

The European Commission's Unshell Proposal: Substantive or Not?

by Roland Meuwissen



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In this article, Meuwissen examines the European Commission's Unshell proposal aimed at curbing misuse of shell companies, points out some inconsistencies in its wording, and compares its substance requirements with those of Dutch tax law.

On December 22, 2021, the European Commission published its proposal for a council directive (COM(2021) 565 final) to prevent the misuse of shell companies in the EU (the Unshell proposal, also known as ATAD 3 (the third anti-tax-avoidance directive)). The directive seems to be aimed at countries like the Netherlands, Luxembourg, and Ireland, which have been recognized as countries with a high amount of foreign direct investment, which is connected to tax avoidance.¹

The Unshell proposal attempts to combat tax avoidance and evasion by denying companies that do not have sufficient substance in their countries of tax residency the benefits of the parent-subsidiary directive (2011/96/EU) and the interest and royalty directive (2003/49/EC) and precluding

the application of tax treaties for those companies. In fact, the proposal goes beyond that and orders member states to levy tax as if those shell companies do not exist, while taking the potential risk of double taxation for granted. Further, shell companies must provide information to the tax authorities of their countries of tax residency, which will then be exchanged with other EU tax authorities.

Comparing this proposal with earlier directives, it stands out as much more aggressive by requiring that shell companies be fully disregarded and providing a minimum penalty for noncompliance.

Although announced in May 2021, the Unshell proposal follows in the wake of the European Commission's proposal for a directive to implement the OECD's pillar 2 in the EU. Pillar 2 applies only to multinational groups with consolidated revenue exceeding €750 million, leaving a significant gap in combating tax avoidance by multinationals with less revenue and in situations not involving corporate groups.

The Unshell proposal still needs to be voted on by the EU Council, and I expect it to be discussed in the next Economic and Financial Affairs Council meeting on April 5. Given the directive's far-reaching consequences, it is unclear whether the commission will be able to obtain 27 votes in its favor. On the other hand, at first glance the substance requirements can be met relatively easily, so countries that have experience in that area might think the directive needs more stringent rules. Further, because the substance requirements are not overly harsh, the proposal truly targets shell companies.

This article examines the Unshell proposal and compares its substance requirements with those in the Netherlands.

¹ See Ivana Kienzl Krišto and Elodie Thirion, "An Overview of Shell Companies in the European Union," European Parliamentary Research Service Study PE 627.129 (Oct. 2018); and Jannick Damgaard, Thomas Elkjaer, and Niels Johannesen, "Phantom Investments," *Fin. & Dev.* 11 (Sept. 2019).