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THE UNSHELL DIRECTIVE PROPOSAL: GATEAWAYS COMPABILITY WITH THE FREEDOM OF ESTABLISHMENT

Bachelor's thesis

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I hereby declare that I have compiled the thesis independently
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The document length is 9697 words from the introduction to the end of the conclusion.

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(date)

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ABSTRACT

The European Union has implemented multiple initiatives to tackle tax evasion by multinational enterprises and encourage equitable tax practices. The Unshell Directive is a proposed measure to prevent the misuse of shell entities for tax purposes by standardizing the assessment criteria and processes to identify such entities.

The paper focuses the need for such a measure, the proposed rules, and the impact of the Unshell Directive on companies with structures in multiple jurisdictions. The paper explores two key aspects: whether the Unshell Directive brings concerns that a large number of structures not established for the purpose of using shell companies to avoid tax will be caught by the provisions, and whether the Unshell Directive's general criteria lead to a presumption of abuse compatible with the European Court of Justice regarding the freedom of establishment.

The results, based on the EU legislation, guidelines, literature, and the European Court of Justice case law reflect that there are some unclarities regarding Unshell Directive gateway criteria. The Proposal provide general criteria leading to a presumption of abuse might be seen as incompatible with European Court of Justice case law regarding the freedom of establishment regardless of the rebuttal provisions included in the Proposal since it seems resulting from the European Court of Justice case law that such general presumptions of abuse are not allowed.

Keywords: The unshell directive proposal, ATAD, anti-tax avoidance, freedom of establishment, EU law

LIST OF ABBREVIATIONS

ATAD 1	Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market
BEPS	Base Erosion and Profit Shifting ()
CFC	Controlled foreign company
CJEU	European Court of Justice
DAC	Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC
DTT	Double taxation treaty
EU	European Union
European Commission	The Commission
MS	Member State
OECD	The Organization for Economic Cooperation and Development
Parent-Subridiary Directive	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
Royalties Directives	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
SAAR	Special anti-abuse rule
TFEU	Treaty on the Functioning of the European Union
Unshell Directive	Proposal for a Council Directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive COM(2021) 565

INTRODUCTION

The European Union's (EU) approach to anti-avoidance is based on the principle of ensuring that all taxpayers pay their fair share of tax, regardless of the jurisdiction in which they operate. The EU has taken several measures to combat tax avoidance by multinational corporations and promote fair taxation practices. One of the key measures in this area is the Anti-Tax Avoidance Directive (ATAD), which was adopted by the EU in 2016 and subsequently amended in 2017 and 2018. In the past year, there has been a significant shift in the context for EU business taxation policy by the most drastic economic crisis in the EU history due pandemic. The new Unshell Directive aims to prevent shell entity misuse for tax purposes by standardizing the assessment criteria and processes to identify shell entities through a substance test, and by coordinating their tax treatment among Member States (MSs).

To understand the topic, it is appropriate to define shell company. Assume that Estonian OÜ carries out business in Lithuania without having a permanent establishment in Lithuania thus pays 20% corporate income tax on its profits. The tax is deferred until the profits are distributed, but still 20% tax applies. This is one of the reasons why individuals and businesses may start considering ways to reduce their tax burden. One way to do that is to establish a Lithuanian company that falls under the Lithuanian small companies' tax regime, having 5% CIT on its profits. It is accounted on an annual basis and is not deferred unlike in Estonia, but still 5%. And no additional tax in Estonia when LT subsidiary distributes profits to EE due to Parent-Subsidiary Directive and § 50 (1)' of the Estonian Income Tax Act.[1] If that LT company does not have any actual substance, establishing it can fall under abusive approach. Unshell should tacke such shelf companies. However, it is important to note that not all holding companies are shell companies, and there may be legitimate reasons for using a holding company structure. The number of shell companies in the EU and the corresponding impact of shell companies on the EU economy cannot be determined from the data available.[2]

Although significant progress has been made in this area over the past few years, particularly with the adoption of the anti-tax avoidance directive (ATAD) and the expansion of scope of the

[1] 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. 8-16.*, Art. 4; Income Tax Act RT I, 15.12.1999, 101, 903; OECD. (2022). *OECD Tax Policy Reviews: Lithuania 2022*, OECD Tax Policy Reviews, OECD Publishing, Paris, https://doi.org/10.1787/53952224-en

[2] Krišto I. K., Thirion E. (2018). *An overview of shell companies in the Europe*. European Parliament.

directive on administrative cooperation (DAC)[3], legal entities without the substance and economic activity still pose a risk of being used for improper tax purposes, such as tax evasion and avoidance. Recognizing that there can be valid reasons for the use of such entities, there is also 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 conditions 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.[4]

In order to advance a strong, effective, and fair business tax system in the EU, the European Commission approved a Communication on Business Taxation for the 21st rury on May 18, 2021. It lays out both a long-term and short-term vision and strives to establish a fair and secure business climate that can support the Union's sustainable and job-rich growth. One of the targeted, short-term actions announced in the Communication to enhance the present tax system with a focus on ensuring fair and effective taxation is the Unshell Directive Proposal.[5] Tax avoidance has wider implications beyond financial loss for tax authorities. It undermines critical communal spaces that are essential for the effective functioning of regulatory compliance, organizational integrity, and society as a whole.[6]

Proposal for a Council Directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU also knowns as ATAD 3 (The Proposal), would require undertakings to report information that would enable the respective competent authority to assess in the respective jurisdiction whether the undertaking has a real and substantial presence and an economic activity. In case of absence of a real and substantial presence and an economic activity, benefits to which companies are entitled under.[7]

This thesis aims to assess the compatibility of the Unshell Directive proposal with the EU's fundamental right of freedom of establishment, particularly with regards to companies with

[3] Krišto I. K., Thirion E. (2018)., *supra nota 2*, p. 6
[4] Proposal for a Council Directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive COM(2021) 565 final, p. 1
[5] *Ibid.*
[6] Bird R., Davis-Nozemack K. (2018). Tax Avoidance as a Sustainability Problem. *Journal of Business Ethics*, Vol. 151, No. 4, Special Issue on Leadership and the Creation of Corporate Social Responsibility, pp. 1009-1025
[7] COM(2021) 565 final, *supra nota 4*, p. 19

structures in multiple jurisdictions. To answer the key research question of does this Proposal infringes the freedom of establishment? The thesis focuses on two specific aspects: (a) What are the criteria used in the Unshell Directive's gateway filtering system and how do the criteria affect companies with structures in multiple jurisdictions? And (b) what are the relevant rulings of the CJEU regarding the freedom of establishment in the EU, and how do these rulings impact the Unshell Directive? The thesis follows the qualitative research method by systematising and interpreting the relevant EU law, scientific publications in the field and European court of justice (CJEU) case law which may influence the interpretation of the Unshell directive.

To find the answer to the main research question, the thesis is structured into three chapters. Purpose of the first chapter is to find out and analyse how the new Unshell Directive’s gateway criteria is filtering system is working and the specific rules it creates. The second chapter analyses whether the Unshell Directive is in line with the freedom of establishment which is one on the fundamental freedoms in EU. The freedom of establishment enables companies to operate and establish themselves within the EU without discrimination or undue restrictions, but any limitations must be based on legitimate public interest objectives, necessary to achieve those objectives, and proportionate to the aim pursued. Sub-chapters will provide an analysis to the TFEU and its impact on direct taxation, requirements of the EU Primary Law with respect to competences and assess the Unshell Directive considering these requirements. The chapter overall analyses whether the provisions of the Directive unfairly target companies that have legitimate business reasons for having structures in multiple jurisdictions, thereby potentially limiting their ability to establish themselves in different EU MS. Finally, the chapter analysis the relevant rulings of the Court of Justice of the European Union (CJEU) since it has played a significant role in interpreting and enforcing principle of freedom of establishment and has issued several important rulings regarding it.

1. THE UNSHELL DIRECTIVE

1.1. The Limits of the European Union's Taxation Policy Framework

The EU has a comprehensive tax policy framework that is designed to promote fiscal stability, fair competition, and economic growth among its MSs.[8] The EU does not have the authority to set tax rates for individual MSs. However, the EU can establish certain rules and directives that set a minimum threshold for tax rates or establish certain tax policies. The minimum 15% corporate income tax (CIT) requirement from the minimum tax directive is an example of such a policy.[9] As a topic the taxation policy of the European Union is complex. Its key elements which are indirect taxation and direct taxation. But what are the limits?

Indirect taxation, such as value-added tax (VAT) and excise duties, is an area where the EU has significant authority to harmonize and coordinate policies among MSs. This is because variations in indirect taxation rates and systems can distort competition in the single market and create an unfair advantage for businesses operating in certain countries. The EU has established a VAT system that ensures that goods and services are taxed in a consistent manner across MSs and has also harmonized excise duties on products such as alcohol, tobacco, and energy.[10]

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. Direct taxation, such as income tax and corporate tax, remains the responsibility of individual MSs. The EU does not have the authority to harmonize or set these tax rates.[11] On July 12, 2016, the Council of the European Union adopted the ATAD 1 Council Directive (EU) 2016/1164 as an answer to The Organization for Economic

[8] European Commission, Directorate-General for Taxation and Customs Union, A fair share : taxation in the EU for the 21st century, Publications Office, 2018, https://data.europa.eu/doi/10.2778/848353
[9] COM(2021) 565 final, *supra nota 4*, p. 9
[10] Lasok, K. (2005). Indirect taxation. Eu*ropean Business Law Review*, 16(3), 519-532.
[11] Kaye, T. A. (2012). Direct taxation in the european union: from maastricht to lisbon. *Fordham International Law Journal*, 35(5), 1231-1259.

Cooperation and Development (OECD) Base Erosion and Profit Shifting (BEPS) project delivered in 2015.[12] Directives and Regulations appear to have proper legal nature that allow for the introduction of EU-wide anti-tax avoidance measures while the recommendations and opinions do not have the binding force and the decision is not suitable either due to its normative constraint to only bind those to whom it is addressed.[13] 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.

EU has tried to introduce direct tax measures limits was well tested by the "windfall tax". The windfall tax regulation was introduced last year for energy company's profits they earned due to higher energy prices cause by the Ukraine war. The tax or "solidarity contribution" in EU-speak was called a contribution of similar but is direct tax in its nature. The solidarity contribution will apply in addition to regular domestic taxes and levies.[14] For example, the U.S. oil giant ExxonMobil has filed a lawsuit against the European Commission's (the Commission) proposal through subsidiaries in Germany and the Netherlands, seeking to levy excess profits from European Union-based oil and gas firms at the CJEU. The argument made is that the measure constitutes a tax, which is a right exclusively reserved for national governments. Additionally, the use of Article 122 of the EU Treaty, an emergency procedure that excludes the European Parliament, to enact the legislation is being contested.[15]

Without going in depth to EU tax policy framework next chapters will provide the general overview of the Unshell Directive proposal including its background and main causes, legal basis, scope, and the specific rules which it sets.

[12] Dourado, Ana Paula. (2016). The EU Anti Tax Avoidance Package: Moving Ahead of BEPS? 44(6/7), *Intertax*, 440 – 446. https://doi.org/10.54648/taxi2016036
[13] Craig, P., De Burca, G. (2020). EU Law, Texts, Cases and Materials. Seventh Edition. Oxford University Press. p. 153
[14] Proposal for a Council Regulation on an emergency intervention to address high energy prices COM(2022) 473 final
[15] Action brought, 28.12.2022, ExxonMobil Producing Netherlands and Mobil Erdgas-Erdöl v Council, Case T-802/22 (2023/C 54/27)

1.2. Purpose of EU anti-abuse rules

Tax avoidance is a concern that affects all countries and it is important to distinguish avoidance from other concepts. Avoidance is not evasion. Evasion means dishonestly reporting one's income. For example, a cash business may understate its takings or fail to file any tax return at all. Avoidance is also not mitigation. Mitigation generally means in the present context, reducing one's tax in ways that a governing statute clearly encourages or permits; for example, taking a deduction for a gift to charity. Avoidance falls between evasion and mitigation, encompassing the creation of transactions, usually artificial, to reduce tax that would otherwise be payable under the policy of the relevant tax provision.[16]

It is easy to get the impression that tax planning and tax avoidance is so prevalent in the countries with developed national economies that tax avoidance always has been or has become acceptable behaviour. As mentioned before, judicial sanction of tax planning, however, has not been free from restrictions.[17] The Anti-Tax Avoidance Directive aims to create a minimum level of protection against corporate tax avoidance throughout the EU, while ensuring a fairer and more stable environment for businesses.[18] However, shell entities, or entities that are capable of being used for tax avoidance or evasion but actually perform no actual economic activity, are not expressly targeted by any provisions in the existing tax instruments at the EU level. Recent tax-related scandals have brought to light the risk that such entities may pose for the Single Market and particularly for the tax bases of MSs.[19] Various types of shell entities are used by tax evaders and are frequently layered in an intricate network which covers the identity of beneficial owners.[20]

On December 22, 2021, the Commission issued a proposal for a Directive aimed at fighting the use of shell entities and arrangements for tax purposes. The proposal comes in the form of amendments to Council Directive 2016/1164/EU – the EU Anti-Tax Avoidance Directive (ATAD) and to Council Directive 2011/16 on administrative cooperation in the field of taxation

[16] Prebble, R., & Prebble, J. (2010). Does the use of general anti-avoidance rules to combat tax avoidance breach principles of the rule of law a comparative study. Saint Louis *University Law Journal*, 55(1), 21-46.
[17] Ordower, H. (2010). The culture of tax avoidance. *Saint Louis University Law Journal*, 55(1), 50.
[18] Council Directive (EU) 2016/1164 of laying down rules against tax avoidance practices that directly affect the functioning of the internal market, (Anti Tax Avoidance Directive), *OJ L 193, 12.7.2016, Art. 3*
[19] COM(2021) 565 final, *supra nota 4*, p. 2
[20] Pacini C., Wadlinger N. (2018). *How shell entities and lack of ownership transparency facilitate tax evasion and modern policy responses to these problems.* Vol. 102, Issue 1. Marquette Law Review. pp. 111-166

(DAC). The proposed new measures will establish transparency standards around the use of shell entities, so that their abuse can more easily be detected by tax authorities. Using several objective indicators related to income, staff and premises, the proposal will help national tax authorities detect entities that exist merely on paper. The Unshell directive requires unanimity in the European Council for its adoption, following the consultation with the European Parliament. Once adopted as a Directive, it should be transposed into MS's national law by 30 June 2023 and come into effect as of 1 January 2024.[21] Next chapters will provide analysis of

1.4. Placement in the anti-abuse rule hierarchy

ATAD 1 requires EU MSs to introduce the GAAR as part of their domestic tax law. GAAR is a legislative provision aimed at preventing abusive tax practices that exploit gaps or mismatches in tax rules across different jurisdictions. While the GAAR provisions in ATAD 1 aim to prevent abusive tax practices, they are not specifically targeted at addressing the issue of profit shifting, which is a key concern addressed by the Proposal. However, the Proposal may contain similar provisions to the GAAR to prevent abusive tax practices, as part of its broader efforts to create a more transparent and fairer corporate tax environment in the EU.[22] Due to an amendment of the Parent-Subsidiary Directive, the EU MSs must include a 'common minimum anti-abuse rule' in their legislation for circumstances that fall under the Parent-Subsidiary Directive which makes it the first time that it has become obligatory to incorporate a GAAR in the tax legislation of the EU Member States. [23]

By requiring companies to have a genuine economic link to the MS where they claim tax benefits, the Proposal reinforces, for example, the anti-abuse provisions of the Parent-Subsidiary Directive (PSD). The PSD aims to prevent double taxation of profits distributed between companies that are part of the same corporate group. Specifically, it allows for the elimination of withholding taxes on dividends paid by subsidiaries to their parent companies located in other EU MSs. If a company is deemed a shell company, it will not be able to access tax relief and the benefits of the tax treaty

[21] Pacini C., Wadlinger N. (2018), *supra nota 21*, p. 111.166
[22] Council Directive (EU) 2016/1164, *supra nota 18,* Art. 11
[23] Weber, D. (2016). New common minimum anti-abuse rule in the eu parent-subsidiary directive: background, impact, applicability, purpose and effect. *Intertax,* 44(2), 98-129.

network of its MS and/or to qualify for the treatment under the Parent-Subsidiary and Interest and Royalties Directives.[24]

The Unshell Directive applies to all undertakings that are considered tax resident and are eligible to receive a tax residency certificate in a MS. It applies to all entities and legal arrangements that are tax residents in the EU, without any revenue threshold. The directive specifically targets arrangements where undertakings are set up within the EU but do not conduct any real economic activity and are only used to obtain tax advantages for their beneficial owner or group.[25] On the other hand, the legal framework on the minimum level of taxation applies only to Multinational Enterprise 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.[26] The ATAD is a minimum directive (de minimis approach), offering multiple options for MSs. This means that MSs are obliged to ensure the level of protection as described in the directive and cannot offer less restrictive rules. Consequently, MSs are allowed to apply more restrictive rules (article 3).[27] Therefore, the ATAD includes only general provisions that give MSs the discretion to implement the directive in a manner that aligns with their corporate tax systems.

1.5. A seven-step Approach

1.5.1. Undertakings that should report

The first step is undertakings that should report (chapter II, article 6). It divides the various types of undertakings in those at risk for lacking substance and be misused for tax purposes versus those at low risk. Low-risk cases that do not cross the gateway are irrelevant for the purposes of the Directive. Only the undertakings considered at risk at the first step proceed to the second step, which is the core of the substance test itself. As a result, resources can be focused on the riskiest cases, i.e., those that existent all relevant features and consequently cross the gateway.[28]

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[24] Council Directive (EU) 2016/1164 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (recast) (Parent-Subsidiary Directive), *OJ L 345, 30.11.2011, p. 8–16*
[25] Popa Oana. (2022). Proposal for an EU Directive Laying Down Rules to Prevent the Misuse of Shell Entities for Tax Purposes (Unshell): Seven Steps towards Disgrace or Redemption. European Taxation.
[26] COM(2021) 565 final, *supra nota 4,* p. 2
[27] Council Directive (EU) 2016/1164, *supra nota 18,* Art. 3
[28] COM(2021) 565 final, *supra nota 4,* p. 9

Risk cases are those that existent simultaneously several features usually identified in undertakings that lack substance. 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, professional third-party service providers or equivalents. These criteria are commonly referred to as 'gateway'. Low-risk cases are those that present none or only a few of these criteria than those that do not pass the gateways.[29]

For tax certainty, certain activities are excluded from the Unshell Directive because they are considered low-risk and not relevant to the Directive. These activities include undertakings that would not qualify for the Directive or, if they did, they would be found to be irrelevant at a later stage of the test. For example, for listed entities, specific regulated financial entities, certain holding entities of operational businesses in the same MS and entities with at least five own full-time equivalent employees exclusively carrying out the activities generating the relevant income. Undertakings that fall under these exclusions do not need to go through the initial qualifying step. Only undertakings considered at risk during this step move on to the second step, which is the substance test itself.[30]

However, the proposed regulation will have a significant impact at least on the international investment structures of investment industry players. The proposed regulation may cause challenges in the investment structures of such operators, and it is possible that some of the companies in the investment structures will be considered shell companies in the future, which will be denied tax benefits.[31]

1.5.2. Reporting

The second step is possibility of gaining exemption from reporting for lack of tax motives (chapter II, article 7). As mentioned above, the undertakings considered at risk at the first step

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[29] COM(2021) 565 final, *supra nota 4*, p. 9
[30] *Ibid.*
[31] Investment Europe. (2017). *The Use of Holding Companies and Choice of Jurisdictions by the Private Equity Industry*. Retrieved March 2, 2023, from https://www.investeurope.eu/media/1184/the-use-of-holding-companies-and-choice-of-jurisdictions-in-private-equity.pdf

proceed to the second step, which is the core of the substance test itself. Since they are at risk, these undertakings are asked to report on their substance in their tax return.[32]

Reporting on substance means providing detailed information, usually 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 particular circumstances that are usually present in an undertaking that performs substantial economic activity.[33]

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. Third, at least one director resident close to the undertaking and is committed to its activities or, alternatively, a sufficient number of company employees who carry out its core activities and being resident close to the undertaking.[34]

A director's commitment to the undertaking's activities can be seen in his or her qualifications, which should be such that they enable the director to actively participate in decision-making processes, the formal powers in which he or she is vested, and the director's actual participation in the undertaking's day-to-day management. Alternatively, it would be expected that the undertaking has adequate nexus to the MS of claimed tax residence if most of its employees that perform day-to-day management are resident for tax purposes close to that MS. Decision-making should also take place within the MS 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 regarding undertakings with cross-border activities that are geographically mobile, and which do not have own resources for their own administration.[35]

Moreover, the reporting must be supported by satisfactory documentary evidence, which, if not already included, should be attached to the tax return as well. The evidence required is aimed at allowing the tax administrations to directly verify the truth of the reported information as well as

[32] COM(2021) 565 final, *supra nota 4,* p. 9
[33] *Ibid.*
[34] *Ibid.*
[35] *Ibid*., p. 10

to form a general overview of the situation of the undertaking to consider whether to initiate a tax audit.[36]

1.5.3. Presumption of lack of minimal substance and tax abuse

The third step of the test prescribes the appropriate valuation of the information that the undertaking reported in the second step in terms of substance (chapter II, article 8). It sets out how the outcome of the reporting, in other words, 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 who's reporting also leads to the conclusion 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, lacking substance and being misused for tax purposes.[37]

An undertaking that is a risk case but whose reporting reveals that it has all relevant elements of substance should not be considered a "shell" for the purposes of the Directive. This presumption, however, does not preclude tax administrations from concluding 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.[38]

1.5.4. Possibility of rebuttal

The fourth step is rebuttal of presumption (chapter II, article 9). It entails the right of the undertaking, which is assumed to be shell and misused for tax purposes, to prove that it has substance or, in any case, that it is not misused for tax purposes of the Directive. This is a critical opportunity because the substance test is dependent on indicators and, as a result, may fail to capture the specific facts and circumstances of each individual instance.[39]

As a result, taxpayers will have an effective right to assert that they are not a shell in the meaning of the Directive. To claim a rebuttal of a presumption of shell the taxpayers ought to produce

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[36] COM(2021) 565 final, *supra nota 4,* p. 10
[37] *Ibid.*, p. 10
[38] *Ibid.,* p.10-11
[39] *Ibid.*

concrete evidence of the activities they perform and how. The evidence produced is predictable to include information on the commercial (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 and to include information on the resources that such undertaking uses to perform its activity and to include information allowing to verify the nexus between the undertaking and the MS where it claims to verify that the key decisions on the value generating activities of the undertaking are taken there.[40]

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.[41]

The General Anti-Abuse Rule (GAAR) in ATAD 1 requires MSs to consider the economic substance of a transaction in order to determine whether it is abusive and should be counteracted. This means that taxpayers who engage in transactions that are solely designed to obtain a tax advantage without any underlying economic substance are at risk of being challenged by tax authorities. In the area of unharmonized direct law European Court of Justice (CJEU) has clarified that MSs have no obligation to enact measures preventing abusive practices. ATAD 1's required all MSs to have by 1 January 2019 a general measure available in their domestic law to strike down abusive corporate tax practices, even where such practices do not involve any cross-border element. GAAR applies where the main or one of the main purposes of the arrangement is to obtain a tax advantage and the CJEU's case law often appears to apply more taxpayer's

[40] COM(2021) 565 final, *supra nota 4*, p. 11
[41] *Ibid.*

welcoming tests.[42] Although the intention of Article 6 is to harmonize general anti-abuse rules in the domain of tax law among all MSs, its broad scope and wording give rise to numerous issues, particularly regarding its proper interpretation and application in a manner that is compatible with EU law.[43]

In the Proposal to evidence economic substance, taxpayers must be able to demonstrate that the transaction or arrangement has a valid commercial purpose and is consistent with the economic reality of the situation. This can include providing evidence of the business purpose of the transaction, the nature and value of the assets involved, the functions performed, and risks assumed by the parties, and the commercial rationale for the transaction.

1.5.5. Exemption for lack of tax motives

The fifth step is an exemption for lack of tax motives (chapter II, article 10). 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.[44]

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 planning.[45]

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

[42] De Broe, L., & Becker, D. (2017). The general anti-abuse rule of the anti-tax avoidance directive: an analysis against the wider perspective of the european court of justice's case law on abuse of eu law. *EC Tax Review*, 26(3), 133-144.
[43] Kuzniacki, B. (2019). The c.j.e.u. case law relevant to the general anti-avoidance rule (g.a.a.r.) under the anti-tax avoidance directive (a.t.a.d.). *University of Bologna Law Review*, 4(2), 261-282.
[44] COM(2021) 565 final, *supra nota 4,* p. 11
[45] *Ibid.*

for a tax year. As the process for obtaining an exemption could create a burden for both the undertaking and the tax administration while lead 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 (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.[46]

1.5.6. Tax consequences

The sixth step is tax consequences regulated in (chapter III, articles 11 and 12). Identification as a shell entity may lead to multiple detrimental tax consequences, such as the denial of issuance of certificates of tax residence allowing the shell entity to benefit from income tax treaties or the relevant EU (parent-subsidiary and interest-royalty) directives' tax reliefs, or taxation of the shell entity's relevant income at the level of the shareholder (CFC-like rule).[47]

Moreover, the shell entity's state of residence still would be able to tax this entity accordingly. It is striking that the draft directive does not include any measures to prevent double taxation, whereas prevention of double taxation was exactly the purpose of the parent-subsidiary and interest-royalty directives. MSs would apply an additional penalty applicable to infringements of the local implementation of this draft directive that includes an administrative sanction of at least 5% of the shell entity's turnover.[48]

1.5.7. Exchange of information

The seventh step is the exchange of information (chapter IV, article 13). All MSs 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 MSs from the first step, when an undertaking is classified as being at risk for the purposes of this Directive.[49]

Exchange will also apply where the tax administration of a MS makes an assessment based on facts and circumstances of individual cases and decides to certify that a certain undertaking has

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[46] COM(2021) 565 final, *supra nota 4,* p. 11
[47] *Ibid.*, p. 12
[48] *Ibid.*
[49] *Ibid.,* p 14

rebutted the presumption of being shell or should be exempt from the obligations under the Directive. This will ensure that all MS are able to become aware, in a timely manner, of the discretion exercised and the reasons behind each assessment. MSs will also be able to request the MS 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.[50]

To achieve that the information is available to all MSs 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. MSs 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.[51]

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 principle is that such information should allow all MSs to receive the information reported by undertakings at risk for the purposes of this Directive. In addition, where a MS's administration assesses a rebuttal of presumption or an exemption from the obligations of the Directive, the information exchanged should allow other MSs to understand the reasons for this assessment. Other MSs should always be able to request from another MS a tax audit on any undertaking that passes the gateway of this Directive, if they have doubts on whether it has the minimal substance required.The requested MS should perform the tax audit within a reasonable timeframe and share the outcome with the requesting MS. If there is a finding of 'shell' entity, the exchange of information should be automatic in accordance with Article 13 of Unshell Directive Directive.[52]

[50] COM(2021) 565 final, *supra nota 4,* p. 14
[51] *Ibid.*
[52] *Ibid.*

2. GATEAWAYS COMPABILITY WITH THE FREEDOM OF ESTABLISHMENT

2.2. The Nature of Freedom of Establishment

The Treaty on the Functioning of the European Union (TFEU) came into force on December 1, 2009, following the ratification of the Treaty of Lisbon, which made amendments to the Treaty on European Union and the Treaty establishing the European Community (TEC). The TFEU is an amended and renamed version of the TEC. The TFEU includes enhancements to the social dimension of the European Union. As stated before, 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.

The single market, also known as common market or internal market, is essential to the EU and is still its principal economic rationale.[53] The single market of the EU is based on the four fundamental freedoms which are free movement of goods, free movement of capital, free movement of people and freedom to establish and provide services. They promote economic growth, job creation, and increased consumer choice, and provide businesses with a larger market and greater opportunities for expansion. They also strengthen the EU's political and social integration by promoting cross-border cooperation and understanding.[54]

The main focus of the proposed action by the Commission appears to be the abuse of the freedom of establishment to gain access to advantageous domestic laws, double taxation treaties (DTTs), or EU regulations.[55] The existence of a concept of "abuse of rights" in the case-law of

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[53] Craig, P., De Burca, G. (2020). EU Law, Texts, Cases and Materials. Seventh Edition. Oxford University Press. p. 641

[54] *Ibid.*

[55] Pasquale P., Nogueira J. F. P., Turina A., Lazarov I. (2022). Abuse, Shell Entities and Right of Establishment/ A Plea for Refocusing Current Proposals and Achieving Deeper Coordination within the Internal Market. World Tax Journal.

the CJEU is touching various areas, including company law tax legislation, and has been attracting, since the 1990s, much attention and debate in the scholarly literature all over Europe.[56]

Article 49 TFEU contains the right to freedom of establishment, allowing natural and legal persons to establish themselves in other Member States:

"Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State.

Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is affected, subject to the provisions of the Chapter relating to capital."

Article 54 TFEU then further clarifies the concept of a company or a firm:

"Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Union shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States.
'Companies or firms' means companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit-making."

Freedom of establishment has been a promise not only to individuals, but also to companies, and the relevant articles in the EEC Treaty have long been proclaimed to have direct effect (Reyners

[56] Cerioni, L. (2010). The "abuse of right" in EU company law and EU tax law: A re-reading of the ECJ case-law and the quest for a unitary notion. 44(6), 440-446. Brunel University Research Archive.

v Belgium case 1974).[57] The fundamental rights of this unique legal system are found in the Treaty of Rome (the Treaty establishing the European Economic Community) and in the jurisprudence of the European Court of Justice.[58] Freedom of establishment shall contain the right to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is affected, subject to the provisions of the Chapter relating to capital.[59] Entrepreneurs have long considered cross-border merging as an ideal tool to exercise their freedom of establishment. This strategy allows them to consolidate their operations, reorganize their businesses, and simplify their group structure, depending on their specific needs and circumstances.[60]

The exercise of fundamental freedoms such as freedom of establishment enables individuals to benefit from tax differences resulting from tax competition between MSs. As a result, this exercise cannot be penalized by national regulations under any circumstances. However, if this exercise is conducted in a way that violates the objectives of the freedoms or the rules of secondary legislation, it may be subject to appropriate measures by national regulations in accordance with EU regulations.[61]

2.3. The case law of the European Court of Justice

The European Court of Justice (CJEU) has had a major impact on the fact that EU legislation is a ‘coherent whole’. CJEU principles have an essential gap-filling and interpretative function within the framework of EU law completing the existing positive rules and enhancing their consistent interpretation.[62] One could contend that the Court of Justice has played a vast and vital role in the

[57] Bachner Thomas. (2003) Freedom of Establishment for Companies: A Great Leap Forward. The Cambridge Law Journal, Vol. 62, No. 1., 47-48
[58] Marcoux, Laurent Jr. The Concept of Fundamental Rights in European Economic Community Law. *Georgia Journal of International & Comparative Law*, 13(667), 667.
[59] Cuyvers Armin. (2017) East African Community Law: Institutional, Substantive and Comparative EU Aspects. Brill. pp. 376-391
[60] Bejan, F. F. (2012). Freedom of establishment and cross-border merging. *AGORA International Journal of Juridical Sciences*, 2012(2), 1-7.
[61] Lasso, D. (2021). The concept of abuse in tax matters within european union law. *Cuadernos de Derecho Transnacional*, 13(2), 362-401
[62] Craig, P., De Burca, G. (2020). EU Law, Texts, Cases and Materials. Seventh Edition. Oxford University Press.

development and constitutionalizing of EU law and consequently, it is essentially due to the Court that EU law can function as a legal system.[63]

The CJEU has consistently held that the freedom of establishment is a core principle of the EU, enshrined in Article 49 of the TFEU. The right allows natural persons and companies to set up businesses, branches, or subsidiaries, and carry out economic activities in any MS of the EU without discrimination based on nationality. The proposal's gateway criteria require companies to demonstrate that they have "real economic activities" in the jurisdiction where they are established, as well as "genuine economic reasons" for the structure they have adopted. The criteria may be seen as going beyond what is necessary to combat tax avoidance and evasion and could be viewed as creating undue restrictions on the freedom of establishment.

The CJEU has developed a broad interpretation of the freedom of establishment, which includes the right to move freely and reside in other EU MSs, the right to acquire and own property, and the right to manage and operate a business. The Court has also emphasized the importance of mutual recognition, which requires MSs to recognize qualifications and authorizations granted by other MSs, thereby facilitating the free movement of people and businesses within the EU. At the same time, the CJEU has recognized that the freedom of establishment is not an absolute right and may be subject to limitations that are necessary and proportionate for reasons of public policy, public security, or public health.[64] The Court has also established principles for the application of the freedom of establishment in specific contexts, such as the provision of services, recognition of professional qualifications and the establishment of subsidiaries.[65]

The doctrine of abuse of rights is a potent tool in the hands of both national courts and the CJEU. Many MSs have adopted the principle of abuse of rights, either in its teleological form or its subjective-intentional version. While the CJEU's case law on abuse of rights is still evolving, it has begun to take a more nuanced approach. It remains to be seen whether the CJEU will strive for greater consistency and expand its two-pronged approach across its jurisprudence on abuse/avoidance. Economic actors will likely continue to exploit the free movement provisions

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[63] Szudoczky, Rita. The Sources of EU Law and Their Relationships: Lessons for the Field of Taxation. IBFD Doctoral Series

[64] See Court decision, Commission v Italy, C-110/05, EU:C:2009:66; Raymond Vander Elst v Office des Migrations Internationales, C-43/93, EU:C:1994:310; Caixabank, C-224/19, EU:C:2020:578

[65] See Court decision, Reinhard Gebhard v Consiglio dell'Ordine degli Avvocati e Procuratori di Milano, C-55/94, EU:C:1995:411; Reinhard Gebhard v Consiglio dell'Ordine degli Avvocati e Procuratori di Milano, C-55/94, EU:C:1995:411; Centros C-212/97, *supra nota 69*

for arbitrage purposes. Defining the relationship between abuse and arbitrage is a crucial task for the CJEU, particularly given the inadequacies of the EU legislature in addressing such issues. As a result, arbitrage and abuse claims are likely to remain a significant feature of the CJEUs case law going forward.[66]

In the current state of the development of EU law, MSs are allowed any real scope for preventing tax avoidance and evasion, subject to due observance of the proportionality principle, only in cases where entirely artificial arrangements have been established.[67]

2.3.1. The establishment of subsidiaries

The Centros case issued in 1999 involved a Danish company called Centros ApS, which had been incorporated in Denmark with the intention of establishing a subsidiary in the UK to operate a mail-order business. The UK authorities refused to register the subsidiary on the grounds that it was a "letterbox" company (i.e., shell company) meaning it had no real economic activity in the UK and had been established solely for the purpose of taking advantage of more favorable UK tax laws.[68]

The ECJ ruled that, under EU law, companies have the right to establish themselves in any MS and carry out their activities there, as long as they are incorporated in accordance with the laws of their state of origin. The court held that the UK authorities could not deny the registration of Centros' subsidiary solely on the grounds that it had been incorporated in Denmark.[69]

The Centros case is a landmark ruling and was a significant milestone in the development of the EU single market, as it recognized the right of companies to establish themselves in any MS, and carry out their activities there, without facing unnecessary barriers. The principle of freedom of establishment has since been reaffirmed and extended in numerous other cases, and it remains a cornerstone of EU law and policy today.[70]

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[66] Schammo, P. (2008). Arbitrage and abuse of rights in the ec legal system. *European Law Journal*, 14(3), 351-376.
[67] Ronfeldt, T. (2011). Anti-abuse clause or harmonization. *Intertax*, 39(1), 12-18.
[68] Court decision, 9.3.1999, Centros, C-212/97, EU:C:1999:126
[69] *Ibid.*
[70] *Ibid.*

The Unshell Directive's gateway criteria can be seen as an attempt to prevent companies from incorporating in a particular jurisdiction for the sole purpose of taking advantage of more favorable tax laws just like the UK authorities refused to register a subsidiary because it had been incorporated in Denmark solely for the purpose of taking advantage of UK tax laws. However, the Centros case held that companies have the right to establish themselves in any MS and carry out their activities there, as long as they are incorporated in accordance with the laws of their state of origin. Thus, gateway criteria may potentially restrict this right if it unfairly targets companies with legitimate business reasons for having structures in multiple jurisdictions, thereby potentially limiting their ability to establish themselves in different EU MSs.

2.3.2. Cross-border transfer

The Polbud case issued in 2017 involved a Polish company, Polbud Wykonawstwo sp. z o.o., which sought to transfer its registered office from Poland to Luxembourg in order to take advantage of more favorable business conditions in Luxembourg. The Polish authorities denied Polbud's request, arguing that it would effectively result in the liquidation of the company under Polish law. However, the CJEU ruled that EU law allows companies to transfer their registered office from one MS to another, provided that certain conditions are met. Specifically, the court held that MSs cannot impose additional requirements or formalities beyond those set out in the EU's Cross-Border Directive, which governs such transfers.[71]

The Polbud landmark ruling is significant as it clarifies and strengthens the right of companies to establish themselves in any EU MS and to carry out their activities freely within the EU's single market. The ruling reinforces the principles of freedom of establishment and free movement of companies, capital, and services within the EU. It also provides greater legal certainty and clarity for companies seeking to transfer their registered offices across borders within the EU.[72]

The Unshell Directive's gateway criteria for corporate mobility aim to provide a framework for determining when such restrictions may be justified, with a focus on protecting the public interest while promoting cross-border mobility. By considering the Unshell Directive's compability with the Polbud case, the Unshell Directive can help to ensure that MSs comply

[71] Court decision, Polbud – Wykonawstwo, C-106/16, EU:C:2017:804.
[72] *Ibid.*

with EU law and uphold the rights of companies to establish themselves across borders. The Polbud case held that cross-border conversion must be allowed by the MS of departure even if it solely concerns the transfer of the registered office without the pursuit of a genuine economic activity in the MS of arrival. However, the proposal's requirement for a "genuine economic activity" in the MS of destination may create difficulties for companies seeking to exercise their freedom of establishment. This requirement may be seen as imposing additional restrictions on corporate mobility beyond what is required by EU law.

2.3.3. Concept of abuse

The case Cadbury Schweppes plc and Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue (Cadbury Schweppes case) issued in 2006 concerned a UK-based company, Cadbury Schweppes, which had established a subsidiary in Ireland to take advantage of Ireland's lower tax rates. The UK tax authorities argued that this arrangement amounted to artificial tax avoidance and sought to impose a tax charge on the profits of the Irish subsidiary.[73]

The CJEU ruled that EU MSs cannot impose restrictions on the freedom of companies to establish themselves in another MS such restrictions are justified by overriding reasons of public interest. The court found that the UK's tax rules were not aimed at preventing abusive tax avoidance, but rather were intended to protect the UK's tax base by preventing companies from shifting their profits to lower-tax jurisdictions. The court found that the UK's rules did not meet the criteria for justifying restrictions on the freedom of establishment under EU law, and therefore were not compatible with EU law.[74] In the Cadbury Schweppes case CJEU has 'denationalised' the concept of abuse and 'Europeanised' this concept by setting the centre on its effectiveness in the Internal Market, not in the national market.[75]

The ruling reinforced the principles of freedom of establishment and free movement of capital within the EU's single market, which are important foundations of the EU's economic integration. It also established an important precedent for future cases involving cross-border tax planning by companies and has been cited in numerous subsequent cases as a key precedent for

[73] Court decision, Cadbury Schweppes, C-196/04, EU:C:2006:544
[74] I*bid.*
[75] Vanistendael, F. (2006). Halifax and cadbury schweppes: one single european theory of abuse in tax law. *EC Tax Review*, 15(4), 192-195.

upholding these fundamental principles of the EU single market.[76] Additionally, in Leur-Bloem[77] and Foggia[78], it was determined that the anti-abuse provision in the Merger Directive must be applied by MSs on a case-by-case basis, without the use of predetermined general criteria, to comply with primary law.[79] This position was further reinforced in later cases such as Europark[80], Eqiom[81], and Deister[82], where it was ruled that the discretionary application of anti-avoidance measures per Directives, along with predetermined general criteria, constituted an unwarranted restriction on fundamental freedoms.[83]

The Unshell Directive proposal's gateway test must be designed and implemented in a way that is proportionate and complies with EU law, to ensure transparency and fairness in the tax system while respecting the freedom of establishment of companies. If MSs interpret and apply the gateways criteria differently, this could create legal uncertainty and undermine the effectiveness of the proposal in preventing abusive tax practices.

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[76] Vanistendael, F. (2006). *supra nota 76,* p. 192-195.
[77] Court decision, Leur-Bloem v Inspecteur der Belastingdienst/Ondernemingen Amsterdam 2, C-28/95, EU:C:1997:369
[78] Court decision Foggia v. SGPS, C-126/10, EU:C:2011:718
[79] Lazarov, I., Govind, S. (2019). Carpet-bombing tax avoidance in europe: examining the validity of the atad under eu law. *Intertax*, 47(10), 855.
[80] Court decision, Euro Park Service v Ministre des finances et des comptes publics, C-14/16, EU:C:2017:177
[81] Court decision, Eqiom and Enka, C-6/16, EU:C:2017:641
[82] Court decision, Deister Holding and Juhler Holding, C-504/16, EU:C:2017:1009
[83] Lazarov, I., Govind, S. (2019). Carpet-bombing tax avoidance in europe: examining the validity of the atad under eu law. *Intertax*, 47(10), 855.

CONCLUSION

This thesis has focused on examining how and in what ways the Unshell Directive Proposal's gateaway criteria might does infringe the freedom of establishment. To discover the answer to this key research question, the thesis assessed the underlying criteria used in the Unshell Directive's gateway filtering system and how do the criteria affect companies with structures in multiple jurisdictions and the CJEU case law's regarding the freedom of establishment and its impact the Unshell Directive.

Based on the analysis the Unshell Directive might introduce a material level of uncertainty to and compliance obligations for EU international business structures, in a legislative landscape that already avails of tools (ATAD1, GAAR, etc.) for MSs to deny tax benefits to entities that are targeted by this Directive. ATAD 1 GAAR appear to apply only where the main or one of the main purposes of the arrangement is to obtain a tax advantage as the application of the abuse of rights principle by the CJEU is typically done on a case-by-case basis. Thus, the Unshell Directive's gateways test should be clear enough to prove that 'the abuse of right' is clearly present. The Proposal explicitly states that local anti-avoidance regulations, either currently in force or to be implemented in the future, could be enforced simultaneously with, or in addition to, the rules pertaining to shell entities. This means that any certainty gained by identifying at-risk undertakings could be lost, as local tax administrations may still use dissimilar sets of regulations to disqualify EU directive or double tax treaty benefits.

The measures proposed in the Proposal may be argued that the necessity and proportionality of the Proposal are questionable, as it may be perceived as redundant and surpassing what is required to achieve the Proposal's objective. The absence of guidance on the impact of the Directive on other anti-avoidance concepts may be viewed as not fulfilling the goal of tax certainty for genuine business structures. Furthermore, it is crucial to ensure that the text of the Proposal is sufficiently clear and comprehensible, as this is essential in ensuring that the principle of legal certainty is respected when various stakeholders apply the relevant legislation.

Furthermore, the exclusive application of the regulations outlined in the Proposal to undertakings within the European Union raises concerns regarding its compatibility with the freedom of establishment. It could be argued that limiting the scope of the regulations to intra-EU situations puts non-EU undertakings in a favorable position. It is therefore essential to ensure that the Proposal's proportionality, design, and coherence align with the upcoming Proposal for substance requirements for entities outside the EU.

While the Unshell Directive proposal aims to provide clarity and guidance on the circumstances in which MSs may restrict corporate mobility one concern is that the gateway criteria proposed may be too rigid or inflexible, leading to a lack of discretion for MSs in balancing competing interests. For example, some MSs may argue that they have compelling reasons for imposing restrictions on public interest such as national security or maintaining social cohesion. This could lead to a conflict between the MS's legitimate concerns and the EU's desire to ensure the free movement of companies within the Internal Market.

To mitigate the burden on taxpayers and tax administrations, it could be beneficial to incorporate de minimis rule into the Proposal. This provision would exclude businesses that earn less than a certain minimum revenue threshold each year from the new regulations. Such a rule would promote fairness in the application of the rules and prevent unnecessary reporting requirements for taxpayers and tax authorities when there is no significant tax benefit at stake.

Another potential issue is that the Unshell Directive could be subject to interpretation by MSs, leading to inconsistent application across the EU. This could create uncertainty for companies seeking to establish themselves or relocate their registered offices and could lead to legal disputes or delays. However, based on standing CJEU case law, application of anti-abuse legislation cannot rely on fixed criteria. Instead, it must be established on a case-by-case basis whether the substance of an undertaking is inappropriate for the activities performed.

Finally, there is a risk that the Unshell Directive could be perceived as an infringement on MS sovereignty, particularly if it is seen as imposing additional restrictions on corporate mobility beyond what is required by EU law. Some MSs may argue that they should have greater discretion in determining when and how to restrict corporate mobility, particularly in cases where there are compelling public interest reasons at stake.

The proposed Directive has a broad scope and is expected to have a significant impact on both commercial and personal undertakings falling within its purview. Undertakings failing to meet the minimum substance requirements and unable to demonstrate their authentic business purpose may face restrictions on the current benefits they enjoy under the Parent-Subsidiary Directive or the Interest and Royalties Directive, as well as any relevant double tax treaties they rely on. While the opportunity for genuine business undertakings to prove their legitimacy to tax authorities is a positive development, the added administrative burden on both taxpayers and tax authorities is substantial. This burden is compounded by the recent anti-avoidance legislation and the forthcoming changes under the OECD international tax reform proposals.

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