

ability to move in some cases “from unanimity to qualified majority voting in the council and co-decision — which the European Parliament has strongly pleaded for — must be a priority for the future,” he said.

“It was only as a member of the European Parliament that I learned how many European initiatives, sometimes really great initiatives, often called for and supported by the European Parliament, died a silent death in council,” Paul Tang, chair of the EP’s subcommittee on tax matters, said during a keynote speech. His colleague, EP Vice President Othmar Karas, called for the end of the tax veto and said that in the tax area, the EU needs more regulations, not directives. Regulations do not have to be transposed by member states, which prevents delays and differences in implementation. ■

Broad Legal Interpretation Could Test Unshell, AG Kokott Says

by Sarah Paez

There are potential legal issues with the European Commission’s proposed Unshell directive, including the expanded interpretation of a treaty article to justify new reporting obligations, a Court of Justice of the European Union official said.

Advocate General Juliane Kokott said the commission should consider how the usage of article 115 of the Treaty on the Functioning of the European Union — which provides the legal basis for Unshell — has shifted over the years from removing obstacles for the freedom of establishment and movement to ensuring effective tax collection by member states, and whether the latter remains a legally defensible position. Kokott was speaking at an October 25 panel at the annual Congress of the International Fiscal Association in Cancun, Mexico.

The Unshell proposal, which tackles the misuse of shell entities for tax abuse, is the subject of intense debate among member states in the EU Council. The Spanish presidency likely won’t have an agreement on the Unshell proposal by the November 14-15 meeting of the Economic and Financial Affairs Council, but it hopes to reach a final agreement on the directive “as soon as possible,” according to María José Garde, chair of the EU Code of Conduct Group (Business Taxation), who spoke at the panel.

Most EU member states have told the council they are open to changing the commission’s Unshell proposal into an information exchange requirement, something that the Spanish presidency had laid out in an October 4 high-level working party on taxation meeting. The change calls for a two-step approach that would turn the Unshell proposal into an amendment to the directive on administrative cooperation (DAC) adding a requirement for member states to exchange information on shell entities, and allow member states to decide in the future if tax consequences should be introduced.

While member states agree on the goal of the Unshell proposal to fight tax evasion, there are lingering disagreements over determining and establishing economic substance criteria, the

severity of tax consequences, and tax residence activity, Garde said. Member states are concerned about breaking down internationally accepted standards for fighting tax abuse and evasion and want the solution to comply with existing commitments to fight tax abuse. Some member states have expressed concerns that parts of the Unshell directive could negatively interact with domestic antiabuse rules, she said.

Member states also want to limit the administrative burden of the proposed directive for both taxpayers and tax administrations, Garde said. The lack of a legal definition of what constitutes a shell entity in the EU has presented challenges to establishing criteria for identifying suspicious entities, she said.

Benjamin Angel, director of direct taxation at the commission's Directorate General for Taxation and Customs Union, confirmed to *Tax Notes* that the commission will not refile the Unshell proposal to include only exchange of information.

"The idea of having a mere exchange of information is indeed not what we proposed," Angel told *Tax Notes* in an email. "Incidentally, it was also tested and did not gather consensus. So, we are still working with the presidency on a compromise that will refine further the [substance] test and foresee tax consequences."

Kokott also said the commission should consider whether the proposed directive's antiavoidance and antiabuse measures and enhanced reporting obligations for companies and intermediaries are still covered by the provision in article 115 concerning the harmonization for approximation of laws in member states that directly affect the functioning of the internal market.

"For abuse prevention, the OECD, EU, and states now focus on those extensive reporting obligations," Kokott said. "And these reporting obligations are becoming so detailed and comprehensive that it is sometimes difficult to know who is under what reporting obligation or what exactly needs to be reported, and this imposes considerable burdens on enterprises and intermediaries — and also risks — because violation of those not-always-clearly-defined reporting obligations are subject, according to the directives, to 'effective, proportionate and dissuasive' penalties."

The CJEU has already declared invalid some reporting obligations introduced in DAC6 that infringed on lawyers' professional privilege, Kokott said. In *Flemish Bar Association v. Belgium*, C-694/20, the Court held that article 8ab(5) of DAC6 partially violates article 7 of the Charter of Fundamental Rights of the European Union. The issue, according to the Court, was that the DAC6 provision requiring attorneys acting as intermediaries in cross-border tax planning arrangements to notify other intermediaries of their reporting obligation violates legal professional privilege.

Kokott said that *Flemish Bar Association* and other CJEU case law show that it may be up to the Court to help find a balance between freedom of establishment of taxpayers and the need for tax administrations to collect taxes effectively.

Angel said during the panel that one of the challenges to getting the Unshell directive over the finish line is that the commission is coming up with all new rules — not rules based on OECD guidance or agreements — to curtail tax abuse. The commission also regularly assesses its legislation, he said. The OpenLux investigation — which in 2021 used the Luxembourg beneficial ownership register to find that 81 percent of over 16,000 regulated investment funds in the country did not declare any beneficial owners — revealed that the EU still has much work to do to curtail the misuse of shell entities, despite the general antiabuse rule, which is used sparingly by member states, Angel said.

"What Unshell is trying to do is to equip a member state with a way to identify, ex ante, the shell companies, rather than ex post via general antiabuse rules," Angel said. ■