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YOUR GLOBAL TAXPERTS

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ATAD 3 (Unshell-Directive) and Abuse

...in the light of the Austrian Administrative Court's jurisdiction

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ATAD III ("Unshell-Directive")

Objective of the EU-proposal

- **Mitigate the misuse of shell companies** with limited or no economic activity
- **Limit tax advantages** they could use under EU-Directives and/or Tax Treaties and **allocation of income to the shareholder**
- **Minimum substance test** – three gateways
 - No substantial real business activity
 - Substantial cross border activities
 - Outsourcing of day-to-day operations to third parties
- If an undertaking **passes all three gateways evidence to be provided in the tax return**
 - That the entity **owns premises** or premises for their **exclusive use** and
 - holds at least one own and **active bank account** in a Member State and
 - has engaged **qualified, authorized and independent management** and/or employees who are resident close to the undertaking's residence

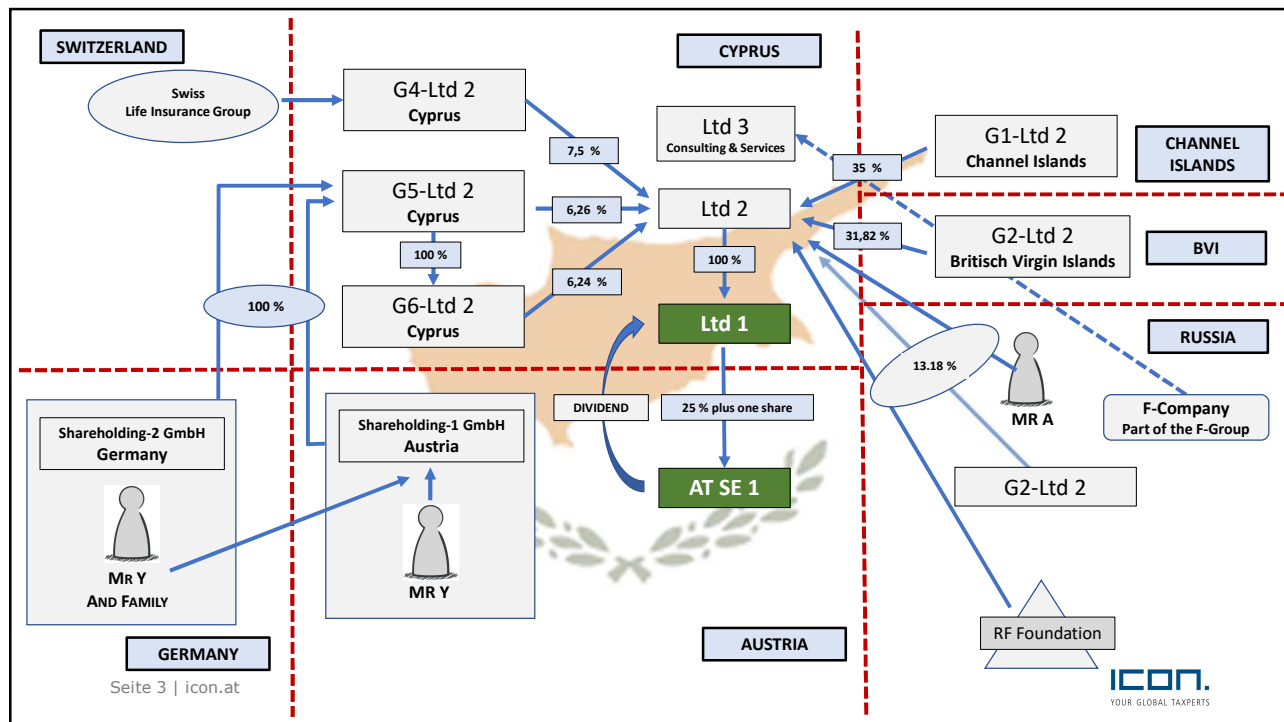
ATAD III tries to define the standards developed by the ECJ for the assumption of abusive interposition of conduits...
....similar to the Austrian Supreme Administrative Courts decisions!



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Refusal of Withholding Tax Relief

VwGH 23.3.2023, Ra 2022/15/0050-10

The Administrative Court's testing scheme:

1. Does the shareholder **conduct an own economic activity**?
2. Are there any **economic or other significant non-tax reasons** for the interposition of the Cyprus holding company?
3. Would the shareholders of the Cyprus holding company **by themselves be entitled to benefit from the withholding tax exemption** provided for in the parent-subsiary directive?

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Refusal of Withholding Tax Relief

Conducting an own economic activity

- **Holding shares is not an „economic activity“**
- **Outsourcing of functions to group entities per se is not harmful, however**
 - Expansion of the Russian market through activities of Ltd 1 could not be substantiated
 - No proof that activities have been transferred to and executed b group companies
 - No written transfer pricing agreements, no arm's length remuneration
 - No information about the individuals managing Ltd 1, Ltd 2 and Ltd 3
 - It could not be proven, that the companies had carried out any activity
 - One expense item for management fees in FJ 2017 only
 - No evidence that Non-arm's length and underprized services have been provided
- **Reference to ECJ decisions**
 - ECJ 26.2.2109, C-115/16 *N Luxembourg 1*, C-118/16 *X Denmark* and C-119/16 *C Denmark*
 - „Substance“ requires to consider aspects like management, financial statements, cost structure, activities actually performed, employees, office facilities and the entities' organisation

Refusal of Withholding Tax Relief

Economic or other significant non-tax reasons

- **Special Purpose Vehicle** was not required for purchasing shares
- **Professionalization and optimisation of the group structure** was not visible
 - Ltd 1 did not hold more than one subsidiary
 - No business-related relevant functions have been performed by Ltd 1, Ltd 2 and Ltd 3
- **Unclear intercompany service relationship**
- **Advantage of using CY as a recognized international location of holding companies** (English language, professionals in CY, favourable legal environment etc.) was not comprehensible in the subject case
 - Active subsidiaries hat its residence in Austria, Russia and Eastern Europe
- **Accumulation of profit distributions** in CY cannot replace missing economic reasons

Refusal of Withholding Tax Relief

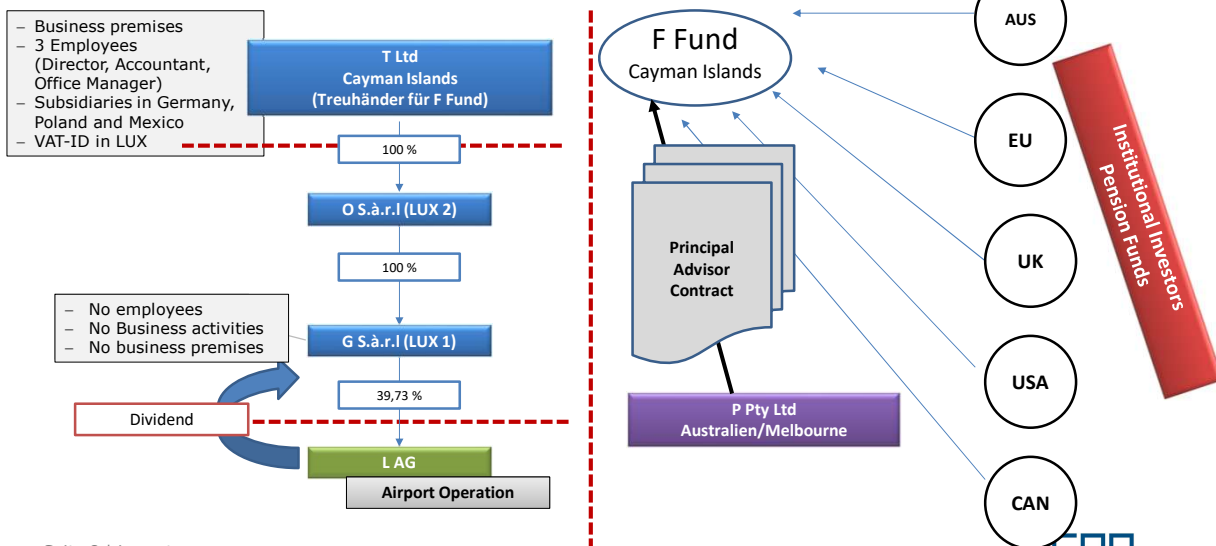
Shareholders of the parent entity not entitled to tax relief

- **Shareholders of the holding company in CY have**
 - deemed to be resident outside the European Union (mainly in Russia) and
 - would not have been entitled to the benefits of the EU-Parent-Subsidiary Directive, if they would have directly received the dividends
- **All the CY companies involved have been held by non-EU-country shareholders**
- **Austrian Tax Authorities are required**
 - to identify whether a shareholder is entitled to the benefits of the Parent-Subsidiary Directive
- **Austrian Tax Authorities are not required**
 - to identify the actual beneficiary
 - are not required to apply possible treaty benefits

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Comparability with the LUX-judgement?

VwGH 27.3.2019, Ro 2018/13/0004



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Comparability with the LUX-judgement?

VwGH 27.3.2019, Ro 2018/13/0004

- Activities of LUX 1 have been performed by LUX 2 based on an **arm's length Service Agreement**
- LUX 2 had sufficient substance
- **Good business reasons** for interposition of LUX 1
 - Pooling of investments by divisions, regions and business fields...
 - ...through several third parties in order to invest in infrastructure projects
 - No involvement of third parties in the CY-case
- **Own economic activity & Sufficient economic and other reasons**
 - An economic reason may not only exist if the desired goal cannot be otherwise achieved but may also exist if the goal can be achieved better and more safely by means of a design.

Holding Companies

Requirements to achieve withholding tax relief?

- ATAD III and judgements **sheds some light on "substance requirements"**
- Economic reasons for interposing conduits have to be **remarkable, reasonable, sound** and **understandable**
- Following reasons have not been accepted by established case-law as **"non-tax-reasons"** excluding the application of abuse of law provisions
 - Access to an international financial center
 - Good location for further investments
 - Separation of activities (within the same group)
 - Advantageous trade and regulatory framework
 - Attractive and simple foundation rules
 - Access to recognized experts, Language
 - Pooling of dividends and simplification of distribution policy
- **Requirement of "own economic activity" still unclear!**