

Hopefully We Will Say Goodbye to the Unshell Proposal

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This note briefly describes an [analysis](#) made by the author regarding the [Unshell Proposal](#) (the Proposal). In that analysis, the author presented her concerns regarding the reasons and benefits outlined by the Commission in its Impact Assessment Report and Explanatory Memorandum (working documents), with a view to encouraging the EU Member States to reach an agreement on the Proposal.

As part of the analysis, the author assessed whether the reasons and benefits outlined by the Commission in the working documents are justified, realistic and desirable. In questioning all these reasons and benefits, the author wondered whether they will prove sufficient and realistic for the EU Member States to commit to implementing the Proposal as it stands. The author also highlighted the undesirable indirect consequences that may occur and affect the EU market.

1. Only 25,000 entities are targeted by the Proposal, but 25.3 million EU active enterprises fall under its scope – which proves to be an unjustified reason

There are 25.3 million EU [active enterprises](#) that fall under scope of the Proposal; however, only 25,000 entities are targeted by the Proposal, which, as per the author, proves to be an unjustified reason for the EU Member States to adhere to it.

Interestingly, there are [no statistics regarding shell entities](#) within the European Union. Nevertheless, the Commission justified the need to implement the Proposal by making reference to studies providing rough estimates. The Commission mentioned in the [Impact Assessment Report](#) that 75,000 shell companies within the European Union are targeted. This is a rough estimation of the upper threshold, with the lower threshold expected to be around 25,000 shell entities, without taking into consideration the carve-out provisions in the Proposal (based on which these upper and lower thresholds are expected to be even lower).

2. Loss of tax revenues will decrease, but this is not generated by shell entities – which proves to be an unrealistic benefit

There is [no data available](#) regarding the loss of tax revenues caused further to the use of shell entities for tax avoidance and tax evasion purposes. Despite this lack of data, the Commission again emphasized that the Proposal will play a role in reducing the [estimated tax loss of EUR 20 billion](#) in the European Union. In the Impact Assessment Report, the Commission even declared that a small decrease of 10% of tax avoidance through shell entities would [recover EUR 2.3 billion per year](#) for EU Member States' public finances. There is no evidence as to how the figure of 10% was chosen. Moreover, the author noticed that different amounts are used in the working documents.

3. Sanctions will bring revenues to the budgets of EU Member States – which proves to be an unrealistic benefit

Surprisingly, as a benefit of the implementation of the Proposal, the [Commission mentioned](#) the increase of tax revenues from the collection of the regulatory charges due to the sanctions provided, but this argument cannot be accepted as a realistic benefit for any tax measure promoted, no matter its scope.

4. Shell entities are present in a few EU Member States, but the Proposal should be implemented by all EU Member States – which is an undesirable indirect consequence

The Commission mentioned three EU Member States in the Impact Assessment Report based on a report published by the IMF. Luxembourg and the Netherlands rank on the top list of the countries with entities through which foreign direct flows were channelled. Ireland then follows, due to the absence of withholding taxes on dividends, interest and royalties.

As the Proposal targets entities through which passive income flows, the lack of withholding taxes on passive income becomes relevant. Luxembourg and the Netherlands have already taken [measures to improve their legislation](#). However, the Commission considers that these tax measures are probably not enough and that all EU Member States should thus collectively implement measures to counter shell entities.

5. Targeted measures at the level of EU Member States are not enough, despite the fact that the Proposal brings more complexity – which proves to be an unjustified reason

Many measures have already been implemented by EU Member States to counter aggressive tax planning structures, such as the Anti-Tax Avoidance Directive ([ATAD 1](#) and [ATAD 2](#)) and the [Directive on Administrative Cooperation](#). It is also worth mentioning the amendment regarding mandatory reporting of arrangements by tax intermediaries, known as DAC 6. Despite the fact that there is no evaluation of these already implemented measures at the level of the EU Member States, the Commission continues to [promote new measures](#), as “legal entities with no minimal substance and economic activity continue to pose a risk of being used for improper tax purposes, such as tax evasion and avoidance”.

Based on a review of the tax legislation of EU Member States, it was recognized that the applicable laws lack measures to specifically counter shell entities and the recent EU actions considered as relevant (such as ATAD 1, ATAD 2 and DAC 6) for curbing the problem of shell entities present limitations, but the [Commission has not detailed them](#).

6. Lack of definitions for shell, tax avoidance and tax evasion causes tax uncertainty instead of certainty – which is an undesirable indirect consequence

As the Proposal does not define “shell entities”, “tax avoidance” or “tax evasion” (the main concepts of the Proposal), there is a high risk that the number of disputes will increase among EU Member States, which brings uncertainty to taxpayers.

7. Penalizing shell entities by not issuing a certificate of tax residence presents the risk of affecting all taxpayers when requiring certificates of tax residence – which is an undesirable indirect consequence

The Proposal stipulates that no certificate of tax residence will be issued by the tax authorities of the EU Member State in which the undertaking is resident if the minimum substance criteria are not met. In addition to the problems raised by the implementation of the vague text of the Proposal by all EU Member States, the big

question that remains is whether there is any risk that the EU Member States will require all taxpayers, not only risky shell entities, to follow the procedure stipulated by the Proposal when issuing a certificate of tax residence.

8. Substance criteria are not clear enough, thus the number of disputes is expected to increase – which is an undesirable indirect consequence

As the minimum substance criteria are not adapted to the new realities, combined with the fact that they are open to different interpretation by the 27 EU Member States, the author expects the Proposal to increase the number of disputes between tax authorities of different EU Member States and between taxpayers and their tax authorities.

9. Information will be better assessed, but there is a lack of resources in the tax administrations allocated for this purpose – which is an undesirable indirect consequence

The Commission mentioned that the Proposal will help tax authorities gain access to information through the exchange-of-information procedures and that, in this way, the phenomenon of shell entities would be better understood. Thus, more resources will be needed in each EU Member State to analyse, understand and assess the value of the information collected and exchanged among EU Member States. However, the Commission seems to not have paid attention to the [feedback received in the public consultation](#), in which the business stakeholders complained that there is insufficient capacity within tax administrations to process the already available information on tax avoidance structures along with insufficient cooperation between EU Member States.

10. More documents will need to be prepared, without a guarantee that the same documents will be required in all EU Member States – which is an undesirable indirect consequence

As per the author, the fight for simplicity of rules is lost considering the compliance burden increases due to all recent measures implemented at the EU level, including the Proposal, and the fear amongst taxpayers that different documents will be required in all 27 EU Member States, an indirect consequence that the Commission did not take into account in its working documents for the Proposal.

11. Limited costs are needed for implementation of the Proposal, but in reality higher costs will be incurred by taxpayers and tax authorities – which proves to be an unjustified reason

In the author's opinion, higher costs will be due for complying with the Proposal, enhanced by the lack of clarity of definitions and criteria that the undertakings and tax authorities must comply with. This proves contrary to the opinion of the Commission that there will be a significant share of entities that will not have to do anything, as the reporting is not applicable to them or they are covered by one of the carve-outs or exemptions.

12. Lack of a procedure to perform an audit at the request of another EU Member State may disturb the activity of tax authorities from the other EU Member State – which is an undesirable indirect consequence

It is not clear how a tax audit will be performed and how the results of such a tax audit will be used by the EU Member States directly involved, as well as in the other EU Member States. A procedure needs to be drafted and implemented at the level of the EU Member States, otherwise there is a risk that the tax authorities from one EU Member State will interfere in the activities of the tax authorities of another EU Member State, an indirect consequence that the Commission did not take into account in its working documents for the Proposal. At present, there are rumours that the option to require a tax audit will be eliminated from the Proposal, but no official position has been published by the Commission.

Is this the end?

Until now, the EU Member States have not reached consensus on the Proposal. In June 2024, under the Belgian presidency of the EU Council, some compromise solutions for agreeing on the Proposal were discussed; however, under the Hungarian presidency, the Proposal is not considered a priority. The author is wondering whether it is time to say goodbye to the Proposal.

IBFD references

- > For an overview of legislative initiatives at the EU level on direct tax matters from the moment they are planned by the European Commission until their adoption by the Council of the European Union, see the [EU Direct Tax Law Initiatives Dossier](#)
- > For details on the Harmonization of Corporate Taxation in the European Union, see [C. Valério & S. Kale, Direct Taxation, Global Topics IBFD](#), in particular section 3.6., on the Unshell proposal.
- > [S. Kleefstra, The \(Un\)intended Consequences of the Proposed Unshell Directive, Talking Points 19 \(2022\), Journal Articles & Opinion Pieces IBFD](#)
- > [R.H.M.J. Offermanns, The Proposed Unshell Directive – The Luxembourg and Netherlands Approach, 62 Eur. Taxn. 6 \(2022\), Journal Articles & Opinion Pieces IBFD](#)
- > [P. Pistone et al., Abuse, Shell Entities and Right of Establishment: A Plea for Refocusing Current Proposals and Achieving Deeper Coordination within the Internal Market, 14 World Tax J. 2 \(2022\), Journal Articles & Opinion Pieces IBFD](#)
- > [O. Popa, Proposal for an EU Directive Laying Down Rules to Prevent the Misuse of Shell Entities for Tax Purposes \(Unshell\): Seven Steps towards Disgrace or Redemption, 62 Eur. Taxn. 4 \(2022\), Journal Articles & Opinion Pieces IBFD](#)
- > [O. Popa, What to expect in terms of EU tax law and policy from the second half of 2024 \(and beyond\), EU Tax Focus \(8 July 2024\), IBFD](#)
- > [A. Xygka, The “lost but not found” initiatives’ club: Unshell and others, EU Tax Focus \(24 June 2024\), IBFD](#)
- > EU tax law developments are reported in the daily IBFD [Tax News Service](#).

IBFD webinar: [Unshell Directive Proposal: Tax Implications and Critical Issues | IBFD](#)