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UEL response to the EU public consultation launched regarding the EU directive proposal laying down rules to prevent the misuse of shell entities for tax purposes

The EU Commission released in December 2021 a proposal for a Directive laying down rules to prevent the misuse of shell entities for tax purposes (hereafter the “EU Proposal”).

UEL and the Luxembourg business sectors it represents, support the aim of combating tax avoidance and evasion practices. We generally support the EU Proposal, however we believe it needs to be further amended such that the rules are better targeted, to ensure it is proportionate and administrable for compliant and genuine EU businesses. We also believe that the rules in the EU Proposal must be sufficiently clear and detailed in order to ensure legal certainty for genuine businesses and for tax authorities, and to enable a uniform and consistent implementation across the EU.

Ensuring that the rules are targeted, proportionate and administrable

We call on the EU Commission to reduce the heavy and resource-intensive administrative burden this initiative will bring for genuine and compliant businesses. This should be a key priority to ensure a targeted scope, uniform transposition and application of the EU Proposal by Member States (hereafter “MS”), so as to limit the increase of compliance costs, administrative burden and legal uncertainty for taxpayers and MS’ tax administrations alike.

In order to ensure that the rules are targeted, proportionate and administrable, all quantitative and qualitative criteria relied upon in the EU Proposal (whether in the gateway tests, carve-outs or otherwise), have to be clear and easy to apply. By way of example, the exemption provided in Article 10 of the EU Proposal is too broad and generic, which makes it almost impossible to apply.

More generally, we are calling for additional definitions and clarifications of the various provisions and concepts of the EU Proposal in order to ensure a smooth and consistent application by all MS, as well as to increase legal certainty for taxpayers. This would be the case, for instance, of Article 6 (1) (c) of the EU Proposal which would require further guidance on the concepts of “outsourcing of decision-making on significant functions” and “outsourcing of administration of day-to-day operations”.

In addition, we stress that any direct or indirect retroactive effect must be avoided. This would require, in particular, a reworking of Article 6 of the EU Proposal which currently provides for a 2-year look-back period.

Finally, we call on the EU Commission to elaborate on fast-track procedures according to which taxpayers should be able to appeal in a timely manner against decisions taken by MS’ tax administrations (e.g., denial of tax residency certificates, denial of exemption and/or rebuttal).

Removing barriers to cross-border investments in the single market

We call on the EU Commission to further consider whether the various provisions of the EU proposal are fully in line with EU law principles and, in particular, with the proportionality principle. Furthermore, we stress that this EU Proposal should be better integrated with other initiatives of the EU Commission to complete the Capital Markets Union and to promote a true European market that encourages cross-border investments.

Indeed, we are concerned that the general functioning of the current EU Proposal may prevent non-shell entities to obtain tax residency certificates in a timely manner (even in situations where taxpayers do not pass the gateway tests of Article 6 (1), including because they benefit from one of the carve-outs of Article 6 (2) of the EU Proposal). We also point out that the current procedures and timing foreseen in the EU Proposal will significantly increase the administrative burden and compliance costs for taxpayers and tax administrations alike.

We therefore strongly recommend rethinking the EU Proposal to address these concerns. In particular, we call on the EU Commission to include, in the EU Proposal, a mechanism to secure the timely issuance of tax residency certificates for taxpayers that are not subject to the minimum substance requirements (i.e., because they do not pass the gateway tests).

If the above issues are not properly taken into consideration, we fear that the EU Proposal would prevent compliant and genuine EU businesses from benefiting from relief at source on interest, royalties or dividends and would create additional barriers to cross-border investments and free movements of capital. This could ultimately be detrimental to the EU's competitiveness compared to third countries.

Ensuring an international level playing field

We stress that the EU Commission should aim at modernizing the European tax system by creating coordinated rules which will apply consistently on a worldwide basis to protect the MS' competitiveness and improve the international level playing field.

However, we are concerned that the current EU Proposal would be detrimental to this objective if it is implemented and applied before equivalent substance requirements (and related tax consequences) for entities located outside the EU are enforced. Furthermore, an EU standalone implementation of the new rules would be neither commensurate nor appropriate considering the fact that the EU tax framework already contains various layers of anti-abuse rules targeting abuse of tax treaties, domestic tax legislation and EU Directives.

We therefore point out that the current EU Proposal should only be implemented after or concomitantly with the equivalent rules for entities located outside the EU. In this respect, we invite the EU Commission to bring this topic for discussion at OECD level in the context of the ongoing BEPS work, which would ensure a harmonised application of these new rules at international level.

Ensuring a proportionate framework for group companies and investment funds alike

According to the current design of the EU Proposal, most of the criteria should be analysed on a standalone (entity-by-entity) basis. We stress the need to adapt the EU Proposal to the business rationale, operating models and specificities of group companies and investment funds. In this respect, an approach that considers activities carried on by personnel of a related party (including, in the case of funds, entities that are controlled by the same fund manager and that would not currently meet the definition of “associated enterprise”) as not constituting “outsourcing” (possibly limited to activities carried on in the same jurisdiction) would be more appropriate in determining which entities are at risk. This would allow taking into consideration how companies active in different sectors operate in practice for pure operational, legal and commercial reasons, while maintaining the effectiveness of the rules.

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About UEL:

UEL (Union des Entreprises Luxembourgeoises) is the Luxembourg Employers’ Association. UEL represents the Luxembourg private-sector businesses, except for the primary sector, and includes the Grand Duchy’s professional chambers and employer federations.

UEL works for a sustainable and prosperous economy for Luxembourg, its inhabitants and those who work there. It endeavors to provide an economy that is attractive to both investors and talented individuals.

To accomplish its mission, UEL facilitates working groups and discussions with its member organizations on major inter-branch topics. It is thereby able to present joint positions to the public authorities and social partners on these topics which they can then review together.

The initiatives launched by UEL are based on the values of the social market economy, sustainable development, business ethics, good governance and dialogue.