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NOTE

From:	Presidency
To:	Working Party on Tax Questions (Direct Taxation)
Subject:	Proposal for a COUNCIL DIRECTIVE laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU - Presidency steering note

In view of the meeting of the Working Party on Tax Questions on 4 July 2023, delegations will find attached the Presidency steering note.

Presidency steering note

WPTQ meeting (Direct Taxation – UNSHELL proposal)

JULY 4, 2023

The proposal for a Council Directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU (so-called "Unshell proposal") was tabled by the Commission on 22 December 2021.

The proposal has been discussed in three HLWP and eleven WPTQ meetings along 2022 and 2023. During these meetings, delegations have expressed concerns about some parts of the proposal and a strong support for others. Progress towards finding common ground has been made in several areas of the proposal, including on the scope of application, minimum substance indicators and automatic exchange of information. Based on the discussions taken place so far, the Spanish Presidency is of the view that although some issues may need refining, there is considerable support for the underlying ideas of the proposal and for the latest compromise text. Therefore, the Spanish Presidency has mapped the main outstanding issues which need further discussion in the WPTQ and suggested a possible way forward on these issues, including in the form of compromise texts that can be found in the current note. Changes compared to the latest compromise text prepared by the Swedish Presidency (document WK 4310/2023) are highlighted in bold, underlined and strikethrough.

The Presidency invites delegations to discuss the main outstanding issues and to reply to questions set out below, in order to agree on a way forward and to pave the way for an agreement.

1. TAX CONSEQUENCES

Article 11 related to the "tax consequences" in the Member States other than the Member State of the shell entity has been discussed in many Working Party meetings. At the February 2023 WPTQ meeting, in order to accommodate delegation´s requests, the Presidency put forward a compromise text stating that when an entity is considered a shell entity, other Member States shall deny the shell entity exemptions or reductions of tax that follow from the Parent-Subsidiary Directive (PSD) and the Interest-Royalty Directive (IRD), and double taxation agreements within the EU (DTAs). Almost half of the delegations that expressed a view at the meeting raised concerns and doubts when it comes to a reference to DTAs concluded between Members States, *inter alia* for legal reasons related to interaction between the Directive and these treaties. Nevertheless, it was quite clear that the many delegations were of the opinion that the benefits included in DTAs mirrors the EU Directives.

At the HLWP of April, almost half of the delegations expressed again concerns and doubts when it comes to regulate tax consequences regarding DTAs concluded between Member States.

Therefore, the Presidency considers that it is of key importance to reach an agreement on this matter. It is the Presidency´s view that a possible way forward would be that benefits of the PSD and the IRD should be denied to a shell entity and that aim should not be avoided through the application of a DTA to the same flow of income.

Taking into account that for some Member States it is necessary for the effectiveness of the Directive to deny both instruments, the PSD and IRD and the DTAs, and given the reluctance of other Member States to mention DTAs in the article, the Presidency proposes to include language in the recital of the Directive.

In this regard, rather than amending intra-EU Treaties by an Article of the Directive, it may be possible to see the same outcomes flowing from a well-targeted recital in the Directive. Such a recital would clarify that Member states, other that the Member State of the entity, may apply their anti-avoidance provisions to tackle tax abuse (both contained in the DTAs and internal legislation). For example, they may consider that an entity which is presumed to be a shell entity and does not rebut the presumption, is not the "beneficial owner" within the meaning of any agreement or convention that provides for the elimination of double taxation of income in force between that Member State and the Member State of the entity.

In consequence, we propose this wording:

Article 11

Tax consequences in a Member State other than the Member State of the entity

"Where an entity is presumed to be a shell entity under Article 6(2) and does not rebut the presumption successfully under article 9(2), a Member State other than the Member State of the entity, shall, in relation to relevant income relating to the tax period to which the reporting refers, disallow any exemption or reduction of tax that follows from~~: (a)~~ Articles 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 entity being considered to be resident for tax purposes in a Member State.~~, and~~

~~(b) any agreement or convention that provides for the elimination of double taxation of income and, where applicable, capital, in force between that Member State and the Member State of the entity."~~

Recital (10)

*"To ensure effectiveness of the proposed framework, it is necessary to establish appropriate tax consequences for entities that do not ~~have minimal substance for tax purposes~~ **fulfill the indicators laid down in this Directive.** Entities that are presumed to be shell entities and that have not rebutted this presumption~~, should not be allowed certain exemptions or reductions of tax in other Member States that follow from 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. Such entities~~ should not be allowed to benefit from Council Directives 2011/96/EU and 2003/49/EC.~~ However, the dissallowing of benefits according to those Directives should not imply an obligation for Member States to introduce rules in national law regarding for example withholding taxes, if Member States do not already apply such rules.~~*

~~*The Member State where the entity is resident for tax purposes should when issuing a certificate of tax residence to the entity include a notice in the certificate expressing that the entity is presumed to be a shell entity according to this Directive. Such a notice will serve as a warning, that the entity has been lacking substance for the previous tax period. The issuance of a certificate of tax residence with such a notice, should not set aside the national rules of the Member State of the entity 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 they should examine the entity more closely before deciding how future transactions with the entity should be treated.*~~ ***These tax consequences should not be undermined, from the application of similar exemptions or reductions of tax enshrined in agreements and conventions that provide for the elimination of double taxation of income, and where applicable, capital, concluded between Member States. For this reason, entities that are presumed to be shell entities and that have not rebutted this presumption should not be entitled to the benefits of agreements and conventions that provide for the elimination of double taxation of income in force between Member States, on the basis of the rules of these agreements and conventions covering the same income streams as Directives 2011/96/EU and 2003/49/EC. In addition, it is expected that Member States apply other antiavoidance provisions provided in such agreements or conventions and, where applicable, domestic antiabuse provisions.***

- **Question 1: Would the delegations agree with the proposed wording in Article 11 and the related recital as a compromise?**

2. DOMESTIC ANTI-ABUSE LEGISLATION

During the Swedish Presidency, the scope of the Directive (Article 2 and Recitals 3 and 3a, mainly) has been subject to intense discussions. The compromise texts of January, February and March (documents WK 528/2023 (17 January 2023), WK 1907/2023 (13 February 2023) and WK 3544 /2023 (14 March 2023)) show the progress made in order to reflect the common position of most Member States that the adoption of Unshell Directive would be an exercise of Union competence in an area of shared competence. This means that Member States would not be able to introduce different or derogatory indicators as regards those elements that are governed by EU law, in our case by Unshell Directive (cf. Article 2(2) TFEU). It is important to clarify that in the areas not harmonized by the Directive Member States would remain free to maintain or adopt national measures. It is clear from the discussion at Working Party level that Members States wish to be explicit in that this Directive is not meant to function as safe harbour and thus as an obstacle to preventing tax avoidance, tax evasion, tax fraud, abuse or any kind of tax default.

In this context, most Member States have requested that the Directive should further clarified its interaction with national anti-abuse rules, and that it has to be stated that the national rules continue to be applicable.

According to this line of reasoning, the test in this Directive would not be an exclusive test. It would not preclude source states from continuing to apply other domestic or agreement-based provisions (including provisions corresponding to the anti-tax avoidance rule in the PSD, the IRD or DTAs) on entities that:

- are shell entities according to this Directive;
- are not found to be a shell entity according to this Directive;
- are excluded entities according to the article 2(a) of this Directive; and
- entities out of the scope of the Directive.

The aim of the Directive is not to capture all potential cases of lack of substantial activity of an entity, but only those where certain indicators are met, in order to fight against the manifest cases of shell entities without having an excessive administrative burden. Thus, the Directive lays down indicators for the identification of such manifest cases of shell entities that can be presumed to be misused for tax purposes, but not all the possible cases.

The Presidency takes stock of the general agreement and makes a drafting effort to clarify that the purpose of this Directive is not to create a safe harbour. In this regard, the Presidency proposes to clarify the article 1 of the Directive stating that this Directive only covers manifest cases of misuse of shell entities for tax purposes. Additionally, the article 2 and recitals are modified in order to explain how the national antiabuse rules interact with the Directive.

Proposed wording:

Article 1

Subject matter

This Directive lays down indicators of minimum substance ***for the identification of manifest cases of misuse of shell*** *entities in Member States and rules for disallowing certain tax benefits for entities that do not meet those indicators and* ***are found to be shell entities****, as well as rules on the exchange of information.*

Article 2

Scope

This Directive applies to all entities that are considered tax resident in a Member State, and that are not excluded entities within the meaning of Article 2a.

This Directive shall not preclude Member States from applying domestic or agreement-based provisions required for the prevention of tax avoidance, tax evasion, tax fraud, abuse ***or any other kind of tax default****, provided that such provisions are compatible with Union law, including this Directive.*

Recital (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 entities 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 ***in the Member State of tax residence****. This is done in order to ensure that entities lacking minimal substance are not used as instruments of tax evasion or tax avoidance* ***through the abuse of EU tax directives and Member States' agreements or conventions for the avoidance of double taxation on income, or where applicable capital with similar effect.*** *As those entities 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 a Member State*** ~~*in the internal market*~~ *as well as for delineating* ***certain*** *specific tax consequences linked to such* ***determination*** ~~*insufficient substance*~~*.* ***This Directive therefore lays down indicators for the identification of such manifest cases of shell entities that they can be presumed to be misused for tax purposes in the internal market as well as rules to disallow certain tax benefits to such entities.*** ~~*Where an entity declares that it meets the criteria laid down in this Directive, this should not prevent the Member States from continuing to apply other domestic or agreement-based provisions to assess any possible tax default.*~~

Recital (3a)

Considering that this Directive does not aim to capture all potential cases of lack of substantial activity of an entity and is limited to cases with cross-border relevance that bear features allowing the application of a presumption of misuse for tax purposes, Member States should not be precluded from applying national or agreement-based provisions preventing tax avoidance, tax evasion, tax fraud or other types of tax default to excluded entities or entities that are not found to be shells under this Directive as well as entities out of the scope of this Directive. Equally, given that this Directive prescribes certain limited consequences to be applied by the Member State of tax residence of the shell entity and the Member State from which relevant income flows to a shell entity, Member States should not be precluded from applying further tax consequences to shell entities or parties not subject to consequences under this Directive, e.g. the shareholders of shell entities.

~~*The Directive lays down certain indicators of minimum substance for entities and rules for disallowing certain tax advantages. Therefore, the Directive does not regulate consequences for entities other than those mentioned above, and does not regulate consequences for shareholders.*~~

~~*This should be understood in the sense that Member States may continue to apply the relevant domestic or agreement-based rules with respect to excluded entities or entities that meet the criteria of minimum substance, and with respect to the shareholders of entities lacking minimum substance.*~~

- **Question 2: Would the delegations agree with the proposed wording Articles 1 and 2 and the related recitals as a compromise?**

3. EXCLUDED ENTITIES

At the previous WPTQ meetings, on the one hand, some delegations explained that they would like to have more exclusions; on the other hand, some others were concerned about the long list of such exclusions. Lastly, most delegations expressed the view that, as a compromise, they could accept the latest compromise text, presented by the Swedish Presidency. Therefore, it is the view of the presidency that no changes are proposed to article 2(a).

- **Question 3: Would the delegations agree with the suggestion not to change the latest proposal as a compromise?**

4. MINIMUM SUBSTANCE

At the last Working Party meeting of 22 March 2023, the Swedish Presidency presented a compromise text (WK 4310/2023) where the structure of the indicators for the presumption consists of a mandatory criterion (management), and an optional fulfilment of 3 of the other 4 indicators (one plus three out of four indicators: premises, bank account, employees, board meetings). A majority of delegations considered that the criteria were adequate for the purposes of the Directive.

In the Steering Note of the HLWP in April (WK 4309/2023), it was indicated that "*the main question is how to ensure that the criteria are robust and at the same time easy to report and control. The Presidency compromise text presented in March sets out that substance should be in the Member State of the entity and that criterion (a) regarding managing persons should be a mandatory criterion for entities to fulfil in order to have substance. Furthermore, three out of the four criteria should be met in order to have substance according to the Directive. Whilst views among delegations still diverge, the compromise gained broad support.*"

During HLWP in April it was concluded that the indicators generated a good level of acceptance, and it could be considered that a balance has been found.

In opinion of the Presidency, the broad majority of delegations support the view that: 1) the criteria should be robust but easy to control and report; 2) minimum substance should be in the Member State of residence.

In this regard, the key point is to identify entities that should be captured by the Directive, but without being too strict (which would increase administrative burden).

It is recognized in Recital 9 of the latest compromise text, that "determining "*whether an entity 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 entity."

Therefore, there is a need to establish indicators that are easy to apply and control, but at the same time, the danger is that it may remain difficult to assess the economic substance of an entity through these straightforward indicators.

One delegation has expressed its willingness to strengthen some of the indicators, for example, not to include a required number of employees but a reference depending on the size of the company.

Another issue raised by some delegations during different meetings, including the HLWP held in April, is that it is not essential where the substance of an entity is (for instance, where the meetings of the board of directors take place), and that the only question is whether any substance exists.

However, as mentioned by the Swedish Presidency, most delegations support the approach that the substance must be in the Member State of the entity. Specifically, it was indicated that "*if an entity has tax residency in one State and lack substance in that State, and at the same time has substance in another State, then it is the view of the Presidency that it could indeed be a high risk for tax avoidance motivating such structure of the business. If it is indeed sound business reasons that motivate such a structure, then the rebuttal process offers a possibility for the entity to rebut the presumption of being a shell entity, in its country of residence.*" (See document WK 3554/2023).

Moreover, it is important to bear in mind that the substance test only applies to non-excluded entities, meaning that there is an entry test that fundamentally identifies entities with passive income. The fact that an entity mainly receives passive income and does not have substance in the Member State where it is resident seem reasonable proxies that indicate that the entity may be used for an abusive purpose.

In addition, from the exclusive point of view of the Unshell Directive, to preserve in a Directive the possibility of a duality between MS of residence and MS of substance could open doors to aggressive tax planning. In other words, this duality (residence and substance in different MS) may be aimed at taking advantage of a more favourable network of DTAs in the MS where the entity is resident than in the MS of substance.

Clearly, there may be genuine entities with economic activity with substance in a different MS; but the Directive would establish a risk criterion identifying entities that receive high cross-border income (which is already a very relevant first gateway). In any case, the entity always keeps the possibility to rebut the presumption.

Therefore, the Presidency considers that the indicators requiring substance in the Member State of the entity should be maintained as set out in the latest compromise test.

According to the general views expressed at the HLWP in April, there seems to be a balance between the following elements:

- The indicators are simple and easy to administer;
- In those cases, where an entity is not found to be shell entity according to this Directive nothing impedes to apply ant avoidance domestic rules to those entities;
- If the current indicators are excessive for a specific case, the entities have the possibility of proving otherwise in the rebuttal process.

For these reasons, no modification will be proposed with respect to the indicators of substance.

- **Question 4: Do delegations agree with the analysis provided by the Presidency?**

5. REBUTTAL OF THE PRESUMPTION AND REDUCTION OF ADMINISTRATIVE BURDEN

Rebuttal of the presumption is configured as the right of the entities that are presumed to be shell entities in accordance with Article 6 to prove that they are legitimate and have been established for valid commercial reasons that reflect economic reality.

Whereas most delegations acknowledge the need for providing a possibility to rebut the presumption of being a shell entity, the views among delegations have been diverging on the way of application. Hence, it has been verified that it is necessary to continue the work at a technical level.

At the HLWP meeting on 25 April, various delegations expressed doubts regarding the rebuttal, referring to the administrative burden that this process entails for the tax administration of the entity's State of residence.

In the Presidency´s view, due to the fact that the test is built on the basis of a set of indicators and that there are tax consequences, the rebuttal constitutes an essential element. Hence, whether an entity is actually performing an economic activity or serves mainly for tax avoidance or evasion purposes is a matter of facts and circumstances that have to be assessed on a case-by-case basis. The Presidency is also aware of the burden of proof that the rebuttal represents for both tax administrations and taxpayers.

Consequently, we propose to include only one criteria for the rebuttal of presumption, that is, an entity should prove that it is genuine, that has been put in place and operates for valid

commercial reasons. In order to help to make the assessment, a list of remaining criteria will be provided in the recital as examples.

In the latest compromise text presented by the Swedish Presidency (WK4310/2023), Article 9 (2) provides that Members States shall issue a notice within six months from the request for rebuttal. In order to allow Members States time to adapt, the Presidency considers that the six-month period could be extended during the first tax period of application of this Directive. Accordingly, the Presidency suggests extending the six-month period to one year. This measure will allow Member States to have a longer period to assess the rebuttal process during the first year of application of the Directive, which is when doubts are more likely to arise. In the following tax years, the rebuttal process would be more easily applicable.

The Presidency has also noted that the latest compromise text does not regulate the effects in case Member States do not issue a notice in the above-mentioned six-month period. Therefore, the Presidency proposes that in the event of administrative silence, the presumption of being a shell entity shall be deemed not to have been rebutted.

It is the view of the Presidency that both measures would contribute to reduction of the administrative burden of the rebuttal process.

If the administrative silence operates in the sense described above, the Presidency considers that the automatic exchange of information shall take place within the time limits provided for in Article 13. An addition is therefore suggested to that Article.

Finally, the Presidency proposes a change in Article 9(3) in order to clarify that the entity shall communicate to the competent tax authority of any material changes in its factual and legal circumstances that could influence the rebuttal of the presumption.

Proposed wording:

Article 9

Rebuttal of the presumption

"1. Member States shall take the appropriate measures to allow an entity that is presumed to be a shell entity under Article 6(2) to rebut this presumption by showing the tax authority of the Member State of the entity that it is genuine in the sense that it is put in place for valid commercial reasons which reflect economic reality and not with the main purpose of obtaining a tax advantage. ~~For this purpose, entities shall provide evidence of the rationale behind the establishment and existence of the entity, for instance by showing that it is not part of an arrangement put in place for the main purpose of obtaining a tax advantage. The entities shall also provide evidence that the entity has performed and had control over, and borne the significant risks of, the activities that generated the relevant income or had control over, and borne the significant risks connected with the entity's assets.~~

2. Members States shall ensure that, where they treat an entity as having rebutted the presumption, or where they deny such a request, a notice of that finding is issued to the entity within six months from the request for rebuttal in accordance with paragraph 1. This shall be without prejudice to appeal procedures in accordance with the applicable national law.

If, within six months from the request, the competent authority of the Member State of the entity has not issued a notice, the presumption of being a shell entity shall be deemed not to have been rebutted.

Member States may extend the period referred to in the first and second subparagraphs to a maximum of one year from the request for the rebuttal in the first tax period of application of this Directive.

*3. After the end of the tax period for which the entity rebutted the presumption successfully, in accordance with paragraph 1, a Member State may consider for a period of three tax periods that the entity has rebutted the presumption on the condition that the factual and legal circumstances of the entity undertaking remain unchanged during this period. Such conclusion may include an exemption from the reporting obligations set out in Article 6(1). The entity shall ~~be required to inform~~ **communicate** the tax authority of the Member State of the entity of any material changes in its factual and legal circumstances that could influence the rebuttal of the presumption."*

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 Articles 8(1) and 8ad, 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 according to Directive [OP]

1. The competent authority of the Member State where the entity is resident for tax purposes shall, by means of automatic exchange, inform the competent authorities of all other Member States, in accordance with paragraph 4 of this Article and the applicable practical arrangements adopted pursuant to Article 21. The automatic exchange shall take place within two months following the end of the quarter in which:

(a) the entity was presumed to be a shell entity according to Article 6(2) of Council Directive [OP] without requesting a rebuttal of the presumption according to Article 9(1) of the same Directive; ~~or~~

*(b) a notice under Article 9(2) of Council Directive [OP] was issued concluding that the entity has not rebutted the presumption of being a shell entity**; or***

(c) the period of six months or one year in the first tax period of application of this Directive has ended without any notice under Article 9(2) of Council Directive [OP] issued by the competent authority of the Member State.

(…).

Recital (9)

*"It is recognised that whether an entity 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 entity. Therefore, entities that are presumed to be shell entities should be entitled to prove that they are genuine and put in place for valid commercial reasons which reflect economic reality, and rebut such presumption. The fact that an entity can show that it is not part of an arrangement put into place for the main purpose of obtaining a tax advantage that defeats the object or purpose of the appropriate Union law could be a circumstance to be accounted for when assessing a rebuttal. **After** ~~When~~ 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. **Whilst there should be no requirement for including** an exhaustive list*

of evidence, ~~that it should be required in all cases should not be included. Nevertheless~~ ***entities may provide evidence of the rationale behind their establishment and existence by showing that they are not a part of an arrangement put in place for the main purpose of obtaining a tax advantage but rather for valid economic reasons. Furthermore, the evidence could consist of*** *~~information~~* ***documentation*** *~~regarding~~* ***on*** *the corporate structure of the group coupled with an explanation of the key management tasks and transfer pricing studies which prove that the entity has had control over, and borne the significant risks of, the activities that generated relevant income or* ***that*** *the activities* ***that*** *were connected with its assets ~~could be part of such evidence~~. Evidence that the commercial cause, as laid down in the Articles of Association, matches the actual activity of the entity could also be accounted for. The same applies to evidence showing that assets, typically held for the private use of shareholders, are used within a business activity. Where the Member State, based on such additional evidence, considers that an entity has rebutted a presumption of being a shell entity in a satisfactory manner, it should be able to issue a notice to certify that the entity has minimal substance for tax purposes in accordance with this Directive. Such notice may remain valid for the period during which factual and legal circumstances of the entity remain unchanged and up to 3 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."*

- **Question 5: Would the delegations be in a position of accepting this proposed drafting for the rebuttal of presumption as a compromise?**

6. TAX RESIDENCY CERTIFICATE

At the Working Party meeting of 22 March 2023 the Swedish Presidency presented a compromise text (WK 4310/2023) where it was set out that when an entity is presumed to be a shell entity and does not successfully rebut this presumption, any tax residency certificate granted by the Member State of the entity shall contain a notice that the entity is presumed to be a shell entity for the relevant tax period. Some delegations were of the view that rules on the tax residency certificate would not be useful within the Unshell Directive, mainly because of timing aspects for the application of the tax consequences, and instead would prefer to rely only on exchange of information.

At the 25 April HLWP, several delegations expressed doubts about the relevance of the tax residency certificate indicating that the entity is presumed to be a shell, while others considered that the tax residency certificate would be useful.

The Presidency believes that a way to ease the administrative burden, achieve the deterrent effect, avoid potential defaults and secure the integrity of the rules would be that tax consequences stated in the Directive may apply in the Member State where the entity's income arises not only in the relevant tax period but also in future tax periods, until the taxpayer ceases

to be presumed a shell entity (either by complying with the indicators or by rebutting the presumption). For these reasons, the Presidency suggests a new wording of Article 12.

Taking into account the above, it is proposed that, once an entity is presumed to be a shell entity, tax residency certificates issued afterwards will include a notice, which would alert the withholding agents of Member States. When this situation reverses and the entity ceases to be presumed a shell entity in subsequent periods, tax residence certificates issued afterwards would not have such notice and withholding agents will have to apply the Directives (and the treaties if applicable).

Two scenarios are foreseen:

i) First scenario: The entity is not presumed to be a shell entity, therefore the tax residence certificate would not contain any notice. In this case, the withholding agent would apply the Directives (and treaties if applicable).

If in the following year a MS communicates (EOI) that the entity was a shell entity in the relevant tax period , the actions would be:

> For the payments made before the communication done by the MS, the Shell entity will have to file a tax return including the taxes unpaid. A voluntary period should be given to the shell entity to file the tax return and make the payment. There would be no responsibility for the withholding agent because he acted in accordance with the certificate of residence.
>
> The withholding agent for future payments will have to withhold in accordance to the new certificate of residence that will be issued stating that the entity is a shell entity.

ii) Second scenario: The entity is presumed to be a shell entity, hence the tax residence certificate would contain a notice. In this case, the withholding agent would apply the consequences of article 11.

If in the following year a MS communicates (EOI) that the entity was not a shell entity, the actions would be:

> For the payments made before the communication done by the MS, the Shell entity will have to file a tax return requesting a tax refund.
>
> The withholding agent for future payments will have to withhold in accordance to the new certificate of residence that will be issued stating that the entity is not a shell entity.

Proposed wording:

Article 12

Consequences in the Member State of the entity

"*Where an entity is presumed to be a shell entity under Article 6(2) and does not succesfully rebut this presumption under Article 9(2), any tax residency certificates granted by the Member State of the entity shall contain a notice that the entity is presumed to be a shell entity for the relevant tax period, according to this Directive.*

This notice shall be included in any tax residence certificate granted by the Member State of the entity, unless the taxpayer ceases to be presumed a shell entity, either by complying with the indicators referred to in Article 6 or by rebutting the presumption".

Recital (10b)

The Member State where the entity is resident for tax purposes should, when issuing a certificate of tax residence to the entity, include a notice in the certificate expressing that the entity is presumed to be a shell entity according to this Directive. Such a notice will serve as a warning, that the entity has been lacking substance for the previous relevant tax period. The issuance of a certificate of tax residence with such a notice, should not set aside the national rules of the Member State of the entity with regard to the tax residence and relevant obligations linked thereto. It would rather serve to communicate to other Member States, and third countries ***and withholding agents,*** *that they should examine the entity more closely before deciding how future transactions with the entity should be treated.*

- **Question 6: Do delegations agree with the analysis above on the tax residency certificate? If so, would delegations be in a position to agree with the proposed wording for Article 12 and related recital (10b) as a compromise?**

7. EXCHANGE OF INFORMATION

The Exchange of information was already discussed in previous meetings, including March meeting. Presidency´s view is that no major issues have been raised in relation with the current version of the proposal presented by the Swedish Presidency, so there are no changes proposed by the Presidency to that drafting.

- **Question 7: Are there any issues in relation to the proposed drafting for exchange of information which may prevent your delegation from approving the Directive?**

8. OTHER ISSUES (ARTICLES 3, 14-20)

The rest of the issues have already been discussed in previous meetings and the Presidency´s view is that the text is balanced.

- **Question 8: Are there any obstacles related to Article 3 and 14-20 which may prevent your delegation from agreeing on the Directive?**