

Corporate tax: hybrid mismatches with third countries

2016/0339(CNS) - 25/10/2016 - Legislative proposal

PURPOSE: to adopt new measures to end the exploitation, in the existing differences ('hybrid mismatches') between the tax systems of Member States and those of third countries, by corporations in order to avoid tax.

PROPOSED ACT: Council Directive.

ROLE OF THE EUROPEAN PARLIAMENT: Council may adopt the act only after consulting Parliament and with the approval of the latter.

BACKGROUND: [Council Directive \(EU\) 2016/1164](#) laying down rules against tax avoidance practices provides for a framework to tackle hybrid mismatch arrangements. These arrangements exploit differences in the tax treatment of an entity or instrument under the laws of two or more tax jurisdictions to achieve **double non-taxation**. These types of arrangements are widespread and result in a substantial erosion of the taxable bases of corporate taxpayers in the EU.

The hybrid mismatch rules in the Council Directive laying down rules against tax avoidance practices address the most widespread forms of hybrid mismatches, but only within the EU.

However, taxpayers in the EU engaged in cross-border structures involving third countries also take advantage of hybrid mismatches to reduce their overall tax liability in the EU.

Therefore, the Commission feels it necessary that **hybrid mismatches involving third countries should be countered as well** in order to neutralize hybrid mismatch arrangements.

The Organisation for Economic Co-operation and Development (OECD) has issued concrete action recommendations in the context of the initiative against Base Erosion and Profit Shifting (BEPS). In June 2016, the Council requested the Commission to put forward a proposal on hybrid mismatches involving third countries in order to provide for rules consistent with the rules recommended by the OECD on BEPS.

This proposed directive is part of a package that also includes the re-launch of [the proposal](#) for a common consolidated corporate tax base (CCCTB) and [a proposal](#) on a common corporate tax base (CCTB).

CONTENT: the proposal put forwards an amendment of the Anti-Tax Avoidance Directive. It sets out legally binding rules to enable Member States to effectively tackle hybrid mismatch arrangements that are not dealt with in the Anti-Tax Avoidance Directive. This Directive has the same scope as the Anti-Tax Avoidance Directive and thus aims to capture all taxpayers which are subject to corporate tax in a Member State.

The proposed directive establishes **rules to combat hybrid mismatches with third countries**. The new rules are limited to providing a remedy for cases of double deduction, of a deduction of a payment from the taxable base in one jurisdiction without a corresponding inclusion of that payment in the taxable base of a taxpayer in another jurisdiction.

Furthermore, the proposal includes new rules on:

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hybrid mismatches involving permanent establishments, both in their intra-EU and third-country dimension: a hybrid permanent establishment mismatch between two jurisdictions occurs where the business activities in a jurisdiction are treated as being carried on through a permanent establishment by one jurisdiction, while those activities are not treated as being carried on through a permanent establishment by another jurisdiction;

- **hybrid transfers:** this is an arrangement to transfer a financial instrument where the laws of two jurisdictions differ on whether the transferor or the transferee has got the ownership of the payments on the underlying asset;
- **imported mismatches:** these flow from arrangements involving group members, or structured arrangements in general, which shift the effect of a hybrid mismatch between parties in third countries into the jurisdiction of a Member State through the use of a non-hybrid instrument. A mismatch is imported in a Member State if a deductible payment under a non-hybrid instrument is used to fund expenditure under a structured arrangement involving a hybrid mismatch between third countries. This implies a flow of revenue out of the EU which is eventually not taxed;
- **dual resident mismatches:** this may result in a double deduction outcome if a payment made by a dual resident taxpayer is deducted under the laws of both jurisdictions where the taxpayer is resident.