



Worth knowing about:

Tax and VAT on losses on debtors etc.

This article is about the VAT and tax treatment of losses on all types of receivables.

Tax treatment of losses

With a few exceptions, both individuals and companies can deduct all types of losses on receivables. In turn, the vast majority of gains on such receivables are also taxable. The deductibility applies not only to losses on business debtors, but also to losses on promissory notes, mortgages, bonds and suspense accounts.

Exemption rules for individuals

Individuals do NOT have a deduction for losses on the following types of receivables:

- Receivables in Danish kroner that were purchased or otherwise acquired BE-FORE 27 January 2010, unless they are business debtors or money lending or collateral provided in the course of self-employment.
- Receivables from major shareholder companies, i.e. mainly receivables from companies in which the creditor owns 25% or more of the shares.
- Claims on close family members, i.e. spouse, parents, grandparents, children, grandchildren and their spouses.

Individuals can thus deduct losses on bonds as well as on all types of private money lending that are not covered by the above exceptions. However, a de minimis limit applies, so that losses can only be deducted if they exceed DKK 2,000.

Exemption rules for companies

Companies are not allowed to deduct losses on receivables from affiliated companies. However, there are also exceptions to the exemption. Losses on affiliated companies can be deducted if they are business debtors or interest receivables and the companies have not been jointly taxed.

The time of deduction

When it comes to the timing of deductions, there are significant differences between the rules for companies and individuals. The tax accrual of gains and losses on receivables and payables has been changed several times - most recently with effect for income years starting on or after 1 March 2015. As a result of the legislative changes, a large number of transitional provisions apply to both individuals and companies. In the following, only the main rules are described.

Companies

Companies are generally obliged to apply the inventory principle for all receivables. As an exception to this, companies are free to choose between the inventory and realisation principle for business debtors and intercompany balances.

In practice, most companies choose to use the inventory principle for trade receivables. Normally, it will therefore only be for group receivables that companies use the realisation principle.

Tax Legal

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If the inventory principle is applied to trade receivables (business receivables), the inventory adjustment will typically be based on the accounting valuation, as this will usually be based on an individual assessment or based on the company's experience with bad debt losses.

Effective for income years beginning on or after 1 March 2015, companies can elect the inventory principle for exchange rate changes on foreign currency receivables and payables. An election will also include exchange rate changes on intercompany balances, regardless of whether the realization principle is otherwise elected for these receivables.

Individuals

As a general rule, losses on receivables can only be deducted once the loss has been finally recognized.

When it comes to losses on business debtors, there is a special practice for companies with a very significant number of debtors. For these, a percentage write-down is authorized. In other words, a deduction for losses without an individual assessment of each debtor. The size of the write-down must be based on the company's experience with regard to the size of losses on debtors.

For listed bonds - both Danish and foreign - the inventory principle can be chosen without authorization from SKAT. In relation to foreign listed bonds, the choice will mean that both stock price changes and exchange rate changes will be covered by the inventory principle. Alternatively, the inventory principle can be chosen so that it only covers exchange rate changes on receivables and payables in foreign currency.

Once the inventory principle has been selected, the selection can only be changed after authorization from SKAT.

VAT treatment of losses

For VAT purposes, both VAT-registered individuals and companies have the right to adjust sales tax in connection with losses on business debtors.

It should be noted that a receivable can change character - from a goods receivable to a money loan - if the credit terms are relaxed. In the case of money lending, the creditor is prevented from adjusting the lost VAT on the debtor.

Adjustment of the sales tax is reserved for the business that has supplied the goods or services subject to VAT. If the claim - the receivable - has been sold, for example, to an affiliated company, the buyer cannot make an adjustment if the debtor does not pay.

VAT on losses on business debtors can be adjusted once the loss has been recognized. Recognizing a loss requires - as a starting point - that the creditor has taken internal legal steps to establish the loss. The documentation requirements are quite strict.

SKAT has relaxed the practice for losses on claims over DKK 3,000 outside of bankruptcy and composition, etc., where the loss has not been ascertained by internal court proceedings. The sales tax can then be adjusted - after a specific assessment - if the claim can be considered lost. For claims over DKK 10,000, it is a minimum requirement that the claim has been attempted to be collected by an independent debt collection company. For claims under DKK 10,000, the loss is accepted as established when the claim has gone through an internal reminder procedure in the company. A percentage write-down is not permitted.

In cases other than those described above, regulation of the sales tax requires that there is a declaration of insolvency from the debtor, or that bailiff proceedings have been carried out against the debtor in vain. In relation to claims against bankrupt estates, it is sufficient that there is a declaration from the trustee about the size of the expected dividend.

For minor claims under DKK 3,000, it is usually sufficient that the debtor has unsuccessfully sought payment and that the business relationship has ended.

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