxpayer was obliged to pay on delivery, while unrelated customers were allowed 14 to 90 days for payment;
 - adjustments made for volume rebates; and
 - transport costs were removed (because some sales did not involve delivery by the seller).

However, it seems from the report of the case that some adjustments made by the staff of the French parent company and by the taxpayer's expert were not contested:

- limiting the sample size just to customers that bought in similar volumes;
- the rates used for currency conversions (given that customers paid in currencies other than AUD); and
- the time at which currency conversions should be made – the invoice date.

Proving the arm's length price. The Commissioner's first attack against the data was procedural, arguing that much of the evidence upon which the data sets were constructed was hearsay and inadmissible.

The particular concern was that the SNF executive who compiled Data Sets 1 and 2 had no direct knowledge to support his position that the companies selected were "distributors", like the taxpayer. Arguments then shifted to whether that failing could be resolved in other ways – by tendering documents such as the customers' annual reports or by inference from evidence about the size of the sales to these customers, or whether the Commissioner's objections to accepting the evidence came too late in the proceedings (it had been admitted without objection and only later objected to). The Court concluded that there was sufficient admissible evidence to support the trial judge's conclusions that the companies in Data Set 1 were distributors.

Conclusions about transfer pricing law. Even though much of the case concerned matters of evidence, there are a number of conclusions about transfer pricing law which emerge from the judgment.

Selection of method. The taxpayer argued that the price it had paid was in fact less than the arm's length price because it had paid less than the amount the three suppliers had charged to independent parties in transactions it said were comparable:

[the experts] agreed that an analysis based on a consideration of such comparable transactions was the preferable approach if such comparable transactions were available. [The taxpayer's expert] thought that they were available and based his analysis upon them. [The ATO's expert] however disagreed; there were, in his opinion, no suitable comparable transactions available.⁷

7. Id. at para. 4.

The Commissioner argued that the transactions were not comparable and so the arm's length price should be determined by the transactional net margin method.

The Court agreed with this approach, namely that where comparable sales can be found, the CUP method must be used, and it is only where there is insufficient evidence that other methods come into play:

so long as appropriate comparable transactions were available, an analysis of relevant comparables was appropriate. [The Commissioner's expert] thought the comparables approach was inapplicable because proper comparables were not available. It was that paucity of comparables which drove him to use the TNMM. It follows from our acceptance that the existence of an extensive range of comparables has been established that the premise on which [the expert's] use of the TNMM rested is not made good. The Commissioner's submission that the trial judge should have accepted the TNMM is, therefore, incorrect.⁸

How similar is comparable? The Commissioner also argued that the test of an arm's length price "required one to assume a set of facts in which the purchaser was an entity with all of the qualities of the taxpayer except its relationship to the parent manufacturers [...]". This meant that purchases by unrelated parties would be comparable only if they were purchasers that also suffered similar losses.

The Commissioner argued that this followed from the fiction which the statute prescribed:

The Commissioner submitted that [the relevant sections] together required the positing of a hypothesis. The hypothesis was to consist of an arm's length purchaser in identical circumstances to the taxpayer; in practice, a comparator with all of the qualities of the taxpayer relevant to price save its membership of the SNF Group. On the particular facts of the case, this confined comparable purchasers to those who had a similar history of losses to the taxpayer.⁹

The Full Court stated the Commissioner's submission that comparable purchasers must have identical traits to the taxpayer was "deeply impractical" and overly inflexible – a taxpayer could never discharge the onus of proof under such an interpretation:

But what is to occur, one may ask, if no such comparables are available; what if there exists no other business sharing all the same features of the taxpayer bearing on price so that the crystalline perfection the Commissioner submits is demanded by s 136AA(3)(d) cannot be achieved? The Commissioner's submis-

8. Id. at para. 71.

9. Id. at para. 92.

sion necessarily means that a taxpayer, who bears the onus in tax appeals, can never succeed in such a case for the bar will be set at an unattainable height [...]. It is highly unlikely that the *Guideline*'s reference to comparable circumstances was intended to bring about such eccentric outcomes.¹⁰

Relevance of OECD Transfer Pricing Guidelines. The Commissioner argued that his interpretation and practice – this strict notion of comparability – was in accordance with the OECD Transfer Pricing Guidelines¹¹ and should be adopted for that reason. The Court disagreed that the OECD Guidelines were expressed as strictly as this:

[...] the guidelines upon which the Commissioner seeks to rely make clear that such outcomes were not contemplated at all by the OECD. For example, it did not intend that only such rigidly identical comparables should be brought to bear: 'To be comparable means that none of the differences (if any) between the situations being compared could materially affect the condition being examined in the methodology (eg price or margin), or that reasonably accurate adjustments can be made to eliminate the effect of any such differences' (guidelines at [1.15]). It followed that 'when making the comparisons entailed by application of the arm's length principle, tax administrations should also take these differences into account' [...]

What that reveals is not that the OECD guidelines required that the only comparables which might be considered were those in identical circumstances to the taxpayer but rather that those differences which were material should be taken into account through a process of adjustment. For making the adjustments the OECD guidelines suggested the use of a methodology to take account of material differences.¹²

Moreover, the Court noted that it was examining Australian domestic law, not a treaty, and it was not obvious how the Guidelines came to be relevant to domestic law, although the distinction was not watertight. The Court noted that Australia had concluded treaties with France, the United States and China, and that each treaty had become domestic law in Australia by virtue of being enacted as a Schedule to the International Tax Agreements Act 1953 (Cth). Hence, the discussion which follows in the judgment is in fact analysing Australian domestic law – being the relevant treaties.

The Court noted that each of those treaties contained an equivalent to article 9 of the 2010 OECD Model. While the Commentary to the OECD Model was relevant to the interpretation of the treaty (it is regarded as providing

10. Id. at para. 102.

11. OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD, 1995). The case did not mention the 2010 revision of the Guidelines.

12. *Commissioner of Taxation v. SNF (Australia) Pty. Ltd.*, supra n. 2, at para. 106.

“context” for the interpretation of the treaty), the Commentary provided no support for the strictness of the test of comparability.

The Court then separately considered the OECD Guidelines and examined their status as a matter of international law and the weight that should be afforded to them.

It noted that the Guidelines were not part of the Commentary and were expressed to be “guidelines”. Under the Vienna Convention, the Guidelines might be examined if they reflected subsequent agreement or practice of the parties to the treaty which “establishes the agreement of the parties regarding its interpretation”, but this would require evidence (which was not led) that “each of China, the US and France had either agreed to apply the portion of the guidelines relied upon [...] or that it was their practice to do so”.¹³ This meant that the Guidelines could not be used to interpret the meaning of Australia’s domestic transfer pricing legislation.

12.5. Conclusion

Everything depends on prices. The first thing to note about this case is the way it came about – a resident subsidiary of a multi-national enterprise was suffering continued losses. From this simple fact, the Commissioner deduced that there was a transfer pricing issue.

This preoccupation with prices is clearly a symptom of a fixation of some kind. The Court was not so blinkered. Companies suffer losses for many reasons; prices on transactions with related parties may be the least significant. Clearly, the Courts did not view the entire world of tax through the prism of pricing:

the Commissioner was wholly unsuccessful in persuading the trial judge to the view that the taxpayer’s persistent losses were caused by the prices it was paying to its suppliers. Instead, and to the contrary, the trial judge found [...] that the losses were caused by a congeries of factors – unreasonably low sales per salesperson resulting in higher levels of commercial costs expressed as a percentage of sales; competition in the Australian market; excessive stock levels; poor management – none of which included the Commissioner’s contention that the losses had arisen from the transfer of ‘profits’ to the suppliers.¹⁴

13. Id. at para. 116.

14. Id. at para. 7.

The problems of evidence. Secondly, the case shows a fundamental issue for revenue authorities and taxpayers trying to litigate transfer pricing disputes. Courts are used to insisting on, and receiving, the best evidence of facts. Hearsay evidence is prima facie inadmissible. So how do revenue authorities and taxpayers prove matters about which they have no direct knowledge but which may be critical to the work that will have been done internally?

The Court in *SNF* showed some flexibility in accepting evidence in the form of “direct testimony [...], substantial documentation in the form of annual reports, [...] evidence of [...] comparability [...] and evidence of a global market [...]”,¹⁵ but the problem of evidence in an admissible form is likely to be an ongoing headache.

A new approach. Finally, it is worth remembering that some victories can be pyrrhic. As a result of *SNF* – a loss of approximately AUD 2 million – the Commissioner managed to convince the government that the transfer pricing rules had been dealt a fatal blow. On 1 November 2011, the Assistant Treasurer announced a project to review Australia’s domestic transfer pricing law and treaty practice, and in May 2012 formal legislation dealing with transfer pricing was introduced into the Australian Parliament.¹⁶

One of the major objectives of this bill is to give effect to a position that the ATO has long asserted, namely that the provisions of articles 7 (business profits) and 9 (associated enterprises) of Australia’s tax treaties provide an independent basis which permits the ATO to make transfer pricing adjustments and claim further tax. The second part of the bill seeks to give formal status to the OECD Guidelines for purposes of Australian law, at least where a treaty is involved. The provision in question is only enlivened in cases where a treaty is being relied upon; it does not amend Australia’s domestic law in other cases.

But the combination of these two rules is, one assumes, considered to be sufficient to overturn some aspects of *SNF*. The ATO can argue that the assessment in question is made pursuant to the treaty, not domestic law, and in interpreting that treaty, the OECD Guidelines must be treated as having some authority.

15. Id. at para. 47.

16. Tax Laws Amendment (Cross-Border Transfer Pricing) Bill (No. 1) 2012 (Australia).

Chapter 17

Denmark: Beneficial Owner – Article 10(2) of the Denmark-Luxembourg Income Tax Treaty of 1980*

Søren Friis Hansen

17.1. The case

The only Danish tax treaty case of 2011 is that decided by the Eastern High Court (*Østre Landsret*) on 20 December 2011. The case, reported as SKM2012.121ØLR,¹ deals with the interpretation of the term “beneficial owner” in relation to article 10(2) of the 1980 Denmark-Luxembourg tax treaty (corresponding to article 10(2) of the OECD Model Convention). The main issue of the case was whether a Danish *aktieselskab* (public limited company) was liable to pay withholding tax as a result of a dividend payment made to a Luxembourg S.à.r.l. The deciding factor of the case was whether the S.à.r.l. could be considered a conduit company, in which case the S.à.r.l. would not be the beneficial owner of the dividend received from the Danish company.

17.2. Facts of the case

17.2.1. Factual background and the legal base

The case began with a decision of the Danish National Tax Tribunal (*Landskatteretten*) of 3 March 2010. In 2005, an international group of investors acquired a Danish listed public limited company via a number of limited partnerships based in Delaware (United States), Guernsey, Germany and Bermuda. A Danish non-listed public company was formed as a holding company in relation to the Danish listed company, and the shares in the listed company were used as consideration in kind. Subsequently, an exchange of shares took place, with the result that a Luxembourg S.à.r.l. owned the shares in the Danish holding company.

* DK: Eastern High Court, 20 Dec. 2011, reported as SKM2012.121ØLR.

1. The case is available, in Danish, on the website of the Danish Ministry for Taxation at <http://www.skat.dk/SKAT.aspx?oId=1909349&vId=0>.

On 10 May 2005, the general meeting of Danish holding company decided to pay a dividend of DKK 5.544 million to the Luxembourg company. At the same time, it was decided that the Luxembourg company should give a convertible loan of DKK 5.5 million to the Danish holding company. The loan was converted to share capital on 31 December 2005.

In 2009, the Danish tax authorities concluded that the Danish company was liable to pay withholding tax of DKK 1,552,376,000 (at the time, 28%).

Under article 2(1)(c) of the Danish Corporate Income Tax Act (*Selskabsskatteloven*, SEL),² there is limited tax liability for dividends paid from a company resident in Denmark to a non-resident company, unless the payment is exempt from withholding tax due to the rules in Directive 90/435/EEC or an applicable tax treaty.

The tax treaty relevant to the case was the Denmark-Luxembourg treaty of 17 November 1980,³ specifically article 10(2) thereof.

The Danish tax authorities based their conclusions on the assumption that the Luxembourg S.à.r.l. was a mere “conduit company” and that the Luxembourg company consequently was not the beneficial owner of the dividend received from the Danish company. As the beneficial owners of the dividend were resident in a non-EU state with which Denmark has not concluded a tax treaty, the exemption from Danish withholding tax did not apply.

The decision of the Danish tax authorities was challenged by the Danish company before the National Tax Tribunal, which decided in favour of the company on 10 March 2010.⁴

17.2.2. Procedure before the Eastern High Court

The Danish tax authorities appealed the decision of the National Tax Tribunal before the ordinary courts, and the case was consequently heard by the Eastern High Court in Copenhagen.

2. Now consolidated Act 1403 of 7 Dec. 2010, available at: www.retsinfo.dk.

3. *Convention between the Government of the Grand Duchy of Luxembourg and the Government of the Kingdom of Denmark for the Avoidance of Double Taxation and the Establishment of Rules for Reciprocal Administrative Assistance with Respect To Taxes on Income and Capital*, 17 Nov. 1980, Bekendtgørelse 95 (23 Sept. 1982), Treaties IBFD.

4. Decision reported as SKM2010.268.LSR. For comments on the decision, see J. Bundgaard, *Første slag om “beneficial ownership” er udkæmpet – det endelige venter forude*, Skat Udland (2010), at 144.

Before the High Court, the Danish company claimed that there was no liability to pay withholding tax on the dividend paid to the Luxembourg company. This claim was supported by the argument that the Luxembourg company was indeed the beneficial owner of the dividend and that the exemption from withholding tax should therefore apply.

Before the High Court the Danish company raised some additional questions concerning the refusal to exempt the company from paying withholding tax. According to the Danish company, the refusal to exempt dividend payments to the Luxembourg S.à.r.l. from Danish withholding tax was an infringement of Directive 90/435/EEC, as both companies were subject to the Directive. Furthermore, the Danish tax authorities had changed their interpretation of the terms “beneficial owner” and “conduit company” in relation to tax treaties, and such a change of interpretation should be considered as a retroactive application of tax rules.⁵ The Danish tax authorities made the counterclaim that the Danish company was liable to pay the withholding tax because of negligence.

However, as the Eastern High Court decided the case solely on the basis of the interpretation of the term “beneficial owner”, the above-mentioned questions were not answered by the Court.

The deciding factor in the case was whether the Luxembourg S.à.r.l. was merely a “conduit for channelling income” to its shareholders, which were resident in a non-tax treaty state. If that were the case, the owners of the Luxembourg company would be the beneficial owners of the dividend.

The Danish company argued that the Luxembourg S.à.r.l. could not be considered to be a “conduit for channelling income” simply because the dividend had been returned to the Danish company as a convertible loan.

There is no specific anti-abuse clause in the 1980 Denmark-Luxembourg tax treaty. Before the Court, the tax authorities argued that the dividend payment made from the Danish company to the Luxembourg company constituted an abuse in relation to the tax treaty, as the dividend payment and the loan to the Danish company could not be considered to be an ordinary commercial transaction.

5. See H.S. Hansen, *Det store hykleri – om ‘beneficial owner’ sagerne*, Tidsskrift for skatter og afgifter (2011), at 537.

The Danish company, on the other hand, argued that the provision in article 10(2) on beneficial ownership in the OECD Model could not be applied by the states as a general anti-abuse clause.

17.3. The Court's decision

The Eastern High Court decided the case on 20 December 2011.⁶ In its decision, the Court relied only on the interpretation of the term “beneficial owner” and the conditions under which a company receiving dividend payments may be considered to be a conduit company.

The High Court concluded that the term “beneficial owner” (in Danish, *retmæssig ejer*) is not known in Danish law, and that the term is not defined in the Commentary to the OECD Model Convention.

In the Commentary, there is, however, some guidance for the interpretation of the term. The High Court concluded that the term “beneficial owner” should be given an international tax meaning in order to ensure that a uniform application of the Model Convention could be achieved, and that the interpretation should not be derived from Danish law.

With regard to treaty abuse, the High Court referred to the report from the OECD Committee on Fiscal Affairs from 1986, as well as the 2003 Commentary to the Model convention.

Based on these sources, the High Court concluded that a state may not apply a presumption of abuse based only on the fact that a holding company receives dividends from a subsidiary resident in another state. The fact that an intermediary holding company is located in a state with which Denmark has a tax treaty, cannot in itself justify that a state does not consider the intermediary holding company to be the beneficial owner of dividends paid by the subsidiary.

In the present case, it was not necessary for the High Court to consider the level of control exercised by the owners of the Luxembourg holding company.

The Court concluded that because the dividends received by the Luxembourg company had in fact been returned to the Danish company as a convertible

6. SKM2012.121.ØLR.

loan, the dividend had neither been transferred to a recipient in a state with which Denmark had no tax treaty, nor been destined to be transferred in such a way.

Consequently the High Court concluded that the Luxembourg S.à.r.l. was the beneficial owner of the DKK 5,544,200 received as dividend from the Danish company and that there was no tax liability for withholding tax.

17.4. Comments on the Court's reasoning

With the judgment of the Eastern High Court in this case, the Danish tax authorities suffered a major setback in the fight against so-called conduit companies. Following the judgement by the Eastern High Court, the Danish Ministry for Taxation issued an official statement dated 13 February 2012.⁷ In this statement, the Ministry announced that the decision by the High Court would not be appealed to the Supreme Court. The Ministry concluded that the judgement of the High Court in this case was decided on the basis of the concrete facts of the case, and that the findings of the High Court consequently have no bearing on a number of pending cases dealing with similar questions regarding the interpretation of the term “beneficial owner”.

A number of similar cases have recently been decided by the National Tax Tribunal. Case SKM 2010.729.LSR concerned a Luxembourg S.à.r.l. which was considered to be the beneficial owner of interest payments from a Danish company. In cases SKM2011.57.LSR and SKM 2011.485.LSR, the National tax Tribunal decided that a Swedish company controlled by a company in Jersey (and in the Cayman Islands, respectively) was not the beneficial owner in relation to interest payments made by a Danish company. These cases are currently pending before the High Court.

The decision by the High Court was based on an interpretation of the term “beneficial owner” which is in line with the international understanding of this term, as it is presented in the Commentary to the OECD Model. Furthermore, the Eastern High Court concluded that the mere fact that the management of a holding company receiving a dividend from a subsidiary, has the right to use that dividend under the applicable company law rules, and that the dividend therefore could be transferred to the holding company's shareholders as a dividend, should not in itself lead to the conclusion that the

7. Reported as SKM2012.100.SKAT.

holding company is not the beneficial owner of the dividend.⁸ As there was in fact no distribution in the case, the Court did not answer the more difficult question of the degree of control necessary to establish that a company is a mere “conduit company”.

17.5. Conclusion

The National Tax Council has adopted the decision by the Eastern High Court into its decisions. In its decision of 2 May 2012,⁹ the Tax National Council ruled that a Danish company was not liable to pay withholding tax on a shadow dividend paid to a Dutch naamloze vennootschap (N.V.) via a Cypriot intermediary holding company. This Dutch company is on the list in Directive 2011/96/EU. The National Tax Council concluded that the Dutch company was the beneficial owner (not a mere conduit company), as the dividend was not transferred on to the parent company of the Dutch company.

In its decision of 22 May 2012, the National Tax Council concluded that a Danish company was not liable to pay withholding tax on a dividend paid to its Swedish parent company.¹⁰

On 3 October 2012, the Danish Minister for Taxation presented a draft amendment of the rule in article 2(1)(c) of the Danish Corporate Income Tax Act.¹¹ According to the draft, a foreign parent company will have limited tax liability for dividends paid from a company resident in Denmark if (i) the Danish company is a mere conduit for dividends received from its subsidiaries and (ii) the receiving company is exempt from tax under Directive 2011/96/EU.

A number of cases on beneficial ownership are pending before the Danish courts, and the amendment to article 2(1)(c) is likely to generate debate in the near future. The problem of beneficial ownership will continue to be a subject of debate in Denmark in the years to come.

8. See the commentary of T. Booker, *Beneficial Owner*, Revision & Regnskabsvæsen 10 (2012), at 30, 33f.

9. DK: National Tax Council, 2 May 2012, reported as SKM2012.246.SR.

10. DK: National Tax Council, 22 May 2012, reported as SKM2012.320.SR.

11. Draft Amendment Act L 10 2012/13, presented to the Danish parliament on 3 Oct. 2012, available at www.ft.dk.