

TAX FACTS 2016

Tax facts 2016

2016

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1 Residence and work permits

Requirement for residence and work permits depends on the nationality of the person. Different rules apply for Nordic citizens and citizens from other countries.

Decisions regarding residence and work permits are made by the Danish Agency for International Recruitment and Integration.

Nordic citizens

Citizens of Denmark, Norway, Sweden, Finland and Iceland (the Nordic countries) can reside and work in the Faroe Islands without permission from the authorities. Nordic citizens that wish to come to the Faroe Islands as au pairs or for educational purposes are also free to do so without permission from the authorities.

Citizens from other countries

Foreigners who do not hold citizenship of a Nordic country require a residence permit, if the purpose for staying in the Faroe Islands is other than tourism. In order to work or conduct other similar activities in the Faroe Islands, a work permit is required, whether the work is paid for or not. Foreigners also require a work permit in order to conduct private business in the Faroe Islands.

EU-citizens who come to work with a pre-approved employer can start working immediately provided that the employee has been offered a job of at least 30 hours per week, and that a work permit application form has been submitted to the Police on the first day of work.

If an EU-citizen is promised work with an employer who is not pre-approved, the employee must not enter the Faroes and start to work until a formal permit has been issued by the Danish Agency for International Recruitment and Integration.

Visa requirements

Foreigners from countries with a visa requirement must obtain a visa prior to entering the Faroe Islands. A visa is only intended to allow foreign nationals to visit the Faroe Islands for a limited period of time. Foreigners that wish to work in the Faroe Islands or to reside in the Faroe Islands for an extended period of time have to apply for a work and/or residence permit.

Questions regarding visas for travelling to and from the Faroe Islands can be put to the Police Headquarters in the Faroe Islands or to the Danish Agency for International Recruitment and Integration. Information on residence and work permits in the Faroe Island can also be obtained from the Faroese Immigration Office on their website www.utlendingastovan.fo.

2 Taxation of resident individuals

2.1 Tax liability

All residents are liable to taxation in the Faroe Islands. A foreign individual becomes resident for tax purposes, if accommodation is acquired and residence is taken up in the Faroe Islands. Non-resident individuals, who stay in the Faroe Islands for more than 180 days in a rolling 12-month period, are also liable to taxation as residents from the date of arrival.

Resident individuals are taxed on their worldwide income. The tax liability ends when the individual leaves the Faroe Islands with his family, provided that accommodation in the Faroe Islands is no longer available for permanent use.

Tax liability according to domestic law may be subject to tax treaty relief.

2.2 Entry rules for shares and other securities

When an individual becomes a tax resident of the Faroe Islands, a deemed acquisition value is applied to shares and other securities, based on the fair market value on the day when the individual became resident for tax purposes.

2.3 Taxable income for resident individuals

Resident individuals are taxed on their worldwide income. As a rule all income in money or in kind is treated as taxable income unless a specific tax exemption is provided in the tax legislation. Taxable income for resident individuals is divided between two types of income, which are taxed separately.

Regular taxable income

The most common types of regular taxable income are:

- Remuneration in cash
- Remuneration in kind, e.g. employer paid use of cars and accommodation
- Net income from private business
- Net income from rent of real estate
- Presents, grants and donations
- Certain types of continuous payments from pensions plans

Taxable capital gains income

Taxable capital gains income includes the following types of income:

- Interest from deposits, bonds and securities
- Dividends from shareholdings
- Gains/losses from disposal of shares
- Gains/losses from disposal of bonds and other securities

Wealth tax

No wealth tax is in effect in the Faroe Islands.

2.4 Income in Kind

Certain types of remuneration in kind are included in the regular taxable income at fixed annual rates that are published each year by the Tax Authorities.

Private use of a company car

The taxable rate for private use of a company car is fixed in proportion to the registered type and weight of the car. For 2016, the fixed taxable rates range from DKK 55,500 to DKK 86,900 for passenger cars and from DKK 33,300 to DKK 52,140 for vans.

The taxable rate is based on private driving of 10,000 km for the year. If less private driving can be proven, the taxable rate can be reduced accordingly. Driving between home and workplace is considered as private driving.

Accommodation

The taxable rate for free accommodation depends on the square area that is available for accommodation. For 2016, the annual rate is set at DKK 754 per m². If free accommodation is only provided for a part of the year, the taxable amount is reduced accordingly.

Electricity and heating

Free electricity and heating are taxed at fixed rates. For 2016, the rate for free electricity is DKK 10,000 while the rate for free heating is 22,300. If free electricity and free heating is only provided for a part of the year, the taxable amount is reduced accordingly.

Free meals

Free meals are taxed at fixed rates. For 2016, the rate is DKK 35 per day for one free meal, DKK 46 per day for two free meals, and DKK 61 per day for three free meals.

2.5 Deductions in regular taxable income

In general, private individuals cannot deduct any expenses in their regular taxable income. As such, no expenses to health, education, travel and housing can be deducted in the taxable income. Neither can gifts or donations of any kind be deducted in the taxable income.

Residents can apply for subsidies for some of these expenses, see chapter on tax subsidies for further details.

Regarding personal income from working on board ships or personal income from work in a foreign country, certain types of standard deductions are allowed.

Income from fishing vessels

A deduction of 14% is granted for taxable income derived from fishing vessels registered in the Faroe Islands or in another Nordic country. The deduction is, however, limited to 14% of DKK 470,000 corresponding to a maximum annual deduction of DKK 65,800.

Furthermore, a deduction of DKK 300 per day at sea can also be granted for work on board a fishing vessel registered in another Nordic country provided that the individual is in a 12 month period at sea for either two coherent months or 100 days. The deduction of DKK 300 per day is not granted for work on board Faroese registered vessels.

For work on board fishing vessels that are not registered in the Faroe Islands or in another Nordic country, see below.

Income from work abroad

A deduction of 30% is granted for income from work abroad, either on land or with a foreign vessel of any type. The deduction is, however, limited to 30% of DKK 400,000 corresponding to a maximum annual deduction of DKK 120,000. The reduced taxable income is taxed at a flat rate of 35%.

The rules do not apply to income from ships registered in the Danish International Ships Register (DIS), or to fishing vessels registered in another Nordic country, see above.

Crew on board vessels registered in the Faroese International Ships Register (FAS)

No deductions are allowed regarding income from vessels registered in FAS. Income from such vessels is taxed at a flat rate of 35%.

Crew on board vessels registered in the Danish International Ships Register (DIS)

Income from vessels registered in DIS is included in the regular taxable income but tax relief is granted for the calculated tax that relates to the DIS income. The standard deduction of DKK 300 per day is granted for each day at sea on board a DIS registered vessel.

A summarisation of deductions in personal income

The three types of deduction that are granted in personal income for resident individuals are summarised in the table below

	14%	30%	DKK 300 per day
Faroese fishing vessels	+	-	-
FAS registered vessels	-	-	-
Other Faroese vessels	-	-	-
Work on land in the Faroe Islands	-	-	-
DIS registered vessels	-	-	+
Nordic registered fishing vessels	+	-	+
Other foreign vessels	-	+	-
Work abroad on land or offshore	-	+	-

2.6 Deductions in calculated tax

Child allowance in the calculated income tax

For each child under the age of 18, an allowance is granted in the calculated tax. The annual allowance varies between DKK 9,500 and DKK 16,500 for each child depending on the municipal where the taxpayer resides. If the calculated tax before child allowance is lower than the child allowance, the excess amount is paid out to the individual.

Pensioner allowance in the calculated income tax

Individuals that receive disability pension are granted an annual allowance in the calculated tax. The annual allowance is DKK 10,500 for married persons and DKK 16,200 for single persons.

2.7 Income from private business and rent of real estate

Net income from private business and rent of real estate is included in the regular taxable income.

Private Business

Taxable income from private business encompasses all business related income including gains and recaptured depreciations in connection with disposal of business related assets.

Operating expenses incurred during the year can be deducted in the taxable income. Common types of operating expenses are interest, salaries, rent, maintenance and advertising expenses.

Annual depreciation on plant, machinery, buildings, goodwill and other intangible assets can also be deducted in the taxable income. A closer description of the depreciation rules is provided in the chapter on company taxation.

Rent of real estate

Taxable income from rent of real estate for non-residential purposes is generally calculated according to the same rules as income from other types of private business, see above.

However, when real estate is rented out for residential purposes, the taxable income can be calculated by using either of two allowable methods.

Method 1

The taxable income may be calculated according to the general rules, i.e. as net income after deduction of operating expenses. The net income is included in the regular taxable income. No taxable depreciation is allowed for properties that are rented out for residential purposes, unless the property has at least ten apartments. Furthermore, if the property is also used as the private residence for the owner, interest expenses cannot be deducted in the taxable income. Instead, the owner may apply for interest subsidy, see chapter on subsidies.

Method 2

Instead of deducting normal operating expenses, the owner can choose a standard deduction of DKK 24,000 per year. The net income after the standard deduction is not included in the regular taxable income but is instead taxed separately at a flat rate of 25%.

Taxpayers can choose between method 1 or 2 each year.

2.8 Capital gains income

All capital gains income earned by Faroese residents, irrespective of source, is subject to Faroese taxation according to the regulations in The Capital Gains Income Act.

Taxable capital gains income is pooled together in a separate tax return. Capital gains income from foreign sources may be subject to tax treaty relief.

Interest income

Interest on deposits in Faroese banks is taxed as capital gains income. The tax is payable by the account owner, but is withheld at source by the bank. Interest on deposits in foreign banks is also taxed as capital gains income.

Interest expenses

Interest expenses on loans to buy shares or bonds can be deducted in capital gains income. If there is no capital gains income, the interest may be carried forward as a deduction for the following five years. Interest expenses on loans for other purposes cannot be deducted in the capital gains income.

Shares

Gains and losses on disposal of shares are taxed as capital gains income. Gains or losses are calculated as sales value reduced by acquisition costs.

For shares acquired before 16th November 2001, the acquisition cost is calculated as the fair market value of the shares as per 31st December 2006. Thus only the increase in value after 1st January 2007 is subject to taxation. Income from disposal of shares to the issuing company is taxed as dividend. The sales price without deduction of acquisition costs is included in the capital gains income. However, the Tax Authorities can allow that disposal of shares to the issuing company is taxed as a regular disposal of shares to a third party person, i.e. taxable income is calculated as sales value reduced by acquisition costs.

Liquidation proceeds

Liquidation proceeds, distributed in the calendar year in which the liquidation is finalized, are treated as disposal of shares, and the taxable income is calculated as the difference between liquidation proceeds and acquisition cost for the shares.

Liquidation proceeds, distributed before the year of the final liquidation, are taxed as dividend payments without deduction for acquisition cost.

Dividend

Dividend from a Faroese company is taxed as capital gains income. Dividends from foreign companies are also taxed as capital gains income. When paying out dividend to individuals, Faroese companies must withhold the dividend tax and pay the amount to the Tax Authorities within 14 days.

Bonds

Gains on disposal of bonds are taxed as capital gains income regardless if the bond is Faroese or from a foreign country. Gains on disposal of bonds are calculated as sales value reduced by acquisition costs.

Losses on disposal of bonds are only deductible for individuals, if the bond is registered on a stock exchange.

Debt relief

Debt relief is taxed as capital gains income, however, only to the extent that the debt is written off to an amount that is less than the market value of the debt.

2.9 Exit Tax

When a person becomes a tax resident in another country, and the total market value of his shares and securities is above DKK 100,000, he is deemed to have disposed of his shares and securities. The market value is considered as the sales price, and a gain or loss is calculated as the difference between acquisition value and the market value.

A gain or a loss shall be declared on the next capital gains tax return.

Persons that are liable to pay exit tax can apply for extension to pay the exit tax until the shares and securities are actually disposed of. Extension is conditioned on the person providing credit from a bank.

2.10 Tax exempt income

Certain types of income are listed explicitly in the tax legislation as tax exempt. The most common examples of tax exempt income are:

- Public old age pension
- Social security payments, excluding public disability pension
- Income from sale of non-business related property, unless the property was acquired with the intention to sell on with a profit
- Insurance payments that are paid out as a lump sum payment
- Travel expenses, room and boarding, paid by an employer when the employee is on a business trip or otherwise working away from the regular workplace
- The value of free food and accommodation for employees on board ships
- Income from testimonials
- The value of employer paid home computer
- The value of employer paid phone and internet
- Gifts between spouses and gifts to relatives up or down in a straight line – such gifts are tax free regardless of the value of the gift
- Gifts from employers on special occasions, provided that the value of the gift does not exceed a certain limit. Depending on the occasion, the limit varies between DKK 1,500 and 5,000.
- Inheritance, however, a special estate tax has to be paid, see below
- Prizes from games are generally exempted from income tax but a special tax of 15% is charged on most paid out game prizes

2.11 Tax rates for resident individuals

All residents pay state tax and municipal tax of their regular taxable income. In addition, members of the National Evangelical Lutheran Church also pay church tax of their regular taxable income.

Residents pay a separate state tax on capital gains income. No municipal or church tax is levied on capital gains income.

State Tax Rates

State tax on regular taxable income is calculated based on a progressive tax scheme. For the income year 2016, state tax is calculated as follows:

If income is	but less than	tax is	of	and of the rest
65,000	235,000	0	65,000	15.0%
235,000	330,000	25,500	235,000	20.0%
330,000	800,000	44,500	330,000	25.0%
800,000		162,000	800,000	30.0%

Municipal tax rates

Municipal tax applies to regular taxable income exceeding DKK 30,000. The rates, which are determined each year by the municipality where the taxpayer resides, vary between 16% and 23.25%.

Tax ceiling

The total state and municipal tax paid on regular taxable income cannot exceed 50%.

Church tax rate

Church tax is levied at a rate of 0.6% to 0.9% of regular taxable income exceeding DKK 30,000. Church tax is payable by members of the National Evangelical Lutheran Church.

State tax on capital gains income

Capital gains income is taxed at a flat rate of 35%.

3 Pension contribution

3.1 Mandatory pension savings

All residents aged between 21 and 67 are obliged to contribute to a private pension plan.

Foreigners, who have a time limited job in the Faroe Islands for a period of 60 months at most, can apply to the Tax Authorities to be exempt from contributing to a Faroese pension plan.

Individuals that work abroad for a Non-Faroese employer can apply to the Tax Authorities to be exempt from contributing to a Faroese pension plan.

3.2 The pension contribution

In 2016, the pension contribution is minimum 2% of the regular taxable income. The mandatory pension contribution increases from 1 January 2017 by 1% annually, until it reaches 15% in 2029.

The employer is obliged to transfer the employee's pension contribution to the Tax Authorities who withhold 40% in pension tax before the net contribution is transferred to the employee's pension plan.

Residents with income from private business or income from rent of real estate shall pay the pension contribution at the latest on 1st November in the following income year.

Regardless of the above mentioned rate, no resident is obliged to pay more than DKK 150,000 annually in pension contributions.

3.3 Pension pay-out

In general, a person can only receive pension pay-out on the day he has reached retirement age and at the latest the first day he receives his public old age pension at the age of 67.

At least 45% of the pension savings shall be paid as a lifelong pension payment. The paid out amount is calculated on the basis of the average life expectancy and the amount that has been accumulated on the pension plan. The person will get a monthly pay-out until death.

A maximum of 55% of the pension plan can be paid out as a 10 annuity pension. A maximum of 15% of the pension can be paid out as a capital lump-sum. All pension pay-outs are tax exempt.

4 Taxation of non-residents

Non-residents are liable to pay tax on certain types of income from Faroese sources.

4.1 Tax liability and taxable income

Remuneration for duties performed in the Faroe Islands is taxable provided that the remuneration is received from a Faroese resident employer or a foreign employer who carries out activities through a permanent establishment in the Faroe Islands. Travel and accommodation expenses paid by the employer are tax exempt provided that the individual stays in the Faroe Islands for less than 180 days in a 12 month period.

Non-residents are liable to taxation in the Faroe Islands of income from vessels registered in the Faroe Islands, or from vessels that have been bare-boat chartered by a Faroese company.

Non-residents are also liable to taxation in the Faroe Islands from royalty payments, dividend payments, income from rent of real estate and income from private business carried out from a permanent establishment in the Faroe Islands.

Tax liability according to domestic law may be subject to tax treaty relief.

4.2 Tax Rates for non-resident individuals

Non-residents that only receive remuneration in cash are taxed at a flat rate of 42% of their taxable income. No deductions are allowed in the taxable income.

Non-resident crews on board vessels registered in the Faroe Islands International Registry of Ships (FAS) are taxed at a flat rate of 35% of their taxable income. No deductions are allowed in the taxable income.

Non-residents that have other types of taxable income, e.g. net income from private business or income from rent of real estate, pay state and municipal tax at the same rates as residents.

Non-residents working for a non-resident employer in connection with Hydrocarbon activities in Faroese Waters are taxed at a flat rate of 35%. If the employer is a resident, the non-resident is taxed at a flat rate of 42%. Royalty payments to non-residents are taxed at 25% while dividend payments to non-residents are taxed at 35%.

5 Tax collection for individuals

5.1 Withholding tax

All remuneration in the Faroe Islands has to be paid out through an approved clearing house. In practice, this means that all remuneration is paid out through Faroese banks. The banks withhold the state, municipal and church tax as well as various contributions to social security.

The withheld taxes and social security contributions are transferred and reported to the Tax Authorities by the banks. The net amount, after taxes and social contributions, is then transferred to the owner's account.

Employers have no obligation to withhold tax on wage payments. Employers only have to submit the required information to the chosen Faroese bank, and ensure that sufficient funds are on deposit to cover the gross wage.

Self-employed have to register their expected net annual income with the Tax Authorities and then pay the tax in 12 equal instalments during the income year.

Capital income from Faroese sources, e.g. interest and dividends, are subject to withholding taxes at source.

5.2 Income tax return

Individuals whose taxable income only consists of wages from a Faroese employer receive an annual tax statement from the Tax Authorities. The taxpayer is required to file a tax return only if the information on the tax statement is incorrect. The tax return has to be filed no later than 1st May in the year following the income year.

Individuals who have taxable income other than wages from Faroese employers have to file a tax return no later than 1st May in the year following the income year.

Individuals with capital gains income other than interest from deposits in Faroese banks have to file a capital gains income tax return no later than 1st May in the year following the income year.

5.3 Estate Tax

For deceased persons who were domiciled in the Faroe Islands at the time of death, estate tax is levied on their worldwide estate. If the deceased

was domiciled outside the Faroe Islands, estate tax only has to be paid of the value of real estate in the Faroe Islands. The tax rate depends on the relationship between the beneficiary and the deceased as shown in the following table.

DKK	Group A	Group B	Group C	Group D
under 1,000	1.00%	4.00%	7.00%	10.00%
1,001 - 2,000	1.25%	4.25%	7.25%	10.25%
2,001 - 3,000	1.50%	4.50%	7.50%	10.50%
3,001 - 5,000	1.75%	4.75%	7.75%	10.75%
5,001 - 10,000	2.00%	5.00%	8.00%	11.00%
10,001 - 20,000	2.25%	5.25%	8.25%	11.25%
20,001 - 50,000	2.50%	5.50%	8.50%	11.50%
50,001 - 100,000	2.75%	5.75%	8.75%	11.75%
over 100,000	3.00%	6.00%	9.00%	12.00%

Group A: Spouse and children, including adopted children

Group B: Parents and heirs of parents if they are not part of group A

Group C: Grandparents or their heirs

Group D: Distant relations or not related persons

When the beneficiary is the state, churches, municipalities, associations, institutions etc. the estate tax is 10%.

6 Tax Subsidies

Residents can apply for tax subsidies in connection with certain types of private expenses.

6.1 Interest Subsidy

Residents can apply for interest subsidy for loans to private housing (mortgage loan - buying or repairing) and for loans to pay for education. No subsidy is granted for private consumer loans.

For loans to private housing, subsidy can only be granted when residence is actually taken up. However, when a loan is taken to build a new private residence, subsidy can also be granted for a period of two years before residence is taken up. In such cases the subsidy is paid out retroactively after residence has been taken up.

For loans to private housing, subsidy can be granted with an interest ceiling of DKK 110,000 per year. For the years 2017 and 2018 the ceiling will be lowered to DKK 105,000 and DKK 100,000 respectively.

There is no ceiling for interest on education loans.

The interest subsidy is 35% of the interest.

After approval of an application, interest subsidy is paid out once a month.

6.2 Transportation Subsidy

For travel expenses to and from work, subsidy may be granted at a standard rate provided that the daily transportation distance to and from work exceeds 20 km. For transportation distances above 20 km, the subsidy may be granted at the following daily rates.

Distance to and from work in km	DKK per day
20 to 30 km	6.00
30 to 50 km	14.50
50 to 64 km	21.50
64 to 102 km	28.00
102 to 124 km	33.50
124 to 146 km	39.00
146 to 168 km	44.50
168 to 190 km	50.00
190 to 212 km	55.50
Above 212 km	61.00

Special rates apply for trips by helicopter, ferry or passage through an underwater tunnel. These rates are:

	DKK per trip
Transportation by helicopter	16.90
Transportation by ferry to the South Island (Suðuroy)	16.90
Transportation by ferry to other islands	8.45
Passage through an underwater tunnel	8.45

Transportation subsidy can be granted for a maximum of 220 working days per year. Subsidy is paid out twice a year. A new application has to be submitted each time.

6.3 Other Subsidies

Subsidies may also be granted when residents have expenses in connection with:

- housing due to continues work away from home
- alimony and child support
- education

All subsidies are tax exempt.

7 Social Security

Residents and employers are required to pay social security contributions to the unemployment insurance fund, the fund for maternity leave and the labour market pension fund. Residents are also required to pay contribution to general healthcare.

7.1 Unemployment and maternity leave

Residents aged between 16 and 67, working in the Faroe Islands for a Faroese employer or working for a foreign employer who carries out activities through a permanent establishment in the Faroe Islands are liable to contribute to the unemployment insurance fund (ALS) and to the maternity leave fund (BAS). Contribution to these two funds is also obligatory for the employer.

For both the employer and the employee, the contributions are calculated of the gross taxable remuneration, however not of remuneration in kind. For the employer, the contributions have to be paid along with the remuneration and for the employee maternity leave fund, the contributions are withheld by the bank together with the income taxes.

For 2016, the rates are as follows:

	ALS	BAS
Employer	1.25%	0.71%
Employee	1.25%	0.71%

For employees, the contribution to the unemployment insurance fund is limited to DKK 8,150 per year. For employers, the contributions to both the unemployment fund and the maternity leave fund are tax deductible. Employees cannot deduct contributions to the unemployment fund and the maternity leave fund.

Self-employed persons can voluntarily contribute to the unemployment insurance fund and to the maternity leave fund. The voluntarily contribution to the unemployment insurance fund is DKK 3,000 per year. The voluntarily contribution to the maternity leave fund is DKK 500 per year. Voluntary contributions are not tax deductible.

Residents working for a foreign employer can also voluntarily contribute to the unemployment insurance fund and to the fund for maternity leave. The voluntary contribution is DKK 3,000 per year to the unemployment insurance fund and DKK 500 per year to the fund for maternity leave.

7.2 Labour market pension fund

In general, all individuals, both resident and non-resident, have to contribute to the labour market pension fund (AMEG). Furthermore, all resident employers and foreign employers who carry out activities through a permanent establishment in the Faroe Islands also have to contribute to the labour market pension fund.

The contribution for employees and self-employed is calculated on the basis of the regular taxable income. For employers, the contribution is calculated on the basis of paid out remuneration.

For 2016, the rates are as follows:

	AMEG-contribution
Employer	2.25%
Employee	2.25%
Self-employed	2.25%

For the employer, the contribution is paid along with the remuneration. For the employee, the contribution is paid together with the withheld tax on paid out remuneration. For employers, the contribution is tax deductible. Employees cannot deduct contributions to the labour market pension fund.

7.3 Healthcare

Membership of the national health insurance is mandatory for all residents aged 18 and older. A contribution of DKK 175 in addition to 0.60% of a person's taxable income has to be paid each month. The contribution cannot be deducted in the taxable income. Except from this contribution, health care is generally free in the Faroe Islands, but exceptions apply to medicinal and dental treatment.

8 Company taxation

A company's taxable income consists of regular taxable income and capital gains income, both taxable at 18%.

Partnerships are not subject to company taxation. Partnerships prepare financial statements and each partner then declares their respective profit share on their personal income tax return.

8.1 Tax liability

A company is liable to taxation in the Faroe Islands when it is incorporated under Faroese company law, or when its effective management is situated in the Faroe Islands.

Companies not resident in the Faroe Islands are subject to tax on certain types of income derived from sources within the Faroe Islands, including:

- income gained from a permanent establishment in the Faroe Islands
- profit from participation in enterprises with a permanent establishment in the Faroe Islands
- income from real estate located in the Faroe Islands
- dividend and royalties received from Faroese sources

Income may be subject to tax treaty relief. For more on non-resident companies, see chapter on foreign companies with activities in the Faroe Islands.

8.2 Taxable income

Company income is divided between regular taxable income and capital gains income. The two types of taxable income are calculated separately and stated on separated tax returns.

Regular taxable income

General taxable income is computed on the basis of the annual accounts, adjusted to comply with prevailing tax rules. Deductions include most expenses, which would normally appear in the accounts, provided they are incurred in generating or maintaining the taxable income.

Expenses that are incurred in connection with establishment of a business or a new line of business, or expenses incurred in respect to creation of capital are not deductible.

In general, the accrual concept is followed. Thus, an expense is deductible in the year to which the expenditure relates rather than the year in which payment is made. General provisions are not allowable for tax purposes.

Tax losses can be carried forward without time limitations. Tax losses cannot be carried back and offset against income from past years. A tax loss in regular taxable income can also be offset against a positive capital gains income.

Thin capitalization rules apply to loans from a controlling person or company if the debt to equity ratio exceeds 4:1. External debt where a group related party has provided security may also be covered by the thin capitalization rules. The limitation does not apply to debt on arm's length terms.

Parent companies and their wholly owned Faroese subsidiaries can apply for joint taxation. Foreign companies cannot be part of a joint taxation scheme with a Faroese company.

Capital gains income

Capital gains and losses on shares, bonds and other investment papers are included in the taxable capital gains income. For companies, the total amount of the taxable capital gains income is pooled together in a separate tax return and taxed at a rate of 18%.

The taxable income in connection with disposal of shares or bonds is calculated as the difference between sales price and acquisition cost. The acquisition cost for bonus shares is nil.

The acquisition value for shares acquired prior to 16th November 2001 is the market value of the shares as per 31st December 2006. Thus only the increase in value after 1 January 2007 is subject to taxation for shares acquired prior to 16th November 2001.

All dividend distributions to Faroese companies are tax exempt. Dividend distributions to foreign companies are subject to a withholding tax at 18%. The dividend tax may be reduced according to provisions in tax treaties.

Liquidation proceeds, distributed in the calendar year in which the liquidation is finalized, are treated as disposal of shares. Liquidation proceeds, distributed before the year of the final liquidation, are taxed as dividends.

Tax losses in capital gains income can be carried forward without time limitations. Tax losses cannot be carried back and offset against capital gains income from past years. Tax losses in the capital gains income cannot be offset against positive regular taxable income.

8.3 Depreciations

	Annual depreciation
Machinery and ships on a reduced balance.	30%
For cars registered for private use, the maximum depreciable amount is DKK 150,000.	30%
If the initial expenditure of new machines etc. is DKK 20,000 or less, the expenses can be deducted immediately.	
Similarly, expenses concerning acquisition of software can be deducted immediately, irrespective of the amount.	
Industrial buildings and hotels, including necessary office- and storage facilities.	7% and 2%
Other buildings, including office- and warehouses where at least 75% of the floor space is used commercially including necessary storage facilities.	4% and 1%

Buildings are depreciated using the straight-line method. The higher rates for buildings can only be used the first 10 years. Depreciation of private houses is not allowed.

Recaptured depreciations and capital gains on property and plant, machinery, equipment, aircraft, ships and buildings are included in the regular taxable income.

Capital gain in connection with sale of a building is calculated on the basis of an indexed purchase value and actual sales price. Losses from sale of buildings are not deductible.

Goodwill and other intangible assets can be depreciated with 10% of the purchase price a year.

Ships and fishing licences are depreciated according to the same principles and with the same maximum rate as machinery and equipment, but in a separate pool. It is possible to take up to 45% in advance depreciation on ships before they are brought into operation. Advance depreciation is based on the cost price in the purchase agreement. Advance depreciation cannot exceed 15% of the purchase price per year. After delivery, normal depreciation is calculated on the purchase price reduced by the advance depreciation.

The acquisition cost of fishing days and fishing quotas may be expensed in the year of acquisition.

8.4 Tonnage Taxation

Faroese companies that carry on shipping activities (transporting people or goods) can choose to be taxed according to the tonnage taxation scheme. Under the tonnage tax scheme, the taxable income is not based on a profit and loss account. Instead, a deemed income is calculated based on the company's total net tonnage.

The deemed income is taxed at the normal corporate tax rate of 18%. The deemed income is calculated by multiplying the numbers of the days in a year that a vessel is in operation by the following rates:

Net tonnage for each vessel	DKK per 100 NT per day
Up to 1,000	6
1,001 – 10,000	4
10,001 – 25,000	3
More than 25,000	1

8.5 Hydrocarbon Taxation

Licensees

Licensees are liable to an income tax of 27% of income derived from hydrocarbon production. In principle, the taxable income of a licensee is calculated according to the same rules as for companies subject to regular taxable income.

However, the Minister of tax affairs is entitled to decide on the adoption of norm prices for extracted hydrocarbons for the purpose of assessing taxable income. If a norm price is adopted, the norm price shall be equal to the market price charged in trading between independent parties on an arm's length basis.

The acquisition costs of licences, permits and other rights may be depreciated at equal yearly amounts over a period of five years. Capital gains from the disposal of a hydrocarbon license are taxed at 27%.

In addition to the regular income tax, companies holding a hydrocarbon license shall pay a royalty of 2% of the revenue of hydrocarbons produced. Furthermore, licensees may be liable to pay an additional progressive rent resource tax on supernormal profits.

8.6 Tax collection for companies

Companies must file their tax returns on 1st July at the latest in the year following the income year. Company tax regarding regular taxable income is payable in three instalments in October, November and December. Company tax regarding capital gains income is payable in one instalment. In a joint taxation scheme, the parent company is responsible for filing the tax returns and paying the calculated taxes for all the companies in the joint taxation.

Tax relief may be granted on income from a permanent establishment abroad.

9 Non-resident companies

Non-resident companies that carry out activities in the Faroe Islands can become tax liable to the Faroe Islands depending on the nature and duration of these activities.

9.1 Branch or subsidiary

Generally, the advantages and disadvantages of each form of legal entity must be considered on a case-by-case basis.

The calculation of taxable income is basically the same for a subsidiary as for a branch. Both entities must base their inter-company transactions on the "arm's length" principle and each will be considered as an independent operation for Faroese tax purposes.

Profits of a branch may be remitted to the head office free of withholding tax, whereas dividends remitted by a subsidiary to its foreign parent company are subject to an 18% withholding tax (or such reduced rate as is provided for in a tax treaty). In principle, there are no restrictions on the remittance of the profits of a branch to its head office.

Filing requirements are different for the two types of entities. A subsidiary must file its own annual accounts to the Company Registration Authorities, and its own tax return to the Tax Authorities. A branch must file the annual accounts of its parent company to the Company Registration Authorities, and its own tax return to the Tax Authorities. Annual accounts that are submitted to the Company registration Authorities are available to the general public, while tax returns that are submitted to the Tax Authorities are not available to the general public.

9.2 Permanent establishment

In general the Faroese definition of a permanent establishment follows the OECD definition, meaning that a permanent establishment is a fixed place of business where work is performed or from where the business is managed.

For a permanent establishment to exist in connection with construction activities, the activities must have certain duration, depending on tax treaty between the Faroe Islands and the resident country. The tax treaties with the other Nordic countries and Great Brittan stipulate a 12 month minimum period before a permanent establishment is created in connection with construction activities.

Where the Faroe Islands do not have a tax treaty with the resident country, the foreign company will have a permanent establishment after 30 days in connection with construction activities.

9.3 Interest, dividends and royalties to non-resident companies

In principle, a foreign company receiving dividends or royalties is subject to tax on the amount earned. Faroese companies must withhold 18% of the dividend amount for taxes. In most tax treaties, the withholding tax on dividends is reduced to between 0% and 15%.

A withholding tax of 25% is imposed on royalties. Royalties include any payment received as remuneration for the application of or the right to use any patent, trademark, pattern or model, drawing, secret formula or process of production, or as remuneration for industrial, commercial or scientific know-how. Artistic royalties (copyrights) are not tax exempt from tax. The withholding tax may be reduced according to the tax treaty with the country in question.

The Faroe Islands do not withhold tax on interest paid to non-resident companies.

9.4 Transfer pricing

Faroese transfer pricing legislation applies to foreign companies that carry out tax liable activities in the Faroe Islands either through a branch or a subsidiary. The transfer pricing legislation implies that foreign companies subject to the rules must:

- Apply the arm's length principle when determining intercompany transfer prices
- Disclose the nature and extent of intra-group transactions in their tax return
- Prepare and maintain written documentation which justify that price for company transactions are at arm's length basis

9.5 Thin Capitalization

Thin capitalization rules apply to branches with subsidiaries that have "controlled debt", restricting the deductibility of interest expenses and capital losses. Controlled debt is defined as debt to related parties or debt to a party for which security has been given by a related party.

The effect of the thin capitalization rules is that deduction is denied for interest expenses and capital losses of the controlled debt when a 4:1 debt to equity ratio is not met.

The right to deduct interest on controlled debt is not restricted where the company can show that similar financing can be obtained from an independent lender.

All assets and liabilities of Faroese subsidiaries and branches under common control are consolidated for the purpose of calculating the debt equity ratio.

9.6 Double taxation treaties

The Faroe Islands have concluded tax treaties with the following countries:

- Denmark
- Norway
- Iceland
- Sweden
- Finland
- United Kingdom
- India
- Greenland
- Switzerland

All of these conventions are based on the OECD Model Convention, and the Tax Authorities usually interpret the tax treaties in line with the OECD Model Convention.

10 Value Added Tax

Faroese value added tax (VAT) is levied at a standard rate of 25% on the net invoice price for supply of goods and services.

10.1 VAT liability

All enterprises with activities subject to VAT and with a turnover exceeding DKK 30,000 per year are obliged to register with the Tax Authorities and charge VAT.

VAT is charged on the basis of the net invoice price of goods delivered and services provided, including all costs incurred such as packing, freight, insurance, installation and commission.

VAT is charged on all taxable imports from outside Faroe Islands and is paid to the Tax Authorities by the importer. The taxable value for imported goods is the value as determined for import duty purposes. Exports of goods and certain services are zero-rated for VAT purposes.

VAT on Sales

Most services and all goods supplied in the Faroe Islands are subject to VAT. However, supply of the following services is exempt from VAT:

- Hospital, medical and dental care
- Education
- Certain cultural activities and sports
- Personal transportation
- Financial and insurance transactions
- Sale and rental of real estate (voluntary registration is an option)
- Betting, gambling and lotteries
- Literary, compositional and other artistic activities
- Travel agencies

VAT on Purchases

VAT registered businesses can normally recover all VAT expenses, except VAT on expenses such as:

- Purchases related to business activities that are exempt from VAT
- Meals and housing for the owner and employees of a business enterprise
- Purchases of automobiles for private transportation
- Gifts

10.2 Foreign enterprises

Foreign enterprises with activities subject to Faroese VAT are obliged to register with the Tax Authorities if they have established a place of business or a place of residence in the Faroe Islands.

Foreign enterprises selling goods or services in the Faroe Islands, without having a permanent establishment in the country, are obliged to register with the Tax Authorities through a Faroese VAT representative. The foreign enterprise and the Faroese VAT representative will be jointly liable for the payment of VAT.

However, a foreign enterprise, which exports goods directly to a Faroese importer, is not liable to register, as the importer is responsible to pay the VAT (reverse charge). Enterprises from Iceland can be registered without a Faroese VAT representative.

Foreign enterprises selling services in the Faroe Islands, without having a place of business or a place of residence in the country, are obliged to register with the VAT authorities unless reverse charge rules apply, see below.

Reverse charge

Reverse charge rules always apply when a foreign enterprise supplies the following services to a buyer in the Faroe Islands regardless if the buyer is VAT registered or not:

- transfers and assignments of copyrights, patents, licences, trademarks and similar rights
- advertising services
- services of consultants, engineers, lawyers, accountants and other similar services
- data processing and the provision of information
- supply of staff
- supply of services by intermediaries, acting in the name and on behalf of other persons

Reverse charge rules also apply when a foreign enterprise supplies the following services to a VAT registered buyer in the Faroes:

- services in connection with real estate
- work in the Faroe Islands on movable tangible property
- telecommunications services
- radio and television broadcasting services

10.3 Registration and filing requirements

The registration with the Tax Authorities has to be in place at least 8 days before a VAT activity is undertaken.

VAT returns are due within one month and ten days after the end of each quarter. However, the Tax Authorities may permit some businesses recovering VAT regularly to file returns on a monthly or a weekly basis. The net VAT due must be paid no later than the last date of filing of the VAT return. If VAT is recoverable, the excess amount is normally refunded within three weeks after the return has been filed.

Foreign enterprises that are not VAT registered in the Faroe Islands may claim reimbursement of VAT expenses incurred in the Faroe Islands by filing a claim with the Tax Authorities. The reimbursement is only available to the extent that a similar Faroese enterprise may recover VAT on purchases of a corresponding nature in accordance with the Faroese VAT Act.

10.4 Payroll Tax

Payroll tax is levied on financial and insurance services as well as on VAT exempt medical services.

Payroll tax is payable by the following enterprises:

- financial institutions and insurance companies
- private medical institutions

The payroll tax rate is 2.5% for medical institutions, 10% for insurance companies and 12% for financial institutions. The calculation basis for medical institutions that are operated as private businesses is the payroll adjusted for taxable income. For medical institutions operated as a public or a private company, the calculation basis is the total payroll. For financial institutions and insurance companies, the calculation basis is the total payroll.

11 Customs and Excise Duties

11.1 Customs Duties

Goods imported into the Faroe Islands may be subject to customs duties. The basis of the charge varies with the classification of the goods imported. Goods originating in the European Union, Iceland, Norway or Switzerland are exempt from import duties.

11.2 Excise Duties

Excise duties are levied on a variety of commodities, including alcoholic beverages, tobacco, tea, coffee, chocolate, confectionery and motor fuel. Excise duties are normally levied on the producer or the importer when the commodities are imported.

12 Import of Private Cars

A registration tax is levied on the importation of private cars. The registration tax is in two parts, a value based tax and a carbon dioxide tax.

Value based tax

For cars that are registered for private use, the value based tax is 50% of the cost price up to DKK 100,000 and 75% of the cost price above DKK 100,000. Insurance and freight are included in the cost price (CIF).

No value based tax is paid for electric cars that are registered before 1 January 2020.

For cars that have been registered abroad for less than 5 years before importation to the Faroe Islands, the original cost price is reduced by 10% for each year before the value based tax is calculated. For cars that have been registered abroad for more than 5 years before importation to the Faroe Islands, the original cost price is reduced by 50% before the value based tax is calculated.

Carbon dioxide tax

The carbon dioxide tax is levied according to how much carbon dioxide is emitted by a car per kilometre.

CO2 emissions (g/km)	CO2 tax (DKK/g)
Less than 120	20
Between 120 and 140	200
Between 140 and 180	300
Above 180	400

Importation of cars as removal goods

Persons who stay in the Faroe Islands temporarily can be granted permission to import a car for private use only for up to one year without having to pay registration taxes.

Tax Figures For 2016

DKK	2016
Free accommodation	
Value of free accommodation per m2	754
Free electricity	10,000
Free heating	22,300
Free board	
3 meals a day	61
2 meals a day	46
1 meal a day	35
Private consumption of goods	
Grocers	16,600
Bakers, selling groceries	13,800
Bakers	5,200
Company car	
Less than 1,100 kg	55,500
Between 1,101 kg and 1,300 kg	64,400
Between 1,301 kg and 1,500 kg	77,300
More than 1,500 kg	86,900
Vans and other cars	
Less than 1,100 kg	33,300
Between 1,101 kg and 1,300 kg	38,640
Between 1,301 kg and 1,500 kg	46,380
More than 1,500 kg	52,140
Private use of cars, taxi drivers	18,700

DKK	2016
Unemployment insurance fund	1.25%
Compulsory labour market pension fund	2.25%
Maternity leave fund	0.71%
Deductions in calculated state and local taxes	
Personal allowance, pension, single	16,200
Personal allowance, pension, married	10,500
Deduction in state tax for each child	6,500
Interest subsidy	35%
Tax ceiling	50%

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