Comments on Commission Proposal for a council directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU

German insurers welcome the important step forward that the European Commission has taken in the fight against the misuse of shell entities with this proposal.

Nonetheless, we would like to take the opportunity of this consultation to draw your attention to a few aspects of the draft which we think should be further examined.

1. Risk case criteria in Art. 6 par. 1

Art. 6 par. 1 defines the circumstances in which an undertaking is seen as a risk case. One criterion used is outsourcing. We agree that outsourcing of certain functions may be an indicator for lack of substance. However, where outsourcing is used for a tax avoidance scheme, activities are typically outsourced to parties resident in another jurisdiction. However, it is a different matter, if activities are outsourced to a related group company within the same jurisdiction. In these cases, outsourcing generally does not give rise to tax avoidance risks since the group as a whole has substance in the jurisdiction. Therefore, the outsourcing criterion in Art. 6 par. 1 (c) should be more closely tailored to tax avoidance schemes. Alternatively, it should be made clear that where outsourced activities are performed within the jurisdiction of the undertaking, the presumption of lack of substance may be rebutted under Art. 9 or an exemption under Art. 10 may be granted.

Furthermore, an absolute de-minimis threshold for the amount of relevant income in Art. 6 (1) may be considered. The 60 % and 75 % thresholds in the proposal operate relative to the revenues, relevant income or the book value of assets. Therefore, minimal amounts could trigger the reporting operations absent a de-minimis threshold.

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2. Operation of exemption

According to Art. 10, an undertaking may obtain an exemption from the obligations of the directive where there is no risk of tax avoidance. The wording of the proposal is somewhat unclear as to the order of the process of obtaining such an exemption in relation to the reporting obligation for the substance test under Art. 7. Since the substance test may be burdensome, the holders of an exemption should not have to report on their substance. Therefore, the process for the application of the exemption under Art. 10 should be available before the substance test reporting obligations kick in.

3. Double taxation of shell entity income

Art 11 par. 2 provides that the income of an undertaking that fails to show minimum substance is treated as if it had been directly accrued to the undertaking's shareholder(s). Therefore, one would expect that a subsequent distribution of same income is consequently disregarded. Instead, Art. 11 par. 1 of the directive aims to ensure that a distribution would not benefit from any tax exemption granted by a double tax convention or the parent-subsidiary directive. Taxing the distribution of income that has already been taxed in the hands of the shareholder(s) would, in our perspective, lead to an unjustified double taxation. Therefore, it should instead be considered to include a provision, whereby a distribution of income that has been treated as accrued to the undertakings shareholder(s) under Art. 11 par. 2 is tax exempt in the amount of the income accrued to the shareholder(s). Logically, the same should apply to capital gains resulting from the sale of the shares in the shell entity. Furthermore, the wording of Art. 11 par. 2 which deals with the deductibility of tax (*"tax paid on such income at the Member State of the undertaking")* should be rephrased. The wording should be such that it covers tax on the income of the undertaking as well as withholding tax on a distribution by the shell entity to its shareholder(s). Both taxes should be creditable against the tax liability of the shareholder since a tax liability on the shell entity´s income arises in the hands of the shareholder(s). At least, income tax of the shell entity and withholding tax should be made deductible. However, through a mere deduction of the tax as opposed to a credit double taxation cannot be completely avoided.

4. Harmonisation of substance requirements

Under Art. 11 and 12 of the proposal only a negative substance test outcome, i.e. the assessment by the Member State of residence that an undertaking lacks minimum substance, has an EU wide binding effect. However, a taxpayer in the EU is confronted with many different substance requirements by the Member States. For example, a company which receives dividend payments originating from several Member States may have to

comply with differing substance requirements per Member State leading to multiple filing of different documents to the fiscal authorities in the respective Member States. Therefore, from the taxpayer's point of view, it would be helpful if all EU Member States would recognize the approval of sufficient substance by the fiscal authorities of the Member State of residence and not only where the fiscal authorities have come to the conclusion that an undertaking lacks minimum substance. Not establishing such obligation for EU Member States would be a missed opportunity to improve the Single Market.