Update: European Parliament adopts amended Unshell Directive

January 2023

On 22 December 2021, the European Commission published an EU Directive proposal that lays down rules to prevent the misuse of shell entities for tax purposes and to expand the scope of the EU Council Directive on administrative cooperation ('Unshell Directive'). For a more detailed explanation of this proposal, we refer to our previous insight: see proposal for preventing the misuse of shell entities (ATAD3).

The EU Parliament's Committee on Economic and Monetary Affairs proposed a number of amendments to the Unshell Directive. on January 17th 2023. The European Parliament adopted the European Commission proposal (with the proposed changes) and calls on the European Council to adopt the proposed amendments on 17 January 2023.

Amendments

The most significant changes to the proposed Unshell directive made by the Committee of the European Parliament on Economic and Monetary Affairs relate to the gateway criteria, which have been revised as follows:

- More than 65% (previously 75%) of the revenue in the preceding two years is "relevant income," which broadly covers passive income (e.g., dividends, interest, royalties);
- More than 55% (previously 60%) of the book value of the entity's assets has been located outside the undertaking's member state for at least two years, or more than 55% (previously 60%) of the entity's relevant income is earned through cross-border transactions; and
- The entity has outsourced the administration of its day-to-day operations and decision-making to a third party (bold is added in the proposal).

If an entity responds affirmatively to all three tests, it would be subject to new tax reporting obligations related to economic substance, specifically with respect to its premises, whether it has its own active bank account in the EU and the tax residence of its director(s) and the majority of its full-time employees.

If an entity lacks substance based on one or more of these indicators, it would be presumed to be a shell entity for purposes of the directive and would not be eligible for benefits under the EU Parent-Subsidiary and Interest and Royalty Directives or applicable tax treaties. Failure to comply with the rules would result in a penalty of at least 5% of the entity's turnover for the relevant year. Regardless of whether the entity qualifies as a shell entity, the information reported would be exchanged automatically.

An entity still would be able to rebut the presumption of shell company status by providing additional evidence at least on the commercial rationale for the undertaking.

Next steps

The directive requires unanimity in the European Council for its adoption, following consultation of the European Parliament. The negotiations in the European Council are ongoing.

Analyze your structure

Adoption of the proposed directive would mark a significant step in the area of direct taxation within the EU as it is a first harmonization of minimum substance criteria for tax purposes. Companies that are potentially in scope should carry out an analysis on their corporate structures. We are here to help you in making such an analysis.