

# Procedure file

Basic information		
CNS - Consultation procedure Directive	<a href="#">2021/0434(CNS)</a>	Awaiting final decision
Taxation: rules to prevent the misuse of shell entities for tax purposes Amending Directive 2011/16 <a href="#">2009/0004(CNS)</a>		
Subject 2.70 Taxation		

Key players			
European Parliament	Committee responsible	Rapporteur	Appointed
	 <a href="#">Economic and Monetary Affairs</a>	 <a href="#">PEREIRA Lídia</a>	25/01/2022
		Shadow rapporteur	
		 <a href="#">TANG Paul</a>	
		 <a href="#">BOYER Gilles</a>	
		 <a href="#">URTASUN Ernest</a>	
		 <a href="#">BECK Gunnar</a>	
		 <a href="#">HOOGEVEEN Michiel</a>	
		 <a href="#">WALLACE Mick</a>	
Council of the European Union European Commission	Commission DG <a href="#">Taxation and Customs Union</a>	Commissioner GENTILONI Paolo	

Key events			
22/12/2021	Legislative proposal published	<a href="#">COM(2021)0565</a>	Summary
14/02/2022	Committee referral announced in Parliament		
30/11/2022	Vote in committee		
12/12/2022	Committee report tabled for plenary, 1st reading/single reading	<a href="#">A9-0293/2022</a>	Summary

16/01/2023	Debate in Parliament		
17/01/2023	Results of vote in Parliament		
17/01/2023	Decision by Parliament	<a href="#">T9-0004/2023</a>	Summary

### Technical information

Procedure reference	2021/0434(CNS)
Procedure type	CNS - Consultation procedure
Procedure subtype	Legislation
Legislative instrument	Directive
	Amending Directive 2011/16 <a href="#">2009/0004(CNS)</a>
Legal basis	Treaty on the Functioning of the EU TFEU 115
Other legal basis	Rules of Procedure EP 159
Stage reached in procedure	Awaiting final decision
Committee dossier	ECON/9/08059

### Documentation gateway

Legislative proposal	<a href="#">COM(2021)0565</a>	22/12/2021	EC	Summary
Document attached to the procedure	SEC(2021)0565	22/12/2021	EC	
Document attached to the procedure	SWD(2021)0577	22/12/2021	EC	
Document attached to the procedure	SWD(2021)0578	22/12/2021	EC	
Document attached to the procedure	SWD(2021)0579	22/12/2021	EC	
Economic and Social Committee: opinion, report	<a href="#">CES6494/2021</a>	23/03/2022	ESC	
Committee draft report	<a href="#">PE731.794</a>	12/05/2022	EP	
Amendments tabled in committee	<a href="#">PE735.759</a>	08/09/2022	EP	
Committee report tabled for plenary, 1st reading/single reading	<a href="#">A9-0293/2022</a>	12/12/2022	EP	Summary
Text adopted by Parliament, 1st reading/single reading	<a href="#">T9-0004/2023</a>	17/01/2023	EP	Summary

### Additional information

Research document	<a href="#">Briefing</a>	15/09/2022
-------------------	--------------------------	------------

## Taxation: rules to prevent the misuse of shell entities for tax purposes

**PURPOSE:** to reduce tax revenue loss related to tax avoidance and tax evasion due to the use of shell entities in the EU.

**PROPOSED ACT:** Council Directive.

**ROLE OF THE EUROPEAN PARLIAMENT:** the Council adopts the act after consulting the European Parliament but without being obliged to follow its opinion.

**BACKGROUND:** on 18 May 2021, the European Commission adopted a Communication on Business Taxation for the 21st century to promote a robust, efficient and fair business tax system in the European Union. It sets out both a long-term and short-term vision to support Europe's recovery from the COVID-19 pandemic and to ensure adequate public revenues over the coming years. It aims to create an equitable and stable business environment, which can boost sustainable and job-rich growth in the Union.

The Commission proposal responds to a request from the European Parliament for EU action to counter the misuse of shell entities for tax purposes and, more generally, to the demand of several Member States, businesses and civil society for a stronger and more coherent EU approach against tax avoidance and evasion.

This proposal is one of the short-term, targeted initiatives which were announced in the Communication as a means to improve the current tax system with a focus on ensuring fair and effective taxation. It complements a number of other policy initiatives promoted by the Commission in parallel, in the short- and long-term. These include a [proposal](#) for a Directive on ensuring a global minimum level of taxation for multinational groups in the Union.

As a reminder, shell entities are legal entities and arrangements with no or only minimal business presence and economic activity. Shell companies are often used for aggressive tax planning or tax evasion purposes. Businesses can direct financial flows through shell entities towards jurisdictions that have no or very low taxes, or where taxes can easily be circumvented. Similarly, some individuals can use shells to shield assets particularly real estate from taxes, either in their country of residence or in the country where the property is located.

The number of shell entities within the EU is unknown. This is in particular because within the EU, there is no common definition of what shell entities are and consequently nor statistics about them.

CONTENT: this Commission proposal aims to counter the misuse of shell entities for tax purposes only, and in so doing contribute to fair and effective taxation. It lays down indicators of minimum substance for undertakings in Member States and rules regarding the treatment for tax purposes of those undertakings that do not meet the indicators. It will apply to all undertakings that are considered tax resident and are eligible to receive a tax residency certificate in a Member State.

#### Transparency

The proposal aims to introduce, within the EU, common rules to be able to identify shell entities at high risk of tax abuse. Such rules would define objective substance requirements and would ensure that shell entities used for tax abuse can be identified promptly. However, substance requirements alone are not enough to prevent tax abuse. To be effective, the initiative will set clear, pre-determined, common tax consequences throughout the EU to prevent tax losses and also to prevent tax and regulatory arbitrage in the EU.

#### Substance test

The proposal lays down a test that will help Member States to identify undertakings that are engaged in an economic activity, but which do not have minimal substance and are misused for the purpose of obtaining tax advantages. This test can be commonly referred to as a substance test. Using a number of objective indicators related to income, staff and premises, the proposal will help national tax authorities detect entities that exist merely on paper.

#### Gateways

The proposal introduces a filtering system for the entities in scope, which have to comply with a number of indicators. These levels of indicators constitute a type of gateway. The Commission sets out three gateways. If a company crosses all three gateways, it will be required to annually report more information to the tax authorities through its tax return.

1. The first level of indicators looks at the activities of the entities based on the income they receive. The gateway is met if more than 75% of an entity's overall revenue in the previous two tax years does not derive from the entity's business activity or if more than 75% of its assets are real estate property or other private property of particularly high value.
2. The second gateway requires a cross-border element. If the company receives the majority of its relevant income through transactions linked to another jurisdiction or passes this relevant income on to other companies situated abroad, the company crosses to the next gateway.
3. The third gateway focuses on whether corporate management and administration services are performed in-house or are outsourced.

#### Exchange of information

In addition, Member States need to know about the existence of shell entities being identified as such in another Member State. This would allow other Member States to take effective and prompt actions to address cross-border tax abuse by, for example, denying tax treaty benefits on withholding taxes paid to the shell entity by a company in their own jurisdiction. Timely availability of information on the existence of identified shell entities, both at national level and in other Member States, will provide Member States with an effective mechanism to prevent shell entity tax abuse in the EU. Member States will exchange the information within 30 days from the time the administration has such information.

#### Penalties

The proposal leaves it to Member States to lay down penalties applicable against the violation of the reporting obligations provided by the draft directive as transposed into the national legal order. The penalties shall be effective, proportionate and dissuasive. A minimum level of coordination should be achieved amongst Member States through the set of a minimum monetary penalty as per existing provisions in the financial sector. Penalties should include an administrative pecuniary sanction of at least 5% of the undertakings turnover.

#### Deter trust or company service providers from creating shell entities in the EU

Lastly, the proposal aims to discourage the use of trust or company service providers from creating shell entities in the EU in the first place. The substance requirements include criteria which aim to combat the very services that trust or company service providers offer such as setting up postal addresses.

## Taxation: rules to prevent the misuse of shell entities for tax purposes

---

The Committee on Economic and Monetary Affairs adopted, under the consultation procedure, the report by Lídia PEREIRA (EPP, PT) on the proposal for a Council directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU.

Members recalled that the Pandora Papers revelations reported on the creation of shell companies with the purpose of moving money between bank accounts, avoiding taxes and committing financial crimes, including money laundering, and circumventing Union sanctions on

Russian oligarchs. They consider it essential that the directive sets ambitious and proportionate standards for defining common minimum substance requirements, for improving the exchange of information between national tax administrations and for deterring the use of shell companies promoted by certain intermediaries.

The committee responsible recommends that the European Parliament approve the Commission proposal subject to the following amendments:

#### Identification of companies that do not meet minimum substance indicators

According to Members, Member States should require undertakings meeting the following cumulative criteria to report to the competent authorities of Member States:

- more than 65% (instead of 75%) of the revenues accruing to the undertaking in the preceding two tax years is relevant income of the company's revenue in the previous two tax years is relevant income;
- the undertaking is engaged in cross-border activity on any of the following grounds: (i) more than 55% (instead of 60%) of the book value of the undertakings assets that fall within the scope of Article 4, points (e) and (f), was located outside the Member State of the undertaking in the preceding two tax years; (ii) more than 55% (instead of 60%) of the undertakings relevant income is earned or paid out via cross-border transactions;
- in the preceding two tax years, the undertaking outsourced the administration of day-to-day operations and the decision-making on significant functions to a third party.

Members deleted the derogation for undertakings with at least five own full-time equivalent employees or members of staff exclusively carrying out the activities generating the relevant income.

#### Indicators of minimum substance for tax purposes

Member States should require that undertakings meeting the criteria declare in their annual tax return, for each tax year, whether they meet the following indicators of minimum substance:

- the undertaking has own premises in the Member State, premises for its exclusive use or premises shared with entities of the same group;
- the undertaking has at least one own and active bank account or e-money account in the Union through which the relevant income is received;
- one or more directors of the undertaking are qualified and authorised to take decisions in relation to the activities that generate relevant income for the undertaking or in relation to the undertakings assets;
- the majority of the full-time equivalent employees of the undertaking have their habitual residence as set out in Regulation (EC) No 593/2008 in the Member State of the undertaking, or are at no greater distance from that Member States insofar as such distance is compatible with the proper performance of their duties.

Undertakings should accompany their tax return declaration with documentary evidence including:

- an overview of the structure of the undertaking and associated enterprises and any significant outsourcing arrangements, including the rationale behind the structure, described in the context of a standardised format;
- a summary report of the documentary evidence submitted under this paragraph, containing in particular: (i) a brief description of the nature of the activities of the undertaking; (ii) the number of employees on a full-time equivalent basis; (iii) the amount of profit or loss before and after taxes.

#### Rebuttal of the presumption

Member States should take measures to enable undertakings that are presumed not to have minimum substance to rebut this presumption, without undue delay and excessive administrative costs, by providing any additional supporting evidence of the business activities which they perform to generate relevant income.

To this end, undertakings should provide the following additional evidence: (i) a document allowing to ascertain the business rationale behind the establishment of the undertaking in the Member State where the activity is performed; (ii) information on the profiles of full-time, part-time and freelance employees while ensuring high levels of data protection and privacy.

The Member State should consider a request for the rebuttal of the presumption within a period of nine months after the introduction of the request and it should be considered to be accepted in the absence of an answer from the Member State after the expiry of that nine-month period.

#### Tax consequences of not having minimum substance

Where an undertaking does not have minimum substance for tax purposes in the Member State where it is resident for tax purposes, that Member State should deny any request for a certificate of tax residence to the undertaking for use outside the jurisdiction of that Member State.

When denying a request for such certificate, the Member State should issue an official statement duly justifying such decision and prescribing that the undertaking is not entitled to the benefits of agreements and conventions that provide for the elimination of double taxation of income, and, where applicable, capital, or of international agreements with a similar purpose or effect.

#### Penalties

Penalties should include (i) an administrative pecuniary sanction of at least 2% of the undertakings revenue in the relevant tax year, if the undertaking that is required to report does not comply with such requirement for a tax year within the prescribed deadline and an administrative pecuniary sanction of at least 4% of the undertakings revenue if the undertaking that is required to report makes a false declaration in the tax return.

#### Review

No later than five years after the date of transposition of the Directive, the Commission should present a report on the implementation and operation of the Directive. Where appropriate, the report would be accompanied by a review with a view to increasing the effectiveness of the Directive and a legislative proposal to amend the Directive.

The report should assess:

- the impact of this Directive on tax revenues in Member States, on tax administrations capacities and in particular, whether there is a need to amend this Directive;
- whether it would be appropriate to add a substance indicator based on pre-tax profit per employee and to extend the obligation to report on indicators of minimum substance for tax purposes set out in that Article to regulated financial undertakings and, if necessary, review the exemption granted to them.

## Taxation: rules to prevent the misuse of shell entities for tax purposes

---

The European Parliament adopted by 593 votes to 21, with 8 abstentions, following a special legislative procedure (consultation of Parliament), a legislative resolution on the proposal for a Council directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU.

Members pointed out that the misuse of shell entities for tax purposes leads to a reduction in tax liability and tax loss within the Union. They consider that it is therefore essential that this Directive sets ambitious and proportionate standards for the definition of common minimum substance requirements, for the improvement of exchange of information between national tax administrations and for the dissuasion of the use of shell entities promoted by certain intermediaries.

The European Parliament approved the Commission proposal subject to the following amendments:

Identification of companies that do not meet minimum substance indicators

According to Members, Member States should require undertakings meeting the following cumulative criteria to report to the competent authorities of Member States:

- more than 65% (instead of 75%) of the revenues accruing to the undertaking in the preceding two tax years is relevant income of the company's revenue in the previous two tax years is relevant income;
- the undertaking is engaged in cross-border activity on any of the following grounds: (i) more than 55% (instead of 60%) of the book value of the undertakings assets that fall within the scope of Article 4, points (e) and (f), was located outside the Member State of the undertaking in the preceding two tax years; (ii) more than 55% (instead of 60%) of the undertakings relevant income is earned or paid out via cross-border transactions;
- in the preceding two tax years, the undertaking outsourced the administration of day-to-day operations and the decision-making on significant functions to a third party.

Indicators of minimum substance for tax purposes

Undertakings meeting the criteria declare in their annual tax return should, for each tax year, whether they meet the following indicators of minimum substance:

- the undertaking has own premises in the Member State, premises for its exclusive use or premises shared with entities of the same group;
- the undertaking has at least one own and active bank account or e-money account in the Union through which the relevant income is received;
- one or more directors of the undertaking are qualified and authorised to take decisions in relation to the activities that generate relevant income for the undertaking or in relation to the undertakings assets;
- the majority of the full-time equivalent employees of the undertaking have their habitual residence as set out in Regulation (EC) No 593/2008 in the Member State of the undertaking, or are at no greater distance from that Member States insofar as such distance is compatible with the proper performance of their duties.

Undertakings should accompany their tax return declaration with documentary evidence including:

- an overview of the structure of the undertaking and associated enterprises and any significant outsourcing arrangements, including the rationale behind the structure, described in the context of a standardised format;
- a summary report of the documentary evidence submitted under this paragraph, containing in particular: (i) a brief description of the nature of the activities of the undertaking; (ii) the number of employees on a full-time equivalent basis; (iii) the amount of profit or loss before and after taxes.

Rebuttal of the presumption

Member States should take measures to enable undertakings that are presumed not to have minimum substance to rebut this presumption, without undue delay and excessive administrative costs, by providing any additional supporting evidence of the business activities which they perform to generate relevant income.

To this end, undertakings should provide the following additional evidence: (i) a document allowing to ascertain the business rationale behind the establishment of the undertaking in the Member State where the activity is performed; (ii) information on the profiles of full-time, part-time and freelance employees while ensuring high levels of data protection and privacy.

The Member State should consider a request for the rebuttal of the presumption within a period of nine months after the introduction of the request and it should be considered to be accepted in the absence of an answer from the Member State after the expiry of that nine-month period.

Where a Member State considers that an undertaking has satisfactorily rebutted a presumption of lack of substance, it should be able to adopt a decision certifying that the undertaking has minimum substance for tax purposes. This decision should remain valid for up to 5 years from the date of adoption of the decision.

#### Tax consequences of not having minimum substance

Where an undertaking does not have minimum substance for tax purposes in the Member State where it is resident for tax purposes, that Member State should deny any request for a certificate of tax residence to the undertaking for use outside the jurisdiction of that Member State.

When denying a request for such certificate, the Member State should issue an official statement duly justifying such decision and prescribing that the undertaking is not entitled to the benefits of agreements and conventions that provide for the elimination of double taxation of income, and, where applicable, capital, or of international agreements with a similar purpose or effect.

#### Penalties

Members stressed that Member States must share relevant information to which they have access, implement systems supporting the exchange of that information and, as a final step, enforce proposed sanctions against non-complying entities.

Penalties should include (i) an administrative pecuniary sanction of at least 2% of the undertakings revenue in the relevant tax year, if the undertaking that is required to report does not comply with such requirement for a tax year within the prescribed deadline and an administrative pecuniary sanction of at least 4% of the undertakings revenue if the undertaking that is required to report makes a false declaration in the tax return.

#### Request for a joint tax audit

Where the competent authority of one Member State has reason to believe that an undertaking which is resident for tax purposes in another Member State has not met its obligations under this Directive, the former Member State may, specifying such reasons, request the competent authority of the latter to conduct a joint tax audit of the undertaking. If the requesting competent authority is not able to conduct a joint tax audit due to legal reasons, the competent authority of the requested Member State should initiate a national audit within one month from the date of receipt of the request.

#### Review

No later than five years after the date of transposition of the Directive, the Commission should present a report on the implementation and operation of the Directive. Where appropriate, the report would be accompanied by a review with a view to increasing the effectiveness of the Directive and a legislative proposal to amend the Directive.

The report should assess:

- the impact of this Directive on tax revenues in Member States, on tax administrations capacities and in particular, whether there is a need to amend this Directive;
- whether it would be appropriate to add a substance indicator based on pre-tax profit per employee and to extend the obligation to report on indicators of minimum substance for tax purposes set out in that Article to regulated financial undertakings and, if necessary, review the exemption granted to them.