

## DENMARK

	1995	2000	2001	2002	2003	2004	2005	2006	2006		
<b>A. Structure of revenues</b>									% of GDP	€ bn	Ranking <sup>1</sup>
Indirect taxes	17.0	17.2	17.4	17.5	17.4	17.6	18.0	18.0	39.6	2	
VAT	9.4	9.6	9.6	9.6	9.6	9.8	10.0	10.3	22.6	3	
Excise duties and consumption taxes	3.7	4.1	4.1	4.1	4.0	3.8	3.5	3.4	7.4	8	
Other taxes on products (incl. import duties)	2.3	2.0	1.8	2.0	1.9	2.2	2.6	2.6	5.8	7	
Other taxes on production	1.6	1.6	1.8	1.8	1.8	1.8	1.8	1.8	3.9	11	
Direct taxes	31.0	30.5	29.5	29.3	29.5	30.4	31.8	30.2	66.5	1	
Personal income	26.3	25.6	26.0	25.7	25.6	24.9	24.9	24.5	54.0	1	
Corporate income	2.3	3.3	2.8	2.9	2.9	3.2	3.9	4.3	9.5	5	
Other	2.3	1.6	0.7	0.7	1.1	2.3	3.0	1.4	3.1	4	
Social Contributions	1.1	1.8	1.7	1.2	1.2	1.2	1.1	1.0	2.3	27	
Employers'	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	27	
Employees'	1.1	1.8	1.7	1.2	1.2	1.1	1.1	1.0	2.2	24	
Self- and non-employed	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	26	
<b>B. Structure according to level of government</b>									% of GDP		
Central Government	32.2	31.0	29.7	29.5	29.6	30.9	32.7	31.5	69.3	3	
State Government <sup>2</sup>	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	
Local Government	15.6	16.5	17.0	17.1	17.2	16.9	16.9	16.6	36.4	1	
Social Security Funds	1.1	1.8	1.7	1.2	1.2	1.2	1.1	1.0	2.3	25	
EU Institutions	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.5	24	
<b>C. Structure according to economic function</b>									% of GDP		
Consumption	15.4	15.7	15.7	15.8	15.6	15.8	16.1	16.2	35.5	2	
Labour	27.3	26.6	26.9	26.1	26.0	25.2	25.1	24.7	54.4	2	
Employed	21.1	21.7	22.1	21.2	20.9	20.2	20.1	19.8	43.5	7	
Paid by employers	0.5	0.5	0.6	0.5	0.5	0.5	0.5	0.5	1.1	27	
Paid by employees	20.7	21.3	21.5	20.7	20.4	19.7	19.6	19.3	42.4	1	
Non-employed	6.1	4.9	4.8	4.9	5.1	5.0	5.0	5.0	10.9	1	
Capital	6.4	7.2	6.0	6.1	6.6	8.1	9.7	8.4	18.5	11	
Capital and business income	4.5	4.8	3.4	3.4	3.8	5.3	6.9	5.6	12.4	17	
Income of corporations	2.3	3.3	2.8	2.9	2.9	3.2	3.9	4.3	9.5	5	
Income of households	0.9	0.4	-0.6	-0.5	-0.1	1.1	1.9	0.3	0.7	19	
Income of self-employed (incl. SSC)	1.3	1.1	1.2	1.0	1.0	1.0	1.0	1.0	2.3	18	
Stocks of capital / wealth	1.8	2.4	2.6	2.7	2.8	2.8	2.8	2.8	6.1	8	
Less: amounts assessed but unlikely to be collected	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1			
<b>TOTAL</b>	<b>48.8</b>	<b>49.4</b>	<b>48.4</b>	<b>47.8</b>	<b>48.0</b>	<b>49.0</b>	<b>50.7</b>	<b>49.1</b>	<b>108.1</b>	<b>1</b>	
									% of GDP		
Of which environmental taxes	4.5	5.2	5.1	5.3	5.1	5.5	5.8	6.0	13.2	1	
Energy	2.1	2.5	2.7	2.6	2.6	2.5	2.3	2.2	4.9	7	
Transport	2.1	1.8	1.7	1.9	1.8	2.0	2.2	2.2	4.9	1	
Pollution/Resources	0.3	0.8	0.8	0.8	0.8	1.0	1.3	1.5	3.4	1	
<b>D. Implicit tax rates</b>									%	Ranking <sup>1</sup>	
Consumption	30.5	33.4	33.5	33.7	33.3	33.3	33.6	34.0		1	
Labour employed	40.2	41.0	40.8	38.8	38.1	37.4	37.5	37.0		12	
Capital	29.9	36.0	30.8	30.7	36.7	45.5	47.7	40.9			
Capital and business income	21.2	23.8	17.5	17.2	21.3	29.9	33.9	27.4			
Corporations	20.2	24.4	21.9	21.1	23.2	26.7	28.3	29.8			
Households	20.7	19.6	7.7	7.8	13.3	29.1	37.8	17.1			
<b>p.m.:</b>											
Real GDP growth (annual rate)	3.1	3.5	0.7	0.5	0.4	2.3	2.5	3.9			
Output gap (potential)	-0.1	2.5	1.2	-0.3	-1.6	-1.2	-0.2	1.1			

See ANNEX B for classification of taxes and ANNEX C for explanatory notes.

1) The ranking is calculated in descending order. A "1" indicates this is the highest value in the EU-27. No ranking is given if more than 10 % of data points are missing.

2) This level refers to the Länder in AT and DE, the gewesten en gemeenschappen / régions et communautés in BE and comunidades autónomas in ES.

n.a.: not applicable, - : not available

Source: Commission Services

## Overall trends in taxation

### *Structure and development of tax revenues*

Although the tax-to-GDP ratio dropped by 1.6 % percentage points from 2005 to 49.1 %, Denmark shows the highest ratio in the EU in 2006. It should be noted, however, that the tax-to-GDP ratio overestimates the Danish tax burden somewhat in relation to other countries, since transfer incomes (for example, pensions) are taxed, and not paid out on a net basis, although no corresponding income is taken into account when measuring GDP. Adjusting for this difference of 4-5 % of GDP would not however, substantially change Denmark's ranking as one of the EU's highest taxing countries.

The Danish tax structure stands out in a number of respects. Social contributions are very low as most welfare spending is financed out of general taxation, notably personal income taxation. Correspondingly direct taxes form 61.5 % of total tax revenues (EU-27 31.4 %). Personal income taxes form the bulk of direct taxes, representing 49.9 % of total taxation in 2006. In contrast, the proportion of indirect taxes was 36.6 %, which is slightly below the EU-27 average (38.9 %); this, however, is due not to a low absolute level of indirect taxation but rather to the fact that the revenue from other taxes is comparatively higher; indeed, the effective tax burden on consumption, as measured by the ITR on consumption, is at 34.0 % in 2006 the highest in the EU.

In terms of the distribution of revenue between levels of government, Denmark differs substantially from the EU average because of the small role played by social security funds. As a result, the share of taxes raised by central government and particularly local government is elevated, respectively 64.1 % and 33.7 % (EU-27 59.0 % and 11.3 %).

The tax-to-GDP ratio reached 50.7 % in 2005, nearly two percentage points higher than in the previous year and a peak value for the 1995-2005 period. The increase is largely explained by the pension fund yield tax, which is dependent on financial market developments and may fluctuate considerably from one year to the next. The pension fund yield tax was at an exceptionally high level in 2004 and 2005, but fell by nearly 2 percentage points in 2006 and is expected to remain at this lower level in subsequent years.

### *Taxation of consumption, labour and capital; environmental taxation*

The implicit tax rate on consumption, at 34.0 % (EU-27 22.1 %), remains the highest amongst the Member States. The rate displays a slight upward trend since 2000.

Despite the generally high level of taxation, the ITR on labour, at 37.0 %, is not amongst the EU's highest, but is exceeded in eleven other Member States, including many with a lower overall tax ratio. It has been steadily falling since 2000, resulting at least partly from labour tax cuts introduced in 2004.

The overall implicit tax rate on capital (40.9 %) is currently among the highest in the EU, exceeding the EU-27 average by over 10 percentage points, but has decreased considerably from its peak of 47.7 % in 2005. The implicit tax rate on capital displays a strong fluctuation over the years, reflecting the fluctuation in the yield from pension scheme assets and therefore the tax on these.

Particularly since the environmental tax reform implemented in 1999-2002, Denmark has a comprehensive and ambitious energy tax system. All energy products, including coal, natural gas and electricity, are subject to both CO<sub>2</sub> tax and energy tax. VAT registered companies do not pay energy tax for the energy used in industrial processes, and are also entitled to a refund of their CO<sub>2</sub> tax, the amount of which depends on whether the process is defined as heavy or light and whether the company has concluded an energy saving agreement with the government or not. In 2006 environmental taxes yielded 6.0 % of GDP, the highest proportion in the EU by a wide margin.

### *Current topics and prospects; policy orientation*

In 2008 the government continues the tax policy line of the previous years. The tax freeze policy, introduced in 2002, is maintained implying that tax rates are not increased in nominal or value terms, unless compensated by reductions in other taxes or charges. At the same time the level of labour income taxation is reduced through gradual measures. In line with this policy, the government has concluded an agreement to cut income taxation altogether by DKK 9.5 billion in 2008 – 2009 (4 % of GDP forecast for 2008). In 2008 this is implemented mainly by increasing the earned income tax credit from 2.5 % to 4 % and increasing its upper limit from DKK 7 500 to DKK 12 300. The personal allowance, applicable in municipal, church and state taxation, is also increased by DKK 500. The total impact of these measures is about DKK 4.2 billions in 2008.

As part of the agreement energy tax rates are price-indexed from 2008 onwards using the medium-term inflation rate of 1.8%. Since the energy tax rates are fixed in nominal terms, the measure is meant to maintain their real value and in this way support Denmark's energy and climate policy objectives. In accordance with the tax freeze, the revenues from increased energy taxation are used to lower income taxation along the lines explained above.

A major corporate tax reform, introduced in 2007, is gradually taking effect in 2007 - 2016. The aim of the reform is to prevent the corporate tax base from eroding through the excessive leverage of Danish companies and to make the Danish CFC rules compatible with EU law. As part of the reform package the corporate tax rate is reduced from 28 % to 25 %, while at the same time certain base broadening measures are taken. These measures most notably consist of a limitation of interest deductibility through introduction of an EBIT-rule, a ceiling on deductible interest and a tightening of depreciation allowances for certain assets.

## **Main features of the tax system**

### *Personal income tax*

Personal income taxation in Denmark is characterized by relatively high average and marginal tax rates. As in the other Nordic countries, local taxes play an important role in Danish personal income taxation. Local tax rates are flat and vary from one municipality to the next. The average local income tax rate was 33.3 % in 2006 (including county, municipal and church tax), but has fallen to 25.3 % in 2007 and 25.5 % in 2008 as a consequence of the Local Government Reform (see 2007 edition).

State income taxation is progressive and consists of three tax brackets. The lowest rate is 5.48 % and is paid on personal income (income minus labour market contribution) after the deduction of a personal allowance (DKK 41 000 in 2008, equivalent to €5 500). The medium rate is 6 % and is paid on the part of personal income, which exceeds the medium bracket tax allowance (DKK 279 800 in 2008, €37 500). The top 15 % rate is paid on the share of personal income plus individual contributions to capital pension schemes which exceeds the top bracket basic allowance (DKK 335 800 in 2008, €45 000). Individual contributions to pension schemes are otherwise deductible from personal income. Because of the tax ceiling set at the 59 % marginal tax rate, the full 15 % is not paid in all municipalities. In addition to local and state income taxes, individuals pay an 8 %-labour market contribution, calculated on the gross wage before deduction of any allowance, and since 2007 an 8 %-healthcare contribution. Overall, the system is highly progressive with marginal rates ranging from 8 % (up to the amount of personal allowance) to 63 % (the upper ceiling plus the labour market contribution and the average church tax). However, only a minority of tax-payers pay progressive state taxes: in 2006 approximately 25 % of tax payers fell in the medium bracket, while 20 % paid top tax bracket taxes.

Net capital income (positive or negative) is included in the tax base for both state taxes and local income taxes. However, though interest payments are a part of negative capital income, they are generally deductible only based

on the flat local tax rate, and not on the progressive state income tax rate. Also the earned income allowance and some other deductions are taken into account only in calculating the local income tax base.

At the personal level, dividend income is taxed at two different rates: 28 % for the dividend income not exceeding a threshold (DKK 44 300, €5 943 in 2006) and 43 % for income above this level. Also capital gains on selling shares are generally taxed at the same two rates (28 % or 43 % depending on whether the net gains are below or above the threshold) according to new rules adopted in 2006. As an element of the above-mentioned corporate tax reform in 2007, a third rate at 45 % will apply for dividend income and capital gains on selling shares above DKK 100 000 (€13 416) from 2008.

### *Corporate taxation*

The corporate tax rate was reduced from 30 % to 28 % in 2005 bringing it into line with those of the other Nordic countries (Sweden and Norway 28 %, Finland 26 %), but, in the context of the corporate tax reform, it was brought below this level, to 25 %, in 2007. There are no local taxes on corporations, but municipalities receive a share of corporate income tax revenue. Since 2004 there are mandatory national tax consolidation rules for permanent establishments and resident subsidiaries, while resident group-related subsidiaries of non-resident companies may apply for international consolidation. Loss carry-forward is allowed without limitation, but no carry-back is permitted.

Tax depreciation is straight line over a 20 years period for buildings used for business purposes (not offices) and at a declining base for machinery and equipment (up to 25 %). The depreciation rate for buildings was reduced from 5 % to 4 % in 2008 as a part of the corporate tax reform, extending the depreciation period to 25 year. Tax depreciation for ships, drilling rigs, aircrafts, and trains will gradually be lowered from 25 % in 2007 to 15 % in 2016. Inventories are valued on a FIFO-basis. Acquired goodwill and the acquisition costs of know-how, patents, copyrights and other intangibles may be depreciated over 7 years using the straight-line method.

Denmark applies an R&D tax incentive scheme, which allows deduction of 150 % of the costs of R&D projects, if paid to a public R&D institution, subject to a ceiling. The project must be related to the business of the company and be approved in advance by a public research council.

### *VAT and excise duties*

The VAT rate is 25 % and only newspapers are taxed at a zero rate. Excise duties on tobacco, alcohol and soft drinks were reduced in 2003 in anticipation of changes in cross-border trade restrictions (abolition of 24 hour rules) from January 2004 onwards. From 2008 onwards excise duties on energy are price-indexed and increased by 1.8 % annually.

### *Wealth and transaction taxes*

Immovable property situated in Denmark is subject to municipal and county real estate taxes. The rate of municipal real estate tax varies between 0.6 % and 2.4 %, and that of the county real estate tax is 1 % with a 0.4 % rebate for pensioners in 2006. In 2007, after the Local Government Reform, immovable properties are subject only to a municipal real estate tax varying between 1.6 % and 3.4 %.

### *Social contributions*

As mentioned above, social security contributions play a limited role in Denmark.