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2021/0434 (CNS)

Proposal for a

COUNCIL DIRECTIVE

**laying down rules to prevent the misuse of shell entities for tax purposes and amending
Directive 2011/16/EU**

{SEC(2021) 565 final} - {SWD(2021) 577 final} - {SWD(2021) 578 final} -
{SWD(2021) 579 final}

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

- **Reasons for and objectives of the proposal**

On 18 May 2021, the European Commission adopted a Communication on Business Taxation for the 21st century¹ 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. 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.

While important progress has been made in this area in the last years, especially with the adoption of the anti-tax avoidance directive (ATAD)² and the expansion of scope of the directive on administrative cooperation (DAC)³, 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, as confirmed by recent massive media revelations⁴. While there can be valid reasons for the use of such entities, there is a need for further action to tackle situations where taxpayers evade their obligations under tax law or act against the actual purpose of tax law by misusing undertakings that do not perform any actual economic activity. The outcome of such situations is to lower the taxpayers' overall tax liability. Such outcome leads to a shift of the tax burden at the expense of honest taxpayers and distorts business decisions in the internal market. Unless it is effectively tackled, this situation creates an environment of unfair tax competition and unfair tax burden distribution. This Directive applies to all undertakings that are considered tax resident and are eligible to receive a tax residency certificate in a Member State.

Having the aim of combating tax avoidance and evasion practices, which directly affect the functioning of the internal market, this Directive lays down anti-tax avoidance and evasion rules in a specific area. It 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.

- **Consistency with existing policy provisions in the policy area**

This Directive is part of the central EU strategy on direct corporate taxation with a view to ensuring that everybody pays their fair share. The Commission has been consistent in the pursuit of policies to fight tax avoidance and tax evasion in the last decade.

In particular, and by way of an example, in 2012, the Commission published a recommendation on Aggressive Tax Planning, recommending to Member States specific measures against double non-taxation and artificial arrangements for tax purposes. In 2016, the anti-tax avoidance directive (ATAD) was adopted to ensure coordinated implementation

¹ COM(2021) 251 final

² Council Directive 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (OJ L 193, 19.7.2016, p. 1).

³ Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC (OJ L 64, 11.3.2011, p. 1).

⁴ See, for example, the OpenLux investigation and, more recently, the Pandora Papers

in Member States of key measures against tax avoidance stemming from the international Base Erosion and Profit Shifting Project actions. In parallel, the directive on administrative cooperation (DAC) has, since its adoption in 2011, been revised and expanded on several occasions to allow a large-scale and timely exchange of tax related information across the EU, including on tax rulings and mandatory reporting of arrangements by tax intermediaries mandatory. From an international angle, the EU list of non-cooperative jurisdictions in tax matters has been launched since 2017, amongst others, to protect Member States' tax bases from third countries' harmful tax practices.

Existing tax instruments at EU level do not contain, however, explicit provisions targeting shell entities, i.e. entities that do not perform any actual economic activity, even if they are presumably engaged with one, and that can be misused for tax avoidance or evasion purposes. The risk that such entities may pose for the Single Market and specifically for Member States' tax bases has been highlighted by recent tax-related scandals.

- **Consistency with other Union policies (possible future initiatives of relevance to the policy area)**

This Directive follows up to the Commission's Communication on Business Taxation for the 21st century for a robust, efficient and fair business tax system in the EU and reflects one of the policy initiatives envisaged in such Communication. As such 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. This Directive, which aims to discourage the use of shell entities established in the Union for tax purposes, has a broader scope than the Directive on a minimum level of taxation, as it encompasses all entities and legal arrangements resident for tax purposes in the Union, without any threshold based on revenues. On the other hand, the legal framework on the minimum level of taxation applies only to MNE groups and large-scale domestic groups with combined revenues that exceed EUR 750 million. Such groups also fall within the ambit of this Directive. This is because the two initiatives have different purposes.

The legal framework on the minimum level of taxation exclusively pertains to the rate, i.e. level of taxation. It does not touch upon potentially harmful features of the tax base. Neither does it involve examining whether an entity possesses sufficient substance to carry out the activity that it is supposed to. It is true that the implementation of the rules on the minimum level of taxation may gradually discourage the creation of shell entities to some extent. Yet, this is yet an unknown outcome which cannot be guaranteed at this stage.

In addition, an exclusion from the scope of this Directive of the groups within the scope of the Directive on a minimum level of taxation would create unequal treatment against 'shell' entities belonging to smaller-sized groups that do not meet the threshold of EUR 750 million. It would namely be mostly large MNE groups that would receive a waiver from the transparency requirements and the tax consequences under this Directive.

Additional announced initiatives involve proposals to require all EU entities to publish their effective tax rate on an annual basis and to tackle the tax bias in favour of debt financing by placing equity financing in the single market on an equal footing to debt. In addition, this Directive is consistent with, and complementary to, Union policies in relation to transparency of beneficial ownership information.

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

- **Legal basis**

Direct tax legislation falls within the ambit of Article 115 of the Treaty on the Functioning of the EU (TFEU). The clause stipulates that legal measures of approximation under that article shall be vested the legal form of a Directive.

- **Subsidiarity (for non-exclusive competence)**

This proposal complies with the principle of subsidiarity. The nature of the subject requires a common initiative across the internal market.

The rules of this Directive aim to tackle cross-border tax avoidance and evasion practices and provide a common framework to be implemented into Member States' national laws in a coordinated manner. Such aims cannot be achieved in a satisfactory manner through action undertaken by each Member State while acting on its own.

The use of legal entities and arrangements without minimal substance for tax avoidance or tax evasion purposes is usually not limited to the territory of only one Member State. A key feature of relevant schemes is that they involve the tax systems of more than one Member State at a time. Several Member States could therefore be impacted by a scheme that would include the use of a shell entity located in another Member State.

The review of Member States anti-tax avoidance and evasion rules indicates fragmentation. Some Member States have developed targeted rules or practices, including criteria on substance, to counter abuse by shell entities in the area of taxation. However, most Member States do not apply targeted rules, but may rely on general anti-abuse rules, which they tend to apply on a case-by-case basis. Even amongst the few Member States that have developed targeted rules at national level, the rules differ significantly, and reflect more national tax systems and priorities, rather than target the internal market dimension.

The existing fragmentation could be replicated and possibly worsened, were Member States to take action individually. Such an approach would perpetuate the present inefficiencies and distortions in the interaction of distinct measures. If the objective is to adopt solutions that function for the internal market as a whole and improve its (internal and external) resilience against tax evasion and tax avoidance practices that affect or can affect equally all Member States, the appropriate way forward involves a coordinated initiative at the level of the EU.

Furthermore, an EU initiative would add value, as compared to what a multitude of actions taken at national level can attain. Given that the envisaged rules have a cross-border dimension and that shell entities are commonly used to erode the tax base of a Member State different from that where the shell entity is located, it is imperative that any proposals balance divergent interests within the internal market and consider the full picture, to identify common objectives and solutions. This can only be achieved if legislation is designed centrally. Moreover, a common approach towards shell entities would ensure legal certainty and reduce compliance costs for businesses operating within the EU.

Such an approach is therefore in accordance with the principle of subsidiarity, as set out in Article 5 of the Treaty on the European Union.

- **Proportionality**

The envisaged measures do not go beyond ensuring the minimum necessary level of protection for the internal market. The Directive does not therefore prescribe full harmonization but only a minimum protection for Member States' tax systems.

In particular, the Directive lays down a test to facilitate Member States to identify manifest cases of shell entities misused for tax purposes in a coordinated manner across the EU. National rules, including rules transposing EU law, shall continue to apply to identify shell entities not captured by this Directive. The application of these latter national rules should also be facilitated by virtue of the measures of this Directive, as Member States will have access to new information concerning shell entities. Furthermore, the Directive lays down consequences for shell entities taking into due account agreements and conventions in place between Member States and third countries for the elimination of double taxation of income, and where applicable, capital.

Thus, the Directive ensures the essential degree of coordination within the Union for the purpose of materializing its aims. In this light, the proposal does not go beyond what is necessary to achieve its objectives and is therefore compliant with the principle of proportionality.

- **Choice of the instrument**

The proposal is for a Directive, which is the only available instrument under the legal base of Article 115 TFEU.

3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS

- **Ex-post evaluations/fitness checks of existing legislation**

Existing anti-tax avoidance legislation does not include measures targeted to undertakings that do not have minimum substance for tax purposes. Therefore, evaluation is not relevant.

- **Stakeholder consultations**

On 4 June 2021, TAXUD launched a public consultation on a potential initiative to fight the use of shell entities and arrangement for tax purposes. It contained 32 questions aimed, inter alia, at delineating the problem and its drivers and identifying the appropriate form of EU action and the key features of shell entities being at risk to be misused for tax purposes. The consultation closed on 27 August 2021 with a total of 50 replies.

All respondents acknowledge that in spite of the recent EU anti-tax avoidance measures the problem of tax avoidance and evasion persists, including through the misuse of shell entities. While some respondents welcome new targeted measures to tackle abuse in the tax area, others consider that they are potentially premature.

Respondents point to the low capacity of Member States' tax administrations and inadequate administrative cooperation as the main problem drivers.

As regards the features common in shell entities that present a risk for being misused for tax purposes, there is broad agreement that absence of an own bank account is one of them and is indicative. There is also wide convergence that another common feature is where the directors, in their majority, do not reside in the country where the entity is located. However, there is no wide agreement on the pertinence of other factors, such as the number of employees.

Furthermore, respondents agree that shell entities at risk to be misused are more likely to be identified amongst those engaged with the activity of holding and managing equity or intellectual property or with financing and leasing activity. While respondents consider that a shell entity prone to misuse can be set up in any legal form, they seem to find trusts to be at

slightly higher risk. Whether an entity is a small or medium enterprise (SME) does not arise as a relevant feature to be taken into account.

Notably 33 respondents, in particular business and professional associations, provided extensive input which goes beyond the consultation questions. A significant part of these respondents, differently for the other respondents, has concerns that new EU legislation targeted to tax avoidance and evasion through the misuse of shell entities might not be timely, also in light of the international discussions towards global minimum effective taxation.

Moreover, these respondents stress that defining what is a shell entity is challenging and that assessing lack of substance depends on the facts and circumstances of each specific entity. In this regard, they highlight that taxpayers should have an effective right to provide evidence of their specific circumstances. Usefully, these respondents have also provided specific examples of structures that could be considered not to have substance, i.e. to be shell, but are not put in place to obtain tax advantages but rather for valid commercial reasons.

In addition to the public consultation, national experts in direct taxation have been consulted in a targeted manner. A meeting of Working Party IV on tax questions was held on 22 June 2021 and bilateral consultations followed. Overall Member States expressed support for a new EU initiative targeting the misuse of shell entities to obtain tax advantages. Member States welcomed the definition of common rules on the misuse of shell entities together with a framework for administrative cooperation. Member States also argued for a broad scope of the new measures and stressed that SMEs should be equally covered. Amongst the available policy options, Member States expressed support for regulatory action.

In forming its proposal, the Commission took into account the results of the consultation. In particular, amongst the various policy options, the Commission decided to proceed with a proposal for regulatory and binding action, i.e. a directive under art. 115 TFEU. Furthermore, the directive proposed distinguishes entities at risk to be shell and misused to obtain tax advantages by reference to a set of features common in such entities. Specific shell entities are however carved out upfront as they are commonly used for good commercial reasons. In designing the distinctive criteria that would single out entities at risk and in defining the cases that should be excluded because they do not present tax avoidance or evasion risks, the Commission relied on the input of the stakeholders. SMEs are not excluded from the proposal as there is wide agreement that they do present relevant risks. In recognition of the fact that substance is ultimately a matter of facts and circumstances the directive includes a mechanism allowing taxpayers to challenge the outcome of the test therein, including by evidencing the commercial, non-tax motives, underlying a certain structure. In the same vein, structures that are not put in place with the main purpose to obtain a tax advantage may avail of a mechanism to request an upfront exemption.

As regards the question whether measures targeted to the misuse of shell entities for tax purposes would be timely or premature, the Commission holds that there is indeed a clear need for such measures. The need for such measures arises clearly in the aftermath of continuous scandals on the misuse of shell entities worldwide and specifically in the single market. The future application of the rules on global minimum effective taxation would not fully address the issue of shell companies as those rules would only apply to multinational companies that meet the EUR 750 million threshold, thus leaving all companies below this threshold out of the scope. In the same vein, the Commission appreciates that the protection of Member States' taxable bases is all the more important to ensure a sustainable economy under the exceptional circumstances imposed by the health crisis.

- **Collection and use of expertise**

In identifying appropriate measures to tackle the misuse of shell entities for tax purposes, the Commission drew on an extensive study conducted by the International Bureau of Fiscal Documentation (IBFD). The study was submitted to the Commission in the context of the public consultation. It concludes that existing EU anti-avoidance measures do not suffice to tackle tax related issues surrounding shell companies and coordinated action promoting cross-border consistency in the applicable tax treatment to shell arrangements is to be welcomed. It also observes that Member States' rules targeting specifically shell arrangements are relatively uncommon. In addition, the Commission relied on a study on letterbox companies carried out by an external contractor and commissioned independently from this initiative.

The Commission relied on the results of these studies in defining the specific features that should single out the entities at clear risk to be shell and be misused to obtain tax advantages.

- **Impact assessment**

An impact assessment was carried out to prepare this initiative.

On 22 October 2021 the Regulatory Scrutiny Board (RSB) issued a positive opinion with reservations on the submitted impact assessment regarding the present proposal, including several suggestions for improvement.⁵ The Impact Assessment report (IA) was further revised along these lines, as explained below.

The IA examines four policy options in addition to the baseline scenario, i.e. no action. Option 1 was the pursuit of soft law action by expanding the mandate of an existing peer review instrument, the Code of Conduct (Business Taxation). As an alternative, the IA examined the possibility for the Commission to adopt a recommendation to Member States. However, soft law instruments may be expected to be of limited effect in resolving the problem of the misuse of shell entities for tax purposes, this is a cross-border issue and requires a consistent approach across the EU, which cannot be ensured via soft law.

Options 2, 3 and 4 are regulatory and prescribe a set of rules that should be put in place in all Member States. They differ on the extent to which coordination is sought. Option 2 envisaged coordination of the criteria and processes to identify shell entities as well as coordination on their treatment. Option 3 includes, in addition to Option 2, a mechanism for automatic exchange of information. Option 4 adds to Option 3 a prescription of sanctions against non-compliant entities.

The various Options have been compared against the following criteria: a) effectiveness in reducing the misuse of shell entities, b) tax gains for public finances, c) compliance costs for businesses, d) compliance costs for tax administrations, e) indirect effects on the single market, f) indirect effects on competition among firms, g) indirect effects on EU competitiveness, h) indirect effects – social impacts and i) coherence. The comparison revealed that Options 2, 3 and 4 can be expected to be, despite their costs, effective in meeting the objectives of this initiative. Amongst them, Option 4 appears to perform best. Specifically, it is expected to be the one ensuring the highest level of compliance by the entities in scope, while it is coherent with the current EU agenda on fighting tax avoidance and evasion and builds on existing systems for exchange of information.

⁵ [OP please insert the links to the summary sheet and the positive opinion of the RSB after their publication.]

Economic impacts

The assessment of the economic impacts was subject to data limitations, because the initiative concerns a type of entity for which there is severe lack of data and no commonly acceptable definition.

Benefits

Nevertheless, the preferred option (Option 4) is expected to have a positive economic impact. As main direct benefit, it is expected that there will be an increase in the collection of tax revenues by reducing the misuse of shell entities in the EU. Even a small reduction of the current estimated tax loss (estimated at around EUR 20 billion in the EU) will represent significant additional public resources. Option 4 is the most effective as the outcome of identifying the existence of a shell entity is reinforced by implications: the exchange of information between Member States and a common sanctions regime at EU level. Some additional direct benefits could be obtained from the regulatory charges due to the sanctions. The initiative will also provide significant indirect benefits. Thanks to this action, valuable information will be collected to better understand the phenomenon of shell entities for tax purposes. It will also signal that the EU is committed to ending tax avoidance and evasion within its borders encouraging tax compliance.

Costs

The main costs related to the selected option are the increase in compliance costs for businesses and tax administrations. Tax compliance costs for business are expected to increase in a limited manner. Overall, costs should be relatively limited because the number of companies in scope of this initiative is expected to be low (less than 0.3% of all EU companies), and the additional data to be reported by those in scope should be easy to retrieve and relatively simple to provide. For tax administrations, costs are also expected to increase modestly. Tax administrations should expand their capabilities in order to administer the information that they will have access to, implement the systems supporting the exchange of information and enforce the proposed sanctions. This proposal aims, by design, to find a good balance between positive impacts and additional burden. There are risks in the capacity of Member States to deal with the new responsibilities, for example in the management of tax rulings.

Main changes implemented

The RSB issued a positive opinion with reservations on the IA. In particular, the RSB noted that IA is not clear on why tax avoidance and evasion should be addressed together and what distinguishes legitimate shell entities from those misused for tax purposes. The RSB also noted that the IA does not provide sufficient overview of possible alternative and/or complementary measures, beyond the introduction of EU legislation. Furthermore, the RSB noted that the IA should be enhanced as regards quantitative estimates, in particular compliance costs for businesses, and should better reflect the different stakeholder views in the main analysis. Annex I to the Impact Assessment explains how the RSB reservations were addressed. Several parts of the IA were revised and new parts were added in order to address the concerns raised by the RSB. First, a new section has been added in order to explain, also by way of examples, how shell entities can serve both tax avoidance and tax evasion practices in similar ways and why, therefore, there is room to address them together. In addition, the IA has been revised in order to clarify that the distinction between legitimate and non-legitimate shells is a matter of how they are used rather than one of construction. Second, the IA has been expanded in order to reflect in detail the various alternatives considered at an early stage to tackle the problematic use of shell entities in the tax area. In this respect, it has been

explained why the option of regulating trust and company service providers, as a standalone or complementary measure, has not been promoted. The reasons why the introduction of substance requirements has been considered the option fit for purpose have also been further analysed. Third, the IA has been revised to include further details on the estimated compliance costs for business and administrations, and in particular, details on the reasoning behind the estimations, additional arguments and new evidences. Moreover, several sections of the main part of the IA have been revised in order to include relevant stakeholder input, gathered through public and specific consultations procedures.

4. BUDGETARY IMPLICATIONS

See Legislative Financial Statement.

5. OTHER ELEMENTS

- **Implementation plans and monitoring, evaluation and reporting arrangements**

This proposal, once adopted as a Directive, should be transposed into Member States' national law by 30 June 2023 and come into effect as of 1 January 2024. For the purpose of monitoring and evaluation of the implementation of the Directive, Member States shall provide the Commission, on a yearly basis, with relevant information per tax year, including a list of statistical data. The relevant information is set out in Article 12 of the Directive.

The Commission shall submit a report on the application of this Directive to the European Parliament and to the Council every five years, which should start counting after [1 January 2024]. The results of this proposal will be included in the evaluation report to the European Parliament and to the Council that will be issued by [1 January 2029].

- **Detailed explanation of the specific provisions of the proposal**

The Directive is broadly inclusive and aims to capture all undertakings that can be considered resident in a Member State for tax purposes, regardless of their legal form. In this vein, it also captures legal arrangements, such as partnerships, that are deemed residents for tax purposes in a Member State.

The Directive targets a specific scheme used for tax avoidance or tax evasion purposes. The scheme targeted involves the setting up of undertakings within the EU which are presumably engaged with an economic activity but that, in reality, do not conduct any economic activities. Instead, the reason for which they are in place is to enable certain tax advantages to flow to their beneficial owner or to the group to which they belong, as a whole. For example, a financial holding undertaking may collect all payments from financial activities of undertakings in different EU Member States, taking advantage of the exemptions from withholding taxes under the Interest and Royalty Directive⁶ and then pass on this income to an associated enterprise in a low tax third country jurisdiction, exploiting favourable tax treaties or even domestic tax law of a specific Member State. In order to tackle this scheme, this Directive 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

⁶ Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States (OJ L 157, 26.6.2003, p. 49).

“substance test”. In addition, the Directive attaches tax consequences to the undertakings that do not have minimal substance (shells). It also envisages automatic exchange of information as well as potential request by one Member State to another for tax audits for a broader group of undertakings that are treated as being at risk (as they fulfil certain conditions) but are not necessarily deficient in substance for the purposes of this Directive. The definition of the appropriate tax treatment and the information exchange should discourage the targeted scheme by neutralising any tax advantages gained or that can be gained.

In light of the above, the Directive is structured so as to essentially reflect the logical sequence of each step of the aforementioned substance test. There are 7 steps: undertakings that should report (due to being found to be ‘at risk’); reporting; possibility of gaining exemption from reporting for lack of tax motives; presumption of lack of minimal substance; possibility of rebuttal; tax consequences; exchange of information automatically via making data available on a Central Directory as well as potential request for the performance of a tax audit.

Undertakings that should report

The first step divides the various types of undertakings in those at risk for lacking substance and be misused for tax purposes vs. those at low risk. Risk cases are those that present simultaneously a number of features usually identified in undertakings that lack substance. These criteria are commonly referred to as ‘gateway’. Low-risk cases are those that present none or only some of these criteria, i.e. those that do not pass the gateways.

The relevant criteria that set up the gateways aim to distinguish as at risk those undertakings that seemingly engage with cross-border activities which are geographically mobile and in addition rely on other undertakings for their own administration, in particular professional third party service providers or equivalents.

Low-risk cases that do not cross the gateway are irrelevant for the purposes of the Directive. Resources can therefore focus on the most risky cases, i.e. those that present all relevant features and hence cross the gateway.

For tax certainty, undertakings performing certain activities are carved out explicitly and are therefore considered from the outset as being of low-risk and irrelevant for the purposes of the Directive. These include undertakings that would either not cross the gateway or, if they did, they would be found irrelevant for the purposes of the Directive at a later step of the test. Undertakings that fall in the scope of any of the carve-outs do not need to consider whether or not they cross the gateway.

Reporting

Only the undertakings considered at risk at the first step proceed to the second step, which is the core of the substance test itself. Due to the fact that they are at risk, these undertakings are asked to report on their substance in their tax return.

Reporting on substance means providing specific information, normally already arising from the undertaking’s tax return, in a way that facilitates the assessment of the activity performed by the undertaking. The focus is on specific circumstances that are normally present in an undertaking that performs substantial economic activity.

Three elements are considered important: first, premises available for the exclusive use of the undertaking; second, at least one own and active bank account in the Union; and third at least one director resident close to the undertaking and dedicated to its activities or, alternatively, a sufficient number of the undertaking’s employees that are engaged with its core income generating activities being resident close to the undertaking. A director’s dedication to the

activities of the undertaking may be demonstrated in his qualifications, which should be such as to allow the director to have an active role in the decision-making processes, the formal powers that he/she is vested and the director's actual participation in the day-to-day management of the undertaking. Where no director with the necessary qualifications is resident close to the undertaking, alternatively it would be expected that the undertaking has adequate nexus to the Member State of claimed tax residence if most of its employees that perform day-to-day functions are resident for tax purposes close to that Member State. Decision-making should also take place within the Member State of the undertaking. These specific elements have been selected drawing on the international standard on substantial economic activity for tax purposes.

It must be kept in mind that these elements are set with regard to undertakings with cross-border activities that are geographically mobile and which do not have own resources for their own administration.

Furthermore, the reporting must be accompanied by satisfactory documentary evidence, which should be attached to the tax return as well, if not already included. The evidence required is aimed at allowing the tax administrations to verify directly the truth of the reported information as well as to form a general overview of the situation of the undertaking so as to consider whether to initiate a tax audit.

Presumption of lack of minimal substance and tax abuse

The third step of the test prescribes the appropriate assessment of the information that the undertaking reported in the second step in terms of substance. It sets out how the outcome of the reporting, i.e. the declaration of the undertaking that it has or does not have the relevant elements, should be qualified, at least at first sight.

An undertaking that is a risk case, since it has crossed the gateway, and whose reporting also leads to the finding that it lacks at least one of the relevant elements on substance, should be presumed to be a 'shell' for the purposes of the Directive, i.e. lacking substance and being misused for tax purposes.

An undertaking that is a risk case but whose reporting reveals that it has all relevant elements of substance, should be presumed not to be a 'shell' for the purposes of the Directive. However, this presumption does not exclude that the tax administrations still find that such undertaking:

- is a shell for the purposes of the Directive because the documentary evidence produced does not confirm the information reported; or
- is a shell or lacks substantial economic activity under domestic rules other than this Directive, taking into account the documentary evidence produced and/or additional elements; or
- is not the beneficial owner of any stream of income paid to it.

Rebuttal

The fourth step involves the right of the undertaking which is presumed to be shell and misused for tax purposes, for the purposes of the Directive, to prove otherwise, i.e. to prove that it has substance or in any case it is not misused for tax purposes. This opportunity is very important because the substance test is based on indicators and as such, may fail to capture the specific facts and circumstances of each individual case. Taxpayers will therefore have an effective right to make the claim that they are not a shell in the sense of the Directive.

To claim a rebuttal of a presumption of shell the taxpayers should produce concrete evidence of the activities they perform and how. The evidence produced is expected to include information on the commercial (i.e. non-tax) reasons for setting up and maintaining the undertaking which does not need own premises and/or bank account and/or dedicated management or employees. It is also expected to include information on the resources that such undertaking uses to actually perform its activity. It is also expected to include information allowing to verify the nexus between the undertaking and the Member State where it claims to be resident for tax purposes, i.e. to verify that the key decisions on the value generating activities of the undertaking are taken there.

While the above information is essential and required to be produced by the rebutting undertaking, the undertaking is free to produce additional information to make its case. This information should then be assessed by the tax administration of the undertaking's State of tax residence. Where the tax administration is satisfied that an undertaking rebuts the presumption that it is a shell for the purposes of the Directive, it should be able to certify the outcome of the rebuttal process for the relevant tax year. As the rebuttal process is likely to create a burden for both the undertaking and the tax administration while leading to the conclusion that there is minimum substance for tax purposes, it will be possible to extend the validity of the rebuttal for another 5 years (i.e. for a total maximum of 6 years), after the relevant tax year, provided that the legal and factual circumstances evidenced by the undertaking do not change. After this period, the undertaking will need to renew the process of rebuttal if it wishes to do so.

Exemption for lack of tax motives

An undertaking that might cross the gateway and/or does not fulfil the minimum substance could be used for genuine business activities without creating a tax benefit for itself, the group of companies of which it is part or for the ultimate beneficial owner. Such an undertaking should have an opportunity to evidence this, at any time, and to request an exemption from the obligations of this Directive.

To claim such an exemption, the undertaking is expected to produce elements allowing to compare the tax liability of the structure or the group to which it is part with and without its interposition. This is similar to the exercise recommended to be undertaken in order to assess any type of aggressive tax planning schemes (Commission Recommendation of 6 December 2012 on aggressive tax planning⁷).

As is the case with the rebuttal of the presumption, the tax administration of the place of claimed tax residence of the undertaking may be considered best placed to assess the relevant evidence produced by the undertaking. Where the tax administration is satisfied that the interposition of a specific undertaking within the group does not impact on the tax liability of the group, it should be able to certify that the undertaking is not at risk of being found a 'shell' under this Directive for a tax year. As the process for obtaining an exemption could create a burden for both the undertaking and the tax administration while leading to the conclusion that there is no tax avoidance or evasion purpose, it will be possible to extend the validity of the exemption for another 5 years (i.e. for a total maximum of 6 years), provided that the legal and factual circumstances evidenced by the undertaking do not change. After this period, the undertaking will need to repeat the process of requesting for an exemption if it wishes to continue being exempt and can substantiate that it remains entitled to.

⁷ OJ L 338, 12.12.2012, p. 41.

Consequences

Once an undertaking is presumed to be a shell for the purposes of the Directive, and does not rebut such presumption, tax consequences should kick in. These consequences should be proportionate and aim at neutralising its tax impact, i.e. disallowing any tax advantages which have been obtained, or could be obtained, through the undertaking in accordance with agreements or conventions in force in the Member State of the undertaking or relevant EU directives, in particular Council Directives 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States and 2003/49/EC on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States. These advantages would be in effect disallowed if the relevant agreements, conventions and EU directives were disregarded with regard to the undertaking that was found not to have minimum substance and did not prove the contrary.

Given that to obtain these advantages, an undertaking normally needs to provide a certificate of residence for tax purposes, in order to accommodate for an efficient process, the Member State of tax residence of the shell will either not issue a tax residence certificate at all or will issue a certificate with a warning statement, i.e. including an explicit statement to prevent its use for the purposes of obtaining the above advantages. Not issuing a tax residence certificate or issuing a special certificate, including the warning described above, does not set aside the national rules of the Member State where the shell is tax resident with regard to any tax obligations linked to the shell. It will only serve as an administrative practice to inform the source country that it should not grant the benefits of its tax treaty with the Member State of the shell (or of applicable EU directives) to payments towards the shell.

If tax advantages accorded to the undertaking are disallowed, it should be determined how income flows to and from the undertaking, as well as any assets owned by the undertaking, should actually be taxed. In particular, it should be determined which jurisdiction should have a right to tax such income flows and/ or assets. Such determination should not affect any tax that may apply at the level of the shell itself; the Member State of the shell would thus remain free to continue to consider the shell as resident for tax purposes in its territory and apply tax on the relevant income flows and / or assets as per its national law.

The allocation of taxing rights should take into account all jurisdictions that may be affected by transactions involving the shell. Such jurisdictions, except for the Member State of the shell, are:

- (i) In the case of income flows: on the one hand, the source jurisdiction or jurisdiction where the payer of the income is located and on the other, the jurisdiction of final destination of the flow, i.e. the jurisdiction of the shareholder of the undertaking;
- (ii) In case of real estate assets: on the one hand, the source jurisdiction or jurisdiction where the assets are situated and on the other, the jurisdiction where the owner resides, i.e. the jurisdiction of the shareholder of the undertaking;
- (iii) In case of valuable movable assets, such as art collections, yachts etc.: the jurisdiction of the owner, i.e. of the shareholder of the undertaking.

The allocation of taxing rights necessarily affects only Member States, which are bound by this Directive, i.e. it does not and cannot affect third countries. However, situations involving third countries are indeed likely to arise, e.g. where income from a third country flows to the shell or where the shareholder(s) of the shell are in a third country or where the shell owns assets situated in a third country. In these cases, agreements for the avoidance of double taxation between a Member State and a third country should be duly respected as regards

allocation of taxing rights. In absence of such agreements, the Member State involved will apply its national law.

In detail, four scenarios can be envisaged:

(1) Third country source jurisdiction of the payer – EU shell jurisdiction – EU shareholder(s) jurisdiction

In this case the source jurisdiction is not bound by the Directive, while the jurisdictions of the shell and of the shareholder fall in scope.

- Third country source / payer: may apply domestic tax on the outbound payment or may decide to apply the treaty in effect with EU shareholder jurisdiction
- EU shell: it will continue to be resident for tax purposes in the respective Member State and will have to fulfil relevant obligations as per national law, including by reporting the payment received; it may be able to provide evidence of the tax applied on the payment
- EU shareholder(s): shall include the payment received by the shell undertaking in its taxable income, as per the national law and may be able to claim relief for any tax paid at source, in accordance with the applicable treaty with third country source jurisdiction. It will also take into account and deduct any tax paid by the shell.

(2) EU source jurisdiction of the payer– EU shell jurisdiction – EU shareholder(s) jurisdiction

In this case, all jurisdictions fall in the scope of the Directive and are therefore bound by it.

- EU source / payer: it will not have a right to tax the payment but may apply domestic tax on the outbound payment to the extent it cannot identify whether the undertaking's shareholder(s) are in the EU
- EU shell: it will continue to be resident for tax purposes in the respective Member State and will have to fulfil relevant obligations as per national law, including by reporting the payment received; it may be able to provide evidence of the tax applied on the payment
- EU shareholder(s): will include the payment received by the shell undertaking in its taxable income, as per the national law and may be able to claim relief for any tax paid at source, including by virtue of EU directives. It will also take into account and deduct any tax paid by the shell.

(3) EU source jurisdiction of the payer – EU shell jurisdiction – third country shareholder(s) jurisdiction

In this case only the source and the shell jurisdiction are bound by the Directive while the shareholder jurisdiction is not.

- EU source / payer: will tax the outbound payment according to treaty in effect with the third country jurisdiction of the shareholder(s) or in the absence of such a treaty in accordance with its national law.
- EU shell: will continue to be resident for tax purposes in a Member State and will have to fulfil relevant obligations as per national law, including by reporting the payment received; it may be able to provide evidence of the tax applied on the payment.

- Third country shareholder(s): while the third country jurisdiction of the shareholder(s) is not compelled to apply any consequences, it may be asked to apply a tax treaty in force with the source Member State in order to provide relief.
- (4) Third country source jurisdiction of the payer – EU shell jurisdiction – third country shareholder(s) jurisdiction
- Third country source / payer: may apply domestic tax on the outbound payment or may decide to apply tax according to the tax treaty in effect with the third country jurisdiction of the shareholder(s) if it wishes to look through the EU shell entity as well.
 - EU shell: will continue to be resident for tax purposes in a Member State and fulfil relevant obligations as per national law, including by reporting the payment received; it may be able to provide evidence of the tax applied on the payment
 - Third country shareholder(s): while the third country shareholder jurisdiction is not compelled to apply any consequences, it may consider applying a treaty in force with the source jurisdiction in order to provide relief.

Scenarios where shell undertakings are resident outside the EU fall outside the scope of the Directive.

Exchange of information

All Member States will have access to information on EU shells, at any time and without a need for recourse to request for information. To this effect, information will be exchanged among Member States from the first step, when an undertaking is classified as being at risk for the purposes of this Directive. Exchange will also apply where the tax administration of a Member State makes an assessment based on facts and circumstances of individual cases and decides to certify that a certain undertaking has rebutted the presumption of being shell or should be exempt from the obligations under the Directive. This will ensure that all Member States are in a position to become aware, in a timely manner, of the discretion exercised and the reasons behind each assessment. Member States will also be able to request the Member State of the undertaking to perform tax audits where they have grounds to suspect that the undertaking might be lacking minimal substance for the purposes of the Directive.

To achieve that the information is available to all Member States that may have an interest to it in a timely manner, the information will be exchanged automatically through a central directory by deploying the existing mechanism of administrative cooperation in tax matters. Member States will exchange the information in all above scenarios without delay and in any case within 30 days from the time the administration has such information. This means within 30 days from receiving tax returns or within 30 days from when the administration issues a decision to certify that an undertaking rebutted a presumption or should be exempt. Automatic exchange will also take place within 30 days from the conclusion of an audit to an undertaking at risk for the purposes of the Directive, if the outcome of such audit has an impact on the information already exchanged or that should have been exchanged for this undertaking. The information to be exchanged is prescribed in Article 13 of this Directive. The principle is that such information should allow all Member States to receive the information reported by undertakings at risk for the purposes of this Directive. In addition, where a Member State's administration assesses a rebuttal of presumption or an exemption from the obligations of the Directive, the information exchanged should allow other Member States to understand the reasons for this assessment. Other Member States should always be able to request from another Member State a tax audit on any undertaking that passes the

gateway of this Directive, if they have doubts on whether or not it has the minimal substance required. The requested Member State should perform the tax audit within a reasonable timeframe and share the outcome with the requesting Member State. If there is a finding of ‘shell’ entity, the exchange of information should be automatic in accordance with Article 13 of this Directive.

Penalties

The proposed legislation leaves it to Member States to lay down penalties applicable against the violation of the reporting obligations provided by this 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 undertaking’s turnover. Such minimum amount should take into account the circumstances of the specific reporting entity.

Proposal for a

COUNCIL DIRECTIVE

laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 115 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Parliament¹,

Having regard to the opinion of the European Economic and Social Committee²,

Acting in accordance with a special legislative procedure,

Whereas:

- (1) Ensuring fair and effective taxation in the internal market and tackling tax avoidance and evasion remain high political priorities in the Union. While recent years saw important progress in this area, especially with the adoption of Council Directive 2016/1164³ concerning anti-tax avoidance and the expansion of scope of Council Directive 2011/16/EU⁴ on administrative cooperation, further measures are necessary to tackle specifically identified practices of tax avoidance and evasion, which are not fully captured by the existing legal framework of the Union. In particular, multinational groups often create undertakings with no minimal substance, to lower their overall tax liability, including by shifting profits away from certain high-tax Member States in which they carry out economic activity and create value for their business. This proposal complements the progress achieved in corporate transparency through requirements concerning beneficial ownership information introduced by the anti-money laundering framework, which address situations where undertakings are created to conceal true ownership, whether of the undertakings themselves or of the assets they manage and own, such as real estate or property of high value.
- (2) It is acknowledged that undertakings with no minimal substance may be set up in a Member State with the main objective of obtaining a tax advantage, notably by eroding the tax base of another Member State. While some Member States have developed a legislative or administrative framework to protect their tax base from such schemes, the relevant rules often have a limited effect, as they only apply in the

¹ OJ C , , p. .Not yet published in the Official Journal.

² OJ C , , p. .Not yet published in the Official Journal.

³ Council Directive 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (OJ L 193, 19.7.2016, p. 1).

⁴ Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC (OJ L 64, 11.3.2011, p. 1).

territory of a single Member State and do not effectively capture situations that involve more than one Member State. Furthermore, the national rules that apply in this field significantly differ across the Union while some Member States have no rules at all, to tackle the misuse of undertakings with no or minimal substance for tax purposes.

- (3) It is necessary to lay down a common framework, in order to strengthen Member States' resilience against practices of tax avoidance and evasion linked to the use of undertakings which do not perform an economic activity even if presumably they are engaged with economic activity and therefore do not have any or have only minimal substance for tax purposes. This is done in order to ensure that undertakings lacking minimal substance are not used as instruments of tax evasion or tax avoidance. As those undertakings may be established in one Member State but may be used with the effect of eroding the tax base of another Member State, it is critical to agree on a common set of rules for determining what should be considered as insufficient substance for tax purposes in the internal market as well as for delineating specific tax consequences linked to such insufficient substance. Where an undertaking has been found to have sufficient substance under this Directive, this should not prevent the Member States from continuing to operate anti-tax avoidance and evasion rules, provided that these are consistent with Union law.
- (4) To ensure a comprehensive approach, the rules should apply to all undertakings in the Union which are taxable in a Member State, regardless of their legal form and status, as long as they have their residence for tax purposes in a Member State and are eligible to obtain a certificate of tax residence in that Member State.
- (5) To ensure the proper functioning of the internal market, the proportionality and effectiveness of potential rules, it would be desirable to limit their scope to undertakings which are at risk of being found to lack minimal substance and used with the main objective of obtaining a tax advantage. It would therefore be important to establish a gateway criterion, in the form of a set of three cumulative, indicative conditions, in order to conclude which undertakings are sufficiently at risk as aforementioned to justify that they be subjected to reporting requirements. A first condition should enable the identification of undertakings presumably engaged mainly in geographically mobile economic activities, as the place where such activities are actually carried out is usually more challenging to identify. Such activities normally give rise to important passive income flows. Hence, undertakings, which income consists predominantly of passive income flows would meet this condition. It should also be taken into account that entities holding assets for private use, such as real estate, yachts, jets, artworks, or equity alone, may have no income for longer periods of time, but still enable significant tax benefits by way of owning those assets. As purely domestic situations would not pose a risk for the good functioning of the internal market and would be best addressed at domestic level, a second condition should focus on undertakings engaged in cross-border activities. Engagement in cross-border activities should be established having regard, on the one hand, to the nature of the transactions of the undertaking, domestic or foreign, and on the other, to its property, given that entities that only hold assets for private, non-business, use may not engage in transactions for a considerable time. Additionally, a third condition should point out to those undertakings which have no or inadequate own resources to perform core management activities. In this regard, undertakings that do not have adequate own resources tend to engage third party providers of administration, management, correspondence and legal compliance services or enter into relevant

agreements with associated enterprises for the supply of such services in order to set up and maintain a legal and tax presence. Outsourcing of certain ancillary services only, such as bookkeeping services alone, while core activities remain with the undertaking, would not suffice in itself for an undertaking to meet this condition. While such service providers might be regulated for other, non-tax purposes, their obligations for such other purposes cannot always mitigate the risk that they enable the set up and maintenance of undertakings misused for tax avoidance and evasion practices.

- (6) It would be fair to exclude from the envisaged rules undertakings whose activities are subject to an adequate level of transparency and therefore do not present a risk of lacking substance for tax purposes. Companies having a transferable security admitted to trading or listed on a regulated market or multilateral trading facility as well as certain financial undertakings which are heavily regulated in the Union, directly or indirectly, and subject to increased transparency requirements and supervision, should equally be excluded from the scope of this Directive. Pure holding undertakings which are situated in the same jurisdiction as the operational subsidiary and their beneficial owner(s) are not likely to serve the objective of obtaining a tax advantage either. Similar is the case of sub-holding undertakings which are situated in the same jurisdiction as their shareholder or ultimate parent entity. On this basis, they should also be excluded. Undertakings that engage an adequate number of persons, full-time and exclusively, in order to carry out their activities should equally not be considered to lack minimal substance. While they are not reasonably expected to pass the gateway criterion, they should be excluded explicitly for purposes of legal certainty.
- (7) To distinguish amongst undertakings which are at risk of being found to lack substance for tax purposes and ensure that the rules capture only undertakings that lack substance for tax purposes, undertakings should provide information on their resources in the Member State where they are resident for tax purposes. Such information is necessary to verify that the undertaking has resources and actually performs economic activity in the Member State of its tax residence and that there is sufficient nexus between the income or the assets of the undertaking and that Member State.
- (8) To facilitate implementation of this Directive, undertakings at risk of being found to lack substance and used with the main objective of obtaining a tax advantage should declare, in their annual tax return, that they possess a minimum level of resources such as people and premises in the Member State of tax residence and provide documentary evidence if that is the case. While it is recognised that different activities may require a different level or type of resources, a common minimum level of resources would be expected under all circumstances. This assessment should solely aim at identifying the substance of undertakings for tax purposes and does not question the role that “trust or company service providers”, as defined in Directive (EU) 2015/849 of the European Parliament and of the Council⁵, have in the identification of money laundering, its predicate offences and terrorist financing. Conversely, the absence of a minimum level of resources may be considered to indicate a lack of substance where an undertaking is

⁵ Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC (OJ L 141, 5.6.2015, p. 73).

already at risk of being found to lack substance for tax purposes. To ensure compatibility with relevant international standards, a common minimum level should draw on the existing Union and international standards on substantial economic activity in the context of preferential tax regimes or in the absence of corporate taxation⁶, as developed in the context of the Forum on Harmful Tax Practices. It is necessary to provide for submission of documentary evidence with the tax return in support of the declaration of the undertaking that it disposes a minimum of resources. It is also necessary in order to allow the administration to form a view based on the facts and circumstances of the undertaking and decide whether to initiate an audit procedure.

- (9) To ensure tax certainty, it is imperative to lay down common rules on the content of undertakings' declarations. Undertakings that pass the gateway criterion and are consequently subject to reporting requirements should be presumed not to have sufficient substance for tax purposes if they also declare not to possess one or more of the elements that cumulatively constitute a minimum level of substance, or do not provide the required supporting evidence. Undertakings that declare to possess all the elements of the minimum level of substance and provide the required supporting documentation should instead be presumed to have minimal substance for tax purposes and should incur no further obligations and consequences under this Directive. This, however, should be without prejudice to any applicable law and the right of the administration to perform an audit, including on the basis of the supporting documentation, and possibly, arrive at a different conclusion.
- (10) It is recognised that whether an undertaking is actually performing economic activities for tax purposes or serves mainly tax avoidance or evasion purposes is ultimately a matter of facts and circumstances. This should be assessed on a case by case basis in respect of each specific undertaking. Therefore, undertakings presumed not to have minimal substance for tax purposes should be entitled to prove the contrary, including to prove that they do not serve primarily tax objectives, and rebut such presumption. After fulfilling their reporting obligations under this Directive, they should provide additional information to the administration of the Member State where they reside for tax purposes. While they may provide any additional information that they deem appropriate, it is essential to set common requirements of what may constitute appropriate additional evidence and should thus be required in all cases. Where the Member State, based on such additional evidence, considers that an undertaking has rebutted a presumption of lack of substance in a satisfactory manner, it should be able to issue a decision to certify that the undertaking has minimal substance for tax purposes in accordance with this Directive. Such decision may remain valid for the period during which factual and legal circumstances of the undertaking remain unchanged and up to 6 years from the time the decision is issued. This will allow to limit the resources allocated to cases that have been evidenced not to be a shell for the purposes of the Directive.
- (11) As the objective of this Directive is to prevent tax avoidance and evasion that are likely to flourish through actions by undertakings without minimal substance, and in order to ensure tax certainty and enhance the proper functioning of the internal market,

⁶ General Secretariat of the Council, 9637/18 FISC 241 ECOFIN 555, Code of Conduct (Business Taxation), Guidance on the interpretation of the third criterion; OECD/G20 Base Erosion and Profit Shifting Project, Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5: Final Report

it is paramount to provide for a possibility of exemptions for undertakings which meet the gateway criterion but yet whose interposition has no actual advantageous impact on the overall tax position of the undertaking's group or of the beneficial owner(s). For that reason, such undertakings should be entitled to request the administration of the Member State, where they reside for tax purposes, to issue a decision which exempts them from complying with the proposed rules altogether and upfront. Such exemption should also be limited in time, to allow the administration to verify on a regular basis that the factual and legal circumstances justifying the exemption decision remain valid. At the same time a potential extended duration of such decision will allow to limit the resources allocated to cases that should be exempt from the scope of the Directive.

- (12) To ensure tax certainty and fair taxation in the internal market, it would be appropriate to explicitly lay down the rules that specify the treatment for tax purposes of income flowing to or from undertakings which have been found to lack minimum substance for tax purposes and have not provided evidence to the contrary or evidence that they do not serve the objective of obtaining a tax advantage. Such income should be taxable in the Member State where the undertaking's shareholder(s) reside for tax purposes, as if it were paid directly to such shareholder(s). To prevent the risk of double taxation, tax paid on such income in the Member State of the undertaking, if any, should be taken into account and deducted from the tax payable at the Member State of the undertaking's shareholder(s). If the undertaking's shareholders do not reside for tax purposes in a Member State, such income should be taxable in the jurisdiction of residence for tax purposes of the payer, as if it were paid straight to the undertaking's shareholder(s). Rules of equivalent effect should apply to situations where there are no income flows. In particular, this could occur in the case of holding immovable or other property of very high value for private purposes alone or of pure equity holdings. Considering that there is a risk that several undertakings without minimal substance are set up in a chain, it is also essential to exclude that the income is deemed taxable in the jurisdiction of a shareholder that is itself an undertaking without minimal substance. The allocation of taxing rights in accordance with agreements and conventions that provide for the elimination of double taxation of income, and where applicable, capital concluded between a Member State and a third country should not be affected by this Directive.
- (13) To ensure effectiveness of the proposed framework, it is necessary to establish appropriate tax consequences for undertakings that do not have minimal substance for tax purposes. Undertakings that have crossed the gateway criterion and are presumed to be lacking substance for tax purposes while, additionally, have not provided evidence to the contrary or evidence that they do not serve the objective of obtaining a tax advantage, should not be allowed to benefit from the provisions of agreements and conventions that provide for the elimination of double taxation of income, and where applicable, capital, to which the Member State of their tax residence is a party and from any other agreements, including provisions in international agreements for the promotion and protection of investments, with equivalent purpose or effect. Such undertakings should not be allowed to benefit from Council Directive 2011/96/EU⁷

⁷ Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (OJ L 345, 29.12.2011, p. 8).

and Council Directive 2003/49/EC⁸. To this effect, those undertakings should not be entitled to a certificate of tax residence to the extent that this serves to obtain those benefits. The Member State where the undertaking is resident for tax purposes should therefore deny to issue a certificate of tax residence. Alternatively, that Member State should be able to issue such certificate while indicating, by means of a warning, that it should not be used by the undertaking to obtain tax benefits as above. This denial of a certificate of tax residence, or alternatively the issue of a special certificate of tax residence, should not set aside the national rules of the Member State of the undertaking with regard to the tax residence and relevant obligations linked thereto. It would rather serve to communicate to other Member States, and third countries, that no relief or refund should be granted with regard to transactions involving this undertaking based on any treaty with the Member State of the undertaking or Union directives, if applicable.

- (14) Considering that undertakings without minimal substance may be used for the purpose of obtaining a tax advantage to the detriment of a Member State other than the one of their residence for tax purposes, the relevant information should be shared with the competent authorities of other Member States. To ensure that all interested Member States have timely access to such information, the information should be exchanged automatically through the common communication network ('CCN') developed by the Union. In this context, information should be recorded in a secure central directory on administrative cooperation in the field of taxation available to all Member States. Member States should be required to implement a series of practical arrangements, including measures to standardise the communication of all requisite information through the creation of a standard form. This should also involve specifying the linguistic requirements for the envisaged exchange of information and upgrading the CCN accordingly. Where necessary, following the stage of mandatory automatic exchange of information under this Directive, a Member State should be able to rely on Article 5 of Council Directive 2011/16/EU as regards the exchange of information on request to obtain additional information on reporting undertakings from the Member State to which such undertakings would be liable to have reported this information. Considering that the sooner replies to requests for information are received, the more effective they are, it is appropriate to ensure that replies to requests for information are provided swiftly.
- (15) Directive 2011/16/EU should therefore be amended accordingly.
- (16) In order to improve effectiveness, Member States should lay down penalties against the violation of the national rules that transpose this Directive. Such penalties should be effective, proportionate and dissuasive. To ensure tax certainty and a minimum level of coordination across all Member States, it is necessary to fix a minimum monetary penalty, also taking into account the situation of each specific undertaking. The envisaged rules rely on self-assessment by the undertakings as regards whether or not they meet the gateway criteria. To achieve effectiveness of the provisions, incentivising adequate compliance across the Union, and taking into account that a shell undertaking in one Member State may be used to erode the tax base of another Member State, it is important that any Member State has the right to request another Member State to conduct tax audits of undertakings at risk for not fulfilling minimum

⁸ Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States (OJ L 157, 26.6.2003, p. 49).

substance as defined in this Directive. Accordingly, to reinforce effectiveness, it is essential that the requested Member State has an obligation to carry out such audit and to share information on the outcome, even where there is no finding of ‘shell’ entity.

- (17) As the proper implementation and enforcement of the proposed rules in each Member State is critical for the protection of other Member States’ tax base, such implementation and enforcement should be monitored by the Commission. Member States should therefore communicate to the Commission on a regular basis, specific information, including statistics, on the implementation and enforcement in their territory of national measures adopted pursuant to this Directive.
- (18) In order to evaluate the effectiveness of the proposed new rules, the Commission should prepare an evaluation on the basis of the information provided by Member States and other available data. The Commission’s report should be published.
- (19) In order to ensure uniform conditions for the implementation of this Directive and Directive 2011/16/EU, in particular for the automatic exchange of information between tax authorities, implementing powers should be conferred on the Commission to adopt a standard form with a limited number of components, including the linguistic arrangements, the necessary practical arrangements for upgrading the central directory on administrative cooperation in the field of taxation. Those powers, as provided in the Directive 2011/16/EU, should be exercised in accordance with Regulation (EU) No 182/2011 of the European Parliament and of the Council⁹.
- (20) The European Data Protection Supervisor was consulted in accordance with Article 42 of Regulation (EU) 2018/1725 of the European Parliament and of the Council¹⁰.
- (21) Any processing of personal data carried out within the framework of Directive 2011/16/EU should comply with Regulation (EU) 2016/679 of the European Parliament and of the Council¹¹ and Regulation (EU) 2018/1725. Data processing is set out in Directive 2011/16/EU solely with the objective of serving a general public interest, namely the matters of taxation and the purposes of combating tax fraud, tax evasion and tax avoidance, safeguarding tax revenues and promoting fair taxation, which strengthen opportunities for social, political and economic inclusion in Member States.
- (22) Since the objective of this Directive cannot sufficiently be achieved by the Member States but can rather, by reason of the fact that such undertakings are normally established in one Member State but are used in a manner impacting the tax base of one or more other Member States, be better achieved at Union level, the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality

⁹ Regulation (EU) No 182/2011 of the European Parliament and of the Council of 16 February 2011 laying down the rules and general principles concerning mechanisms for control by Member States of the Commission’s exercise of implementing powers (OJ L 55, 28.2.2011, p. 13)

¹⁰ Regulation (EU) 2018/1725 of the European Parliament and of the Council of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data, and repealing Regulation (EC) No 45/2001 and Decision No 1247/2002/EC (OJ L 295, 21.11.2018, p. 39)

¹¹ Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) (OJ L 119, 4.5.2016, p. 1)

as set out in that Article, this Directive does not go beyond what is necessary in order to achieve that objective.

HAS ADOPTED THIS DIRECTIVE:

CHAPTER I GENERAL PROVISIONS

Article 1 Subject matter

This Directive 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.

Article 2 Scope

This Directive applies to all undertakings that are considered tax resident and are eligible to receive a tax residency certificate in a Member State.

This Directive is without prejudice to other legal acts of the Union.

Article 3 Definitions

For the purposes of this Directive the following definitions shall apply:

- (1) ‘undertaking’ means any entity engaged in an economic activity, regardless of its legal form, that is a tax resident in a Member State;
- (2) ‘tax year’ means a tax year, calendar year or any other appropriate period for tax purposes;
- (3) ‘revenues’ means the sum of the net turnover, other operating income, income from participating interests, including dividends received from affiliated undertakings, income from other investments and loans forming part of the fixed assets, other interest receivable and similar income as listed in Annexes V and VI to Directive 2013/34/EU of the European Parliament and of the Council¹²;
- (4) ‘Member State of the undertaking’ means the Member State where the undertaking is resident for tax purposes;
- (5) ‘beneficial owner’ means beneficial owner as defined in Article 3, point (6), of Directive (EU) 2015/849 of the European Parliament and of the Council;
- (6) ‘undertaking’s shareholders’ means the individuals or entities directly holding shares, interest, stakes, participations, membership rights, entitlement to benefits or any equivalent rights or entitlements in the undertaking and in the case of indirect holdings, those individuals or entities holding interest in the undertaking through one

¹² Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013, p. 19)

or a chain of undertakings none of which fulfils the indicators of minimum substance set out in Article 7(1) of this Directive.

Article 4 ***Relevant income***

For the purposes of Chapters II and III ‘relevant income’ shall mean income falling under any of the following categories:

- (a) interest or any other income generated from financial assets, including crypto assets, as defined in Article 3(1), point 2 of the proposal for a Regulation of the European Parliament and of the Council on Markets in Crypto-assets, and amending Directive (EU) 2019/1937¹³;
- (b) royalties or any other income generated from intellectual or intangible property or tradable permits;
- (c) dividends and income from the disposal of shares;
- (d) income from financial leasing;
- (e) income from immovable property;
- (f) income from movable property, other than cash, shares or securities, held for private purposes and with a book value of more than one million euro.
- (g) income from insurance, banking and other financial activities;
- (h) income from services which the undertaking has outsourced to other associated enterprises.

Article 5 ***Associated enterprise***

1. For the purposes of Articles 4 and 7, ‘associated enterprise’ shall mean a person who is related to another person in any of the following ways:
 - (a) a person participates in the management of another person by being in a position to exercise a significant influence over the other person;
 - (b) a person participates in the control of another person through a holding that exceeds 25 % of the voting rights;
 - (c) a person participates in the capital of another person through a right of ownership that, directly or indirectly, exceeds 25 % of the capital;
 - (d) a person is entitled to 25 % or more of the profits of another person.
2. If more than one person participates in the management, control, capital or profits of the same person, as referred to in paragraph 1, all persons concerned shall be regarded as associated enterprises.

If the same persons participate in the management, control, capital or profits of more than one person, as referred to in paragraph 1, all persons concerned shall be regarded as associated enterprises.

¹³ COM/2020/593 final

3. For the purposes of paragraphs 1 and 2, a person shall mean both legal and natural persons. A person who acts together with another person in respect of the voting rights or capital ownership of an entity shall be treated as holding a participation in all of the voting rights or capital ownership of that entity that are held by the other person.
4. In indirect participations, the fulfilment of the criteria set out in point (c) of paragraph 1 shall be determined by multiplying the rates of holding through the successive tiers. A person holding more than 50 % of the voting rights shall be deemed to hold 100 %.

An individual, his or her spouse and his or her lineal ascendants or descendants shall be treated as a single person.

CHAPTER II

IDENTIFICATION OF UNDERTAKINGS THAT DO NOT MEET INDICATORS OF MINIMUM SUBSTANCE FOR TAX PURPOSES

Article 6 *The reporting undertakings*

1. Member States shall require that undertakings meeting the following criteria to report to the competent authorities of Member States in accordance with Article 7:
 - (a) more than 75% of the revenues accruing to the undertaking in the preceding two tax years is relevant income;
 - (b) the undertaking is engaged in cross-border activity on any of the following grounds:
 - (i) more than 60% of the book value of the undertaking's 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) at least 60% of the undertaking's relevant income is earned or paid out via cross-border transactions;
 - (c) in the preceding two tax years, the undertaking outsourced the administration of day-to-day operations and the decision-making on significant functions.

An undertaking which holds assets that can generate income falling within the scope of Article 4, points (e) and (f), shall also be deemed to meet the criterion set out in point (a) of the first subparagraph, irrespective of whether income from these assets has accrued to the undertaking in the preceding two tax years, if the book value of these assets is more than 75% of the total book value of the undertaking's assets.

An undertaking which holds assets that can generate income falling within the scope of Article 4, point (c), shall also be deemed to meet the criterion set out in point (a) of the first subparagraph, irrespective of whether income from these assets has accrued to the undertaking in the preceding two tax years, if the book value of these assets is more than 75% of the total book value of the assets of the undertaking.

2. By derogation from paragraph 1, Member States shall ensure that the undertakings falling within any of the following categories are not subject to requirements of Article 7:

- (a) companies which have a transferable security admitted to trading or listed on a regulated market or multilateral trading facility as defined under Directive 2014/65/EU of the European Parliament and of the Council¹⁴;
- (b) regulated financial undertakings;
- (c) undertakings that have the main activity of holding shares in operational businesses in the same Member State while their beneficial owners are also resident for tax purposes in the same Member State;
- (d) undertakings with holding activities that are resident for tax purposes in the same Member State as the undertaking's shareholder(s) or the ultimate parent entity, as defined in Section I, point 7, of Annex III to Directive 2011/16/EU;
- (e) undertakings with at least five own full-time equivalent employees or members of staff exclusively carrying out the activities generating the relevant income;

Point (b) of the first subparagraph shall apply to the following 'regulated financial undertakings':

- (a) a credit institution as defined in Article 4(1), point (1), of Regulation (EU) No 575/2013 of the European Parliament and of the Council¹⁵;
- (b) an investment firm as defined in Article 4(1), point (1), of Directive 2014/65/EU of the European Parliament and of the Council¹⁶;
- (c) an alternative investment fund manager (AIFM) as defined in Article 4(1), point (b), of Directive 2011/61/EU of the European Parliament and of the Council (2), including a manager of Euveca under Regulation (EU) No 345/2013 of the European Parliament and of the Council¹⁷, a manager of Eusef under Regulation (EU) No 346/2013 of the European Parliament and of the Council¹⁸ and a manager of Eltif under Regulation (EU) 2015/760 of the European Parliament and of the Council¹⁹;

¹⁴ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349–496).

¹⁵ Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

¹⁶ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).

¹⁷ Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 on European venture capital funds (OJ L 115, 25.4.2013, p. 1).

¹⁸ Regulation (EU) No 346/2013 of the European Parliament and of the Council of 17 April 2013 on European social entrepreneurship funds (OJ L 115, 25.4.2013, p. 18).

¹⁹ Regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 on European long-term investment funds (OJ L 123, 19.5.2015, p. 98).

- (d) an undertaking for collective investment in transferable securities (UCITS) management company as defined Article 2(1), point (b), of Directive 2009/65/EC of the European Parliament and of the Council²⁰;
- (e) an insurance undertaking as defined in Article 13, point (1), of Directive 2009/138/EC of the European Parliament and of the Council²¹;
- (f) a reinsurance undertaking as defined in Article 13, point (4), of Directive 2009/138/EC;
- (g) an institution for occupational retirement provision as defined in Article 1, point (6) of Directive 2016/2341 of the European Parliament and of the Council²²;
- (h) pension institutions operating pension schemes which are considered to be social security schemes covered by Regulation (EC) No 883/2004 of the European Parliament and of the Council²³ and Regulation (EC) No 987/2009 of the European Parliament and of the Council²⁴ as well as any legal entity set up for the purpose of investment of such schemes;
- (i) an alternative investment fund (AIF) managed by an AIFM as defined in Article 4(1), point (b), of Directive 2011/61/EU or an AIF supervised under the applicable national law;
- (j) UCITS in the meaning of Article 1(2) of Directive 2009/65/EC;
- (k) a central counterparty as defined in Article 2, point (1), of Regulation (EU) No 648/2012 of the European Parliament and of the Council²⁵;
- (l) a central securities depository as defined in Article 2(1), point (1), of Regulation (EU) No 909/2014 of the European Parliament and of the Council²⁶;
- (m) an insurance or reinsurance special purpose vehicle authorised in accordance with Article 211 of Directive 2009/138/EC;

²⁰ Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 302, 17.11.2009, p. 32).

²¹ Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (OJ L 335, 17.12.2009, p. 1).

²² Directive (EU) 2016/2341 of the European Parliament and of the Council of 14 December 2016 on the activities and supervision of institutions for occupational retirement provision (IORPs) (OJ L 354, 23.12.2016, p. 37).

²³ Regulation (EC) No 883/2004 of the European Parliament and of the Council of 29 April 2004 on the coordination of social security systems (OJ L 166, 30.4.2004, p. 1).

²⁴ Regulation (EC) No 987/2009 of the European Parliament and of the Council of 16 September 2009 laying down the procedure for implementing Regulation (EC) No 883/2004 on the coordination of social security systems (OJ L 284, 30.10.2009, p. 1).

²⁵ Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (OJ L 201, 27.7.2012, p. 1).

²⁶ Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (OJ L 257, 28.8.2014, p. 1).

- (n) ‘securitisation special purpose entity’ as defined in Article 2, point (2), of Regulation (EU) No 2017/2402 of the European Parliament and of the Council²⁷;
- (o) an insurance holding company as defined in Article 212(1), point (f), of Directive 2009/138/EC or a mixed financial holding company as defined in Article 212(1), point (h), of Directive 2009/138/EC, which is part of an insurance group that is subject to supervision at the level of the group pursuant to Article 213 of that Directive and which is not exempted from group supervision pursuant to Article 214(2) of Directive 2009/138/EC;
- (p) a payment institution as defined in point (d) of Article 1(1) of Directive (EU) 2015/2366 of the European Parliament and of the Council²⁸;
- (q) an electronic money institution as defined in point (1) of Article 2 of Directive 2009/110/EC of the European Parliament and of the Council²⁹;
- (r) a crowdfunding service provider as defined in point (e) Article 2(1) of Regulation (EU) 2020/1503 of the European Parliament and of the Council³⁰;
- (s) a crypto-asset service provider as defined in Article 3(1), point (8), of [the proposal for a Regulation of the European Parliament and of the Council on Markets in Crypto-assets, and amending Directive (EU) 2019/1937³¹] where performing one or more crypto-asset services as defined in Article 3(1), point (9), of [the proposal for a Regulation of the European Parliament and of the Council on Markets in Crypto-assets, and amending Directive (EU) 2019/1937].

Article 7

Indicators of minimum substance for tax purposes

1. Member States shall require that undertakings meeting the criteria laid down in Article 6(1) declare in their annual tax return, for each tax year, whether they meet the following indicators of minimum substance:
 - (a) the undertaking has own premises in the Member State, or premises for its exclusive use;
 - (b) the undertaking has at least one own and active bank account in the Union;

²⁷ Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012 (OJ L 347, 28.12.2017, p. 35).

²⁸ Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC (OJ L 337, 23.12.2015, p. 35)

²⁹ Directive 2009/110/EC of the European Parliament and of the Council of 16 September 2009 on the taking up, pursuit and prudential supervision of the business of electronic money institutions amending Directives 2005/60/EC and 2006/48/EC and repealing Directive 2000/46/EC (OJ L 267, 10.10.2009, p. 7)

³⁰ Regulation (EU) 2020/1503 of the European Parliament and of the Council of 7 October 2020 on European crowdfunding service providers for business, and amending Regulation (EU) 2017/1129 and Directive (EU) 2019/1937 (OJ L 347, 20.10.2020, p. 1)

³¹ COM/2020/593 final

- (c) one of the following indicators:
 - (i) One or more directors of the undertaking:
 - (1) are resident for tax purposes in the Member State of the undertaking, or at no greater distance from that Member State insofar as such distance is compatible with the proper performance of their duties;
 - (2) are qualified and authorised to take decisions in relation to the activities that generate relevant income for the undertaking or in relation to the undertaking's assets;
 - (3) actively and independently use the authorisation referred to in point (2) on a regular basis;
 - (4) are not employees of an enterprise that is not an associated enterprise and do not perform the function of director or equivalent of other enterprises that are not associated enterprises;
 - (ii) the majority of the full-time equivalent employees of the undertaking are resident for tax purposes in the Member State of the undertaking, or at no greater distance from that Member States insofar as such distance is compatible with the proper performance of their duties, and such employees are qualified to carry out the activities that generate relevant income for the undertaking.
2. Undertakings referred to in paragraph 1 shall accompany their tax return declaration with documentary evidence. The documentary evidence shall include the following information:
- (a) address and type of premises;
 - (b) amount of gross revenue and type thereof;
 - (c) amount of business expenses and type thereof;
 - (d) type of business activities performed to generate the relevant income;
 - (e) the number of directors, their qualifications, authorisations and place of residence for tax purposes or the number of full-time equivalent employees performing the business activities that generate the relevant income and their qualifications, their place of residence for tax purposes;
 - (f) outsourced business activities;
 - (g) bank account number, any mandates granted to access the bank account and to use or issue payment instructions and evidence of the account's activity.

Article 8

Presumption of minimum substance for tax purposes

1. An undertaking that declares to meet all the indicators of minimum substance set out in Article 7(1) and provides the satisfactory supporting documentary evidence in accordance with Article 7(2) shall be presumed to have minimum substance for the tax year.
2. An undertaking that declares not to meet one or more of the indicators set out in Article 7(1) or does not provide satisfactory supporting documentary evidence in

accordance with Article 7(2) shall be presumed not to have minimum substance for the tax year.

Article 9

Rebuttal of the presumption

1. Member States shall take the appropriate measures to allow undertakings that are presumed not to have minimum substance under Article 8(2) to rebut this presumption by providing any additional supporting evidence of the business activities which they perform to generate relevant income.
2. For the purposes of paragraph 1, undertakings shall provide the following additional evidence:
 - (a) a document allowing to ascertain the commercial rationale behind the establishment of the undertaking;
 - (b) information about the employee profiles, including the level of their experience, their decision-making power in the overall organisation, role and position in the organisation chart, the type of their employment contract, their qualifications and duration of employment;
 - (c) concrete evidence that decision-making concerning the activity generating the relevant income is taking place in the Member State of the undertaking.
3. A Member State shall treat an undertaking as having rebutted the presumption if the evidence that the undertaking has provided under paragraph 2 proves that the undertaking has performed and continuously had control over, and borne the risks of, the business activities that generated the relevant income or, in the absence of income, the undertaking's assets.
4. After the end of the tax year for which the undertaking rebutted the presumption successfully, in accordance with paragraph 3, a Member State may consider for a period of five years that the undertaking has rebutted the presumption on the condition that the factual and legal circumstances of the undertaking remain unchanged during this period.

Article 10

Exemption

1. A Member State shall take the appropriate measures to allow an undertaking that meets the criteria laid down in Article 6(1) to request an exemption from its obligations under this Directive if the existence of the undertaking does not reduce the tax liability of its beneficial owner(s) or of the group, as a whole, of which the undertaking is a member.
2. A Member State may grant that exemption for one tax year if the undertaking provides sufficient and objective evidence that its interposition does not lead to a tax benefit for its beneficial owner(s) or the group as a whole, as the case may be. That evidence shall include information about the structure of the group and its activities. That evidence shall allow to compare the amount of overall tax due by the beneficial owner(s) or the group as a whole, as the case may be, having regard to the interposition of the undertaking, with the amount that would be due under the same circumstances in the absence of the undertaking.

3. After the end of the tax year for which an exemption was granted in accordance with paragraph 2, a Member State may extend the validity of the exemption for five years on the condition that the factual and legal circumstances of the undertaking, including of the beneficial owner(s) and the group, as the case may be, remain unchanged in the relevant period.

CHAPTER III

TAX TREATMENT OF UNDERTAKINGS THAT DO NOT HAVE MINIMUM SUBSTANCE FOR TAX PURPOSES

Article 11

Tax consequences of not having minimum substance for tax purposes in Member States other than the Member State of the undertaking

1. Member States other than the Member State of the undertaking shall disregard any agreements and conventions that provide for the elimination of double taxation of income, and where applicable, capital, in force with the Member State of the undertaking as well as Articles 4, 5 and 6 of Directive 2011/96/EU and Article 1 of Directive 2003/49/EC, to the extent that those Directives apply due to the undertaking being deemed to be resident for tax purposes in a Member State, where the following conditions are met:
 - (a) an undertaking is presumed not to have minimum substance;
 - (b) an undertaking does not rebut the presumption referred to in point (a) for a tax year.
2. The Member State of the undertaking's shareholder(s) shall tax the relevant income of the undertaking in accordance with its national law as if it had directly accrued to the undertaking's shareholder(s) and deduct any tax paid on such income at the Member State of the undertaking, where the following conditions are met:
 - (a) the relevant income accrues to an undertaking that is presumed not to have minimum substance;
 - (b) the undertaking does not rebut the presumption referred to in point (a);
 - (c) both the undertaking's shareholders and the payer are resident for tax purposes in a Member State.

The first subparagraph shall apply notwithstanding any agreement or convention that provides for the elimination of double taxation of income, and where applicable, capital, in force with another Member State.

Where the payer is not resident for tax purposes in a Member State, the Member State of the undertaking's shareholder(s) shall tax the relevant income accruing to the undertaking in accordance with its national law as if it had directly accrued to the undertaking's shareholder(s), without prejudice to any agreement or convention that provides for the elimination of double taxation of income, and where applicable, capital, in force between the Member State of the undertaking's shareholders and the third country jurisdiction of the payer;

Where the undertaking's shareholder(s) is not resident for tax purposes in a Member State, the Member State of the payer of this income shall apply withholding tax in

accordance with its national law, without prejudice to any agreement or convention that provides for the elimination of double taxation of income, and where applicable, capital, in force with the third country jurisdiction of the undertaking's shareholder(s).

3. Where property referred to in Article 4 is owned by an undertaking that is presumed not to have minimum substance and does not rebut this presumption:
 - (a) the Member State where property referred to in Article 4, point (e) is situated shall tax such property according to its national law, as if such property was owned directly by the undertaking's shareholder(s), without prejudice to any agreement or convention that provides for the elimination of double taxation of income, and where applicable, capital, in force with the jurisdiction of the undertaking's shareholder(s);
 - (b) the Member State of the undertaking's shareholder(s) shall tax such property in accordance with its national law as if the undertaking's shareholder(s) owned it directly, without prejudice to any agreement or convention that provides for the elimination of double taxation of income, and where applicable, capital, in force with the jurisdiction where the property is situated.

Article 12

Tax consequences of not having minimum substance for tax purposes in the Member State of the undertaking

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 shall take any of the following decisions:

- (a) deny a request for a certificate of tax residence to the undertaking for use outside the jurisdiction of this Member State;
- (b) grant a certificate of tax residence which prescribes 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, and of international agreements with a similar purpose or effect and of Articles 4, 5 and 6 of Directive 2011/96/EU and Article 1 of Directive 2003/49/EC.

CHAPTER IV EXCHANGE OF INFORMATION

Article 13

Amendments to Directive 2011/16/EU

Directive 2011/16/EU is amended as follows:

- (1) in Article 3, point 9 is amended as follows:
 - (a) point (a) is replaced by the following:

“(a) for the purposes of Article 8(1) and Articles 8a to 8ad, the systematic communication of predefined information to another Member State, without prior request, at pre-established regular intervals; for the

purposes of Article 8(1), reference to available information relates to information in the tax files of the Member State communicating the information, which is retrievable in accordance with the procedures for gathering and processing information in that Member State;”

(b) point (c) is replaced by the following:

“(c) for the purposes of provisions of this Directive other than Article 8(1) and (3a) and Articles 8a to 8ad, the systematic communication of predefined information provided in points (a) and (b) of this point.”

(2) In Section II of Chapter II, the following Article 8ad is added:

“Article 8ad

Scope and conditions of mandatory automatic exchange of information on undertakings required to report on indicators of minimum substance

1. The competent authority of a Member State, which receives information from an undertaking established in its territory in accordance with Article 7 of Council Directive [OP] (insert full title and OJ reference)* shall, by means of automatic exchange, and within 30 days from receipt of that information, communicate such information to the competent authorities of all other Member States in accordance with paragraph 4 and applicable practical arrangements adopted pursuant to Article 21.
2. The competent authority of a Member State, which certifies that an undertaking has rebutted the presumption in accordance with Article 9 of Directive [OP] or that an undertaking is exempt in accordance with Article 10 of that Directive shall, by means of automatic exchange, and within 30 days from such certification, communicate such information to the competent authorities of all other Member States, in accordance with applicable practical arrangements adopted pursuant to Article 21.
3. The competent authority of a Member State, which concludes including by way of an audit, under the national law of such Member State, that an undertaking does not meet the indicators of minimum substance laid down in Article 7 of Directive [OP] shall, by means of automatic exchange, and within 30 days from the date when the outcome of the audit becomes definitive, communicate such information to the competent authorities of all other Member States, in accordance with applicable practical arrangements adopted pursuant to Article 21.
4. The information to be communicated by a competent authority of a Member State pursuant to paragraph 1 regarding each undertaking shall include the following:
 - (a) the tax identification number (TIN) of the undertaking required to report pursuant to Article 6 of Directive [OP];
 - (b) the VAT number, where available, of the undertaking required to report pursuant to Article 6 of Directive [OP];
 - (c) the identification of the undertaking’s shareholders and the beneficial owner(s) of the undertaking, as defined in Article 3, points 5 and 6;
 - (d) the identification of the other Member States, if any, likely to be concerned by the reporting of the undertaking;
 - (e) the identification of any person in the other Member States likely to be affected by the reporting of the undertaking;

- (f) the declaration provided by the undertaking, in accordance with Article 7(1);
 - (g) summary of the evidence provided by the undertaking in accordance with Article 7(2).
5. Without prejudice to paragraph 4, the information to be communicated by a competent authority of a Member State pursuant to paragraph 2 shall also include the following:
- (h) the certification by the competent authority of the Member State that the undertaking has rebutted the presumption under Article 9 of Directive [OP] or that the undertaking is exempt from reporting in accordance with Article 10 of that Directive;
 - (i) a summary of the additional evidence considered relevant by the competent authority to issuing the certification that the presumption has been rebutted under Article 9 of Directive [OP] or that the undertaking is exempt from reporting under Article 10 of that Directive.
6. Without prejudice to paragraph 4, the information to be communicated by a competent authority of a Member State pursuant to paragraph 3 shall also include the audit report where such report is issued by the competent authority.
7. To facilitate the exchange of information referred to in paragraphs 4, 5 and 6, the Commission shall, by means of implementing acts, adopt the practical arrangements necessary for the implementation of paragraphs 1 to 6 of this Article, including measures to standardise the communication of the information set out in paragraphs 4, 5 and 6 of this Article. Those implementing acts shall be adopted in accordance with the examination procedure referred to in Article 26(2).
8. For the purposes of paragraphs 1 to 5 of this Article, ‘undertaking’ shall mean undertaking as defined in Article 3, point (1) of Directive [OP].
9. Information processed shall be retained for 5 years and in any case no longer than necessary to achieve the purposes of this Directive.
10. Competent authorities of each Member State shall be considered to be data controllers and the Commission shall be considered to be data processor.
11. Member States in the event of an unauthorised disclosure of information referred to in points (a) – (f) of paragraph 4 may decide to suspend, as a mitigating measure, the exchanges of information under this Directive with the Member State where the unauthorised disclosure occurred.”
- (3) in Article 20, paragraph 5 is replaced by the following:
- “5. The Commission shall, by means of implementing acts, adopt standard forms, including the linguistic arrangements, in the following cases:
- (a) for the automatic exchange of information on advance cross-border rulings and advance pricing arrangements pursuant to Article 8a before 1 January 2017;
 - (b) for the automatic exchange of information on reportable cross-border arrangements pursuant to Article 8ab before 30 June 2019;
 - (c) for the automatic exchange of information on undertakings required to report on indicators of minimum substance pursuant to Article 8ad before 1 January 2024.

Those implementing acts shall be adopted in accordance with the examination procedure referred to in Article 26(2).

Those standard forms shall not exceed the components for the exchange of information listed in Article 8a(6), Article 8ab(14) and Article 8ad(4), (5) and (6), and such other related fields which are linked to these components which are necessary to achieve the objectives of Articles 8a, 8ab and 8ac, respectively.

The linguistic arrangements referred to in the first subparagraph shall not preclude Member States from communicating the information referred to in Articles 8a, 8ab and 8ad in any of the official languages of the Union. However, those linguistic arrangements may provide that the key elements of such information shall also be sent in another official language of the Union.”;

(4) in Article 21, paragraph 5 is replaced by the following:

“5. The Commission shall by 31 December 2017 develop and provide with technical and logistical support a secure Member State central directory on administrative cooperation in the field of taxation where information to be communicated in the framework of Article 8a(1) and (2) shall be recorded in order to satisfy the automatic exchange provided for in those paragraphs.

The Commission shall by 31 December 2019 develop and provide with technical and logistical support a secure Member State central directory on administrative cooperation in the field of taxation where information to be communicated in the framework of Article 8ab(13), (14) and (16) shall be recorded in order to satisfy the automatic exchange provided for in those paragraphs.

The Commission shall by 30 June 2024 develop and provide with technical and logistical support a secure Member State central directory on administrative cooperation in the field of taxation where information to be communicated in the framework of Article 8ad(1), (2) and (3) shall be recorded in order to satisfy the automatic exchange provided for in those paragraphs.

The competent authorities of all Member States shall have access to the information recorded in that directory. The Commission shall also have access to the information recorded in that directory, however within the limitations set out in Articles 8a(8) and 8ab(17). The Commission shall, by means of implementing acts, adopt the necessary practical arrangements for the implementation of the first, second and third subparagraph of this paragraph. Those implementing acts shall be adopted in accordance with the examination procedure referred to in Article 26(2).

Until that secure central directory is operational, the automatic exchange provided for in Article 8a(1) and (2), Article 8ab(13), (14) and (16) and Article 8ad(1), (2) and (3) shall be carried out in accordance with paragraph 1 of this Article and the applicable practical arrangements.”.

CHAPTER V ENFORCEMENT

Article 14 **Penalties**

Member States shall lay down the rules on penalties applicable to infringements of national provisions adopted pursuant to this Directive, and shall take all measures necessary to ensure that they are implemented. The penalties provided for shall be effective, proportionate and dissuasive.

Member States shall ensure that those penalties include an administrative pecuniary sanction of at least 5% of the undertaking's turnover in the relevant tax year, if the undertaking that is required to report pursuant to Article 6 does not comply with such requirement for a tax year within the prescribed deadline or makes a false declaration in the tax return under Article 7.

Article 15 **Request for tax audits**

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 request the competent authority of the latter to conduct a tax audit of the undertaking.

The competent authority of the requested Member State shall initiate it within one month from the date of receipt of the request and conduct the tax audit, in accordance with the rules governing tax audits in the requested Member State.

The competent authority which conducted the tax audit shall provide feedback on the outcome of such audit to the competent authority of the requesting Member State as soon as possible and no later than one month after the outcome of the tax audit is known.

Article 16 **Monitoring**

1. Member States shall communicate the following information to the Commission for each tax year:
 - (a) number of undertakings that meet the conditions laid down in Article 6(1);
 - (b) number of undertakings that reported pursuant to Article 7;
 - (c) penalties imposed pursuant to Article 14 for non-compliance with the requirements of this Directive;
 - (d) number of undertakings presumed not have minimum substance in accordance with Article 8 and number of undertakings that rebutted such presumption in accordance with Article 9;
 - (e) number of undertakings exempt from the requirements under this Directive in accordance with Article 10;
 - (f) number of audits to undertakings that meet the conditions laid down in Article 6(1),

- (g) number of cases where an undertaking presumed to have minimum substance was found not to have substantial activity, in particular following an audit;
- (h) number of requests for exchange of information submitted and number of requests received;
- (i) number of requests for tax audits submitted and number of requests received.

Member States shall communicate to the Commission any other information necessary for monitoring and evaluating the implementation of this Directive upon request by the Commission.

2. Member States shall communicate the information listed in paragraph 1 on a bi-annual basis by 31 December of the tax year following the end of the bi-annual period.

Article 17

Reports

1. By 31 December 2028, the Commission shall present a report to the European Parliament and the Council on the implementation of this Directive.
2. When drawing up the report, the Commission shall take into account the information communicated by the Member States pursuant to Article 15.
3. The Commission shall publish the report on its website.

CHAPTER VI FINAL PROVISIONS

Article 18

Transposition

1. Member States shall adopt and publish, by [30 June 2023] at the latest, the laws, regulations and administrative provisions necessary to comply with this Directive. They shall forthwith communicate to the Commission the text of those provisions.

They shall apply those provisions from [1 January 2024].

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

1. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 19

Entry into force

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Article 20
Addressees

This Directive is addressed to the Member States.

Done at Brussels,

For the Council
The President

LEGISLATIVE FINANCIAL STATEMENT

1. FRAMEWORK OF THE PROPOSAL/INITIATIVE

1.1. Title of the proposal/initiative

UNSHELL

1.2. Policy area(s) concerned

Tax policy.

1.3. The proposal/initiative relates to:

a new action

a new action following a pilot project/preparatory action¹

the extension of an existing action

a merger or redirection of one or more actions towards another/a new action

1.4. Objective(s)

1.4.1. General objective(s)

The Proposal seeks to reduce tax revenue loss related to tax avoidance and tax evasion due to the use of shell entities in the EU. Furthermore, the Proposal will allow Member States to accurately describe and quantify the extent of shell entity tax abuse in the EU. Ultimately, the Proposal should further discourage the creation of shell entities in the EU.

1.4.2. Specific objective(s)

Specific objectives

1) Identification of shell entities in the EU at risk of tax abuse through the use of objective substance criteria. Once a shell entity has been identified as risk of tax abuse, the Proposal will set out clear, pre-determined, common tax consequences throughout the EU in order to prevent tax losses;

2) Competent Authorities of Members States should have information available to be able to identify shell entities in resident/established in other Member States so that they can prevent cross-border tax abuse, for example, by denying tax treaty benefits on withholding taxes;

3) The Proposal aims to discourage the use of TCSP's from creating shell entities in the EU in the first place. The substance criteria identified in 1) above are designed to combat the very services that TCSP's offer, like setting up postal addresses, that TCSP's provide to shell entities.

1.4.3. Expected result(s) and impact

Entities targeted will have to report to tax administrations whether or not they fulfil minimum substance indicators. There will be tax consequences for entities not fulfilling those indicators.

¹ As referred to in Article 58(2)(a) or (b) of the Financial Regulation.

1.4.4. Indicators of performance

Specify the indicators for monitoring progress and achievements.

Objectives	Indicators	Measurement tools/data sources
The use of common substance criteria to identify shell entities to prevent tax revenue loss due to tax evasion and tax avoidance.	Additional tax revenues secured thanks to the initiative preventing shell entities from obtaining a tax benefit at national or cross-border level.	Yearly assessment of automatic exchange of information (source: Member States' tax administrations)
Providing information to Member States to identify shell entities used for tax abuse purposes.	Number of shell exchanges made and compliance activities of Member States.	Data to be submitted on an annual basis by Member States to the Commission for monitoring purposes (source: Member States' tax administrations)
Deterrent effect on TCSP's creating shell entities in the EU.	Qualitative assessment by Member States of the impact of the initiative on deterring TCSP's from offering services to set up shell entities.	Yearly assessment of automatic exchange of information (source: Member States' tax administrations)

1.5. Grounds for the proposal/initiative

1.5.1. Requirement(s) to be met in the short or long term including a detailed timeline for roll-out of the implementation of the initiative

Legal entities and arrangements which are required to report under the Proposal will self-assess using the substance criteria to determine whether they are at risk of tax abuse. Information on entities and arrangements which are required to self-assess in a Member States will be automatically with the Competent Authorities of other Member States. In this context, the Competent Authorities will be required to submit the disclosed information to a Central Directory which all Member States will have access to. The Commission will be given limited access to the Directory in order to ensure that it can be sufficiently informed to monitor the functioning of the Directive. The Proposal will use the practical arrangements currently under the Directive 2011/16/EU on Administrative Cooperation in Direct Taxation (the 'DAC').

In terms of timing from setting up other Central Directories for tax exchanges purpose, like DAC3 and DAC6, Member States and the Commission would require at least 18 months after the adoption of the Proposal to be able to put the systems in place to allow the exchange of information to occur between Member States. Implementation with a start up period is expected from January, 2024.

- 1.5.2. *Added value of Union involvement (it may result from different factors, e.g. coordination gains, legal certainty, greater effectiveness or complementarities). For the purposes of this point 'added value of Union involvement' is the value resulting from Union intervention which is additional to the value that would have been otherwise created by Member States alone.*

The Proposal does not seek to replace existing national and international rules to combat shell entity tax abuse in the EU. Instead, the Proposal aims to reinforce and complement existing measures by providing objective substance criteria to prevent tax abuse in a cross-border context. Having uniform rules would ensure consistency of substance requirements for tax purposes in the EU as well as on the countermeasures to be applied including tax consequences and sanctions for non-compliance.

For group companies across the EU there would be economies of scale as only one set of substance rules would need to be applied. This would then ensure a level playing field and fair competition for businesses in the EU.

- 1.5.3. *Lessons learned from similar experiences in the past*

The initiative is a new mechanism. The preferred option in the Impact Assessment draws on the approach the EU follows in assessing substance in relevant third countries as part of the process leading to the establishment and update of the EU list of non-cooperative jurisdictions for tax purposes. It aims at replicating some of the features of this process.

- 1.5.4. *Compatibility with the Multiannual Financial Framework and possible synergies with other appropriate instruments*

In the Commission Communication on Business Taxation in the 21st Century, the Commission committed to table a legislative proposal setting out union rules to neutralise the misuse of shell entities for tax purposes by the end of 2021. The Proposal will use the procedures, arrangements and IT tools already established or under development under the DAC.

- 1.5.5. *Assessment of the different available financing options, including scope for redeployment*

Implementation costs for the initiative will be financed by the EU budget concerning only the central components for the system of automatic exchange of information. Otherwise, it will be for Member States to implement the measures envisaged.

1.6. Duration and financial impact of the proposal/initiative

limited duration

- in effect from [DD/MM]YYYY to [DD/MM]YYYY
- Financial impact from YYYY to YYYY for commitment appropriations and from YYYY to YYYY for payment appropriations.

unlimited duration

- Implementation with a start-up period from YYYY to YYYY,
- followed by full-scale operation.

1.7. Management mode(s) planned²

Direct management by the Commission

- by its departments, including by its staff in the Union delegations;
- by the executive agencies

Shared management with the Member States

Indirect management by entrusting budget implementation tasks to:

- third countries or the bodies they have designated;
- international organisations and their agencies (to be specified);
- the EIB and the European Investment Fund;
- bodies referred to in Articles 70 and 71 of the Financial Regulation;
- public law bodies;
- bodies governed by private law with a public service mission to the extent that they are provided with adequate financial guarantees;
- bodies governed by the private law of a Member State that are entrusted with the implementation of a public-private partnership and that are provided with adequate financial guarantees;
- persons entrusted with the implementation of specific actions in the CFSP pursuant to Title V of the TEU, and identified in the relevant basic act.

Comments

This proposal builds on the existing framework and systems for the automatic exchange of information using a Central Directory for advance cross-border rulings ('DAC3') and reportable cross-border tax arrangements ('DAC6') which were developed pursuant to Article 21 of Directive 2011/16/EU in the context of these previous amendments to the DAC. The Commission, in conjunction with Member States, shall develop standardised forms and formats for information exchange through implementing measures. As regards the CCN network which will permit the exchange of information between Member States, the Commission is responsible for the development of such a network and Member States will

² Details of management modes and references to the Financial Regulation may be found on the BudgWeb site:
<https://myintracomm.ec.europa.eu/budgweb/EN/man/budgmanag/Pages/budgmanag.aspx>

undertake to create the appropriate domestic infrastructure that will enable the exchange of information via the CCN network.

2. MANAGEMENT MEASURES

2.1. Monitoring and reporting rules

The Commission will ensure that arrangements are in place to monitor and evaluate the functioning of the intervention and evaluate it against the main policy objectives. Given that “Unshell” involves a modification to the DAC, monitoring and evaluation could be carried out in alignment with the other elements of administrative cooperation.

Member States will submit data on an annual basis to the Commission for the information outlined in the above Table on indicators of performance which will be used to monitor compliance with the Proposal.

As monitoring data is available, the Commission will review the scope of the intervention to examine the possibility of extending it to cover additional sectors and/or revising some its features.

An evaluation will take place five years after the implementation of the Proposal which will allow the Commission to review the results of the policy with respect to its objectives as well as the overall impacts in terms of tax revenue, businesses and the internal market.

2.2. Management and control system(s)

2.2.1. Justification of the management mode(s), the funding implementation mechanism(s), the payment modalities and the control strategy proposed

The implementation of the initiative will rely on the competent authorities (tax administrations) of the Member States. They will be responsible for financing their own national systems and adaptations necessary for the exchanges to take place with the Central Directory to be set up for the purposes of Proposal.

The Commission will set up the infrastructure, including the Central Directory, that will allow exchanges to be made between Member States on the identification of shell entities. IT systems have been set up for the DAC which will be used for this initiative. The Commission will finance the systems needed to allow exchanges to take place, including the Central Directory, which will undergo the main elements of control being that for procurement contracts, technical verification of the procurement, ex-ante verification of commitments, and ex-ante verification of payments.

2.2.2. Information concerning the risks identified and the internal control system(s) set up to mitigate them

The proposed intervention will be based on a declarative system, which entails the risk of non-declaration or misdeclaration by legal entities and arrangements that are required to self-assess against the substance criteria under the Proposal. Member States will be required to audit such self-assessments and report to the Commission on an annual basis statistics including the number of entities that have been audited and sanctions for non-compliance.

In order to address the risk of non-compliance of legal entities and arrangements, the Proposal includes a sanctioning framework. National tax authorities will be in charge of enforcing sanctions and more generally of ensuring compliance with “Unshell”. Sanctions are set up at a sufficiently high level to serve as deterrent. Furthermore, national tax administrations will be able to perform audits to detect and deter non-compliance.

To monitor the proper application of the Proposal, the Commission will have limited access to the Central Directory where Member States will exchange information on entities and arrangements reporting under the Proposal.

The main elements of the control strategy are:

Procurement contracts

The control procedures for procurement defined in the Financial Regulation: any procurement contract is established following the established procedure of verification by the services of the Commission for payment, taking into account contractual obligations and sound financial and general management. Anti-fraud measures (controls, reports, etc.) are foreseen in all contracts concluded between the Commission and the beneficiaries. Detailed terms of reference are drafted and form the basis of each specific contract. The acceptance process follows strictly the TAXUD TEMPO methodology: deliverables are reviewed, amended if necessary and finally explicitly accepted (or rejected). No invoice can be paid without an "acceptance letter".

Technical verification of procurement

DG TAXUD performs controls of deliverables and supervises operations and services carried out by contractors. It also conducts quality and security audits of their contractors on a regular basis. Quality audits verify the compliance of the contractors' actual processes against the rules and procedures defined in their quality plans. Security audits focus on the specific processes, procedures and set-up.

In addition to the above controls, DG TAXUD performs the traditional financial controls:

Ex-ante verification of commitments

All commitments in DG TAXUD are verified by the Head of the Finances and the HR business correspondent Unit. Consequently, 100% of the committed amounts are covered by the ex-ante verification. This procedure gives a high level of assurance as to the legality and regularity of transactions.

Ex-ante verification of payments

100% of payments are verified ex-ante. Moreover, at least one payment (from all categories of expenditures) per week is randomly selected for additional ex-ante verification performed by the head of the Finances and HR business correspondent Unit. There is no target concerning the coverage, as the purpose of this verification is to check payments "randomly" in order to verify that all payments were prepared in line with the requirements. The remaining payments are processed according to the rules in force on a daily basis.

Declarations of the Authorising Officers by Sub-Delegations (AOSD)

All the AOSD sign declarations supporting the Annual Activity Report for the year concerned. These declarations cover the operations under the programme. The

AOSD declare that the operations connected with the implementation of the budget have been executed in accordance with the principles of the sound financial management, that the management and control systems in place provided satisfactory assurance concerning the legality and regularity of the transactions and that the risks associated to these operations have been properly identified, reported and that mitigating actions have been implemented.

- 2.2.3. *Estimation and justification of the cost-effectiveness of the controls (ratio of "control costs ÷ value of the related funds managed"), and assessment of the expected levels of risk of error (at payment & at closure)*

The controls established enable DG TAXUD to have sufficient assurance of the quality and regularity of the expenditure and to reduce the risk of non-compliance. The above control strategy measures reduce the potential risks below the target of 2% and reach all beneficiaries. Any additional measures for further risk reduction would result in disproportionately high costs and are therefore not envisaged. The overall costs linked to implementing the above control strategy – for all expenditures under Fiscalis programme – are limited to 1.6% of the total payments made. It is expected to remain at the same ratio for this initiative. The programme control strategy limits the risk of non-compliance to virtually zero and remains proportionate to the risks entailed.

2.3. **Measures to prevent fraud and irregularities**

Specify existing or envisaged prevention and protection measures, e.g. from the Anti-Fraud Strategy.

The European Anti-fraud Office (OLAF) may carry out investigations, including on-the-spot checks and inspections, in accordance with the provisions and procedures laid down in Regulation (EC) No 1073/1999 of the European Parliament and of the Council³ and Council Regulation (Euratom, EC) No 2185/96⁴ with a view to establishing whether there has been fraud, corruption or any other illegal activity affecting the financial interests of the Union in connection with a grant agreement or grant decision or a contract funded under this Regulation.

³ Regulation (EC) No 1073/1999 of the European Parliament and of the Council of 25 May 1999 concerning investigations conducted by the European Anti-Fraud Office (OLAF), OJ L 136 p. 1, 31.5.1999.

⁴ Council Regulation (Euratom, EC) No 2185/96 of 11 November 1996 concerning on-the-spot checks and inspections carried out by the Commission in order to protect the European Communities' financial interests against fraud and other irregularities, OJ L 292 p. 2, 15.11.96.

3. ESTIMATED FINANCIAL IMPACT OF THE PROPOSAL/INITIATIVE

3.1. Heading(s) of the multiannual financial framework and expenditure budget line(s) affected

- Existing budget lines

In order of multiannual financial framework headings and budget lines.

Heading of multiannual financial framework	Budget line	Type of expenditure	Contribution			
			from EFTA countries ²	from candidate countries ³	from third countries	within the meaning of Article 21(2)(b) of the Financial Regulation
	14.03.01	Diff./Non-diff. ¹				
	Improving the proper functioning of the tax systems	Diff./Non-diff.	NO	NO	NO	NO

- New budget lines requested

In order of multiannual financial framework headings and budget lines.

Heading of multiannual financial framework	Budget line	Type of expenditure	Contribution			
			from EFTA countries	from candidate countries	from third countries	within the meaning of Article 21(2)(b) of the Financial Regulation
	Number	Diff				
	N/A	Diff.	NO	NO	NO	NO

¹ Diff. = Differentiated appropriations / Non-diff. = Non-differentiated appropriations.

² EFTA: European Free Trade Association.

³ Candidate countries and, where applicable, potential candidates from the Western Balkans.

3.2. Estimated financial impact of the proposal on appropriations

3.2.1. Summary of estimated impact on operational appropriations

- The proposal/initiative does not require the use of operational appropriations
- The proposal/initiative requires the use of operational appropriations, as explained below:

EUR million (to three decimal places)

Heading of multiannual financial framework	Number	14.03.01
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DG: TAXUD			2022	2023	2024	2025	2026	2027	TOTAL
• Operational appropriations									
Budget line 14.03.01	Commitments	(1a)	0.680	0.082	0.082	0.082	0.082	0.082	1.088
	Payments	(2a)		0.680	0.082	0.082	0.082	0.082	1.008
TOTAL appropriations for DG TAXUD	Commitments	=1a+1b +3	0.680	0.082	0.082	0.082	0.082	0.082	1.088
	Payments	=2a+2b +3		0.680	0.082	0.082	0.082	0.082	1.008

Heading of multiannual financial framework	7	‘Administrative expenditure’
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This section should be filled in using the 'budget data of an administrative nature' to be firstly introduced in the [Annex to the Legislative Financial Statement](#) (Annex V to the internal rules), which is uploaded to DECIDE for interservice consultation purposes.

EUR million (to three decimal places): Current Prices

2023	2024	2025	2026	2027	TOTAL
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							2021 -2027 MFF
DG: TAXUD							
• Human resources		0.300	0.036	0.036	0.036	0.036	0.444
• Other administrative expenditure – Missions		0.020	0.002	0.002	0.002	0.002	0.028
TOTAL DG TAXUD	Appropriations	0.320	0.038	0.038	0.038	0.038	0.472

TOTAL appropriations under HEADING 7 of the multiannual financial framework	(Total commitments = Total payments)	0.320	0.038	0.038	0.038	0.038	0.472
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EUR million (to three decimal places): Current Prices

		2023	2024	2025	2026	2027	TOTAL 2021 – 2027 MFF
TOTAL appropriations under HEADINGS 1 to 7 of the multiannual financial framework	Commitments	1	0.120	0.120	0.120	0.120	1.480
	Payments	0.320	0.718	0.120	0.120	0.120	1.398

3.2.2. Summary of estimated impact on administrative appropriations

- The proposal/initiative does not require the use of appropriations of an administrative nature
- The proposal/initiative requires the use of appropriations of an administrative nature, as explained below:

EUR million (to three decimal places)

	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027	Year 2028	Year 2029	TOTAL
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HEADING 7 of the multiannual financial framework								
Human resources	0.300	0.036	0.036	0.036	0.036	0.036	0.036	0.516
Other administrative expenditure	0.020	0.002	0.002	0.002	0.002	0.002	0.002	0.032
Subtotal HEADING 7 of the multiannual financial framework	0.320	0.038	0.038	0.038	0.038	0.038	0.038	0.548

Outside HEADING 7¹ of the multiannual financial framework								
Human resources								
Other expenditure of an administrative nature								
Subtotal outside HEADING 7 of the multiannual financial framework								

TOTAL	0.320	0.038	0.038	0.038	0.038	0.038	0.038	0.548
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The appropriations required for human resources and other expenditure of an administrative nature will be met by appropriations from the DG that are already assigned to management of the action and/or have been redeployed within the DG, together if necessary with any additional allocation which may be granted to the managing DG under the annual allocation procedure and in the light of budgetary constraints.

¹ Technical and/or administrative assistance and expenditure in support of the implementation of EU programmes and/or actions (former 'BA' lines), indirect research, direct research.

3.2.2.1. Estimated requirements of human resources

- The proposal/initiative does not require the use of human resources.
- The proposal/initiative requires the use of human resources, as explained below:

Estimate to be expressed in full time equivalent units

	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027	Year 2028	Total
• Establishment plan posts (officials and temporary staff)							
20 01 02 01 (Headquarters and Commission's Representation Offices)	1	1	0.4	0.2	0.1	0.1	2.8
20 01 02 03 (Delegations)							
01 01 01 01 (Indirect research)							
01 01 01 11 (Direct research)							
Other budget lines (specify)							
• External staff (in Full Time Equivalent unit: FTE)¹							
20 02 01 (AC, END, INT from the 'global envelope')							
20 02 03 (AC, AL, END, INT and JPD in the delegations)							
XX 01 xx yy zz ²	- at Headquarters						
	- in Delegations						
01 01 01 02 (AC, END, INT - Indirect research)							
01 01 01 12 (AC, END, INT - Direct research)							
Other budget lines (specify)							
TOTAL	1	1	0.4	0.2	0.1	0.1	2.8

XX is the policy area or budget title concerned.

The human resources required will be met by staff from the DG who are already assigned to management of the action and/or have been redeployed within the DG, together if necessary with any additional allocation which may be granted to the managing DG under the annual allocation procedure and in the light of budgetary constraints.

Description of tasks to be carried out:

Officials and temporary staff	Preparation of meetings and correspondence with Member States, work on forms, IT formats and the Central Directory.
External staff	N/A

¹ AC= Contract Staff; AL = Local Staff; END= Seconded National Expert; INT = agency staff; JPD= Junior Professionals in Delegations.

² Sub-ceiling for external staff covered by operational appropriations (former 'BA' lines).

3.2.3. *Compatibility with the current multiannual financial framework*

The proposal/initiative:

- can be fully financed through redeployment within the relevant heading of the Multiannual Financial Framework (MFF).

- requires use of the unallocated margin under the relevant heading of the MFF and/or use of the special instruments as defined in the MFF Regulation.

Explain what is required, specifying the headings and budget lines concerned, the corresponding amounts, and the instruments proposed to be used.

- requires a revision of the MFF.

Explain what is required, specifying the headings and budget lines concerned and the corresponding amounts.

3.2.4. *Third-party contributions*

The proposal/initiative:

- does not provide for co-financing by third parties
- provides for the co-financing by third parties estimated below:

Appropriations in EUR million (to three decimal places)

	Year N ¹	Year N+1	Year N+2	Year N+3	Enter as many years as necessary to show the duration of the impact (see point 1.6)			Total
Specify the co-financing body								
TOTAL appropriations co-financed								

¹ Year N is the year in which implementation of the proposal/initiative starts. Please replace "N" by the expected first year of implementation (for instance: 2021). The same for the following years.

3.3. Estimated impact on revenue

- The proposal/initiative has no financial impact on revenue.
- The proposal/initiative has the following financial impact:
 - on own resources
 - on other revenue
 - please indicate, if the revenue is assigned to expenditure lines

EUR million (to three decimal places)

Budget revenue line:	Appropriations available for the current financial year	Impact of the proposal/initiative ²							
		Year N	Year N+1	Year N+2	Year N+3	Enter as many years as necessary to show the duration of the impact (see point 1.6)			
Article									

For assigned revenue, specify the budget expenditure line(s) affected.

Other remarks (e.g. method/formula used for calculating the impact on revenue or any other information).

² As regards traditional own resources (customs duties, sugar levies), the amounts indicated must be net amounts, i.e. gross amounts after deduction of 20 % for collection costs.