

Anti-Tax Avoidance Directive
Implementation of measures to
counter hybrid mismatch
arrangements

January 2022



Scope

This document provides insights on the impact and implementation of measures to counter hybrid mismatch arrangements in the [EU Directive 2017/952, amending Directive 2016/1164](#) (ATAD 2) into the domestic legislation of the EU member states.

This slide deck is a high level overview of the rules and should not be relied on as tax advice. The surveys used to prepare this deck included certain assumptions, so the actual facts and circumstances should be evaluated on a case-by-case basis.

The survey questions were framed in the context of the choices individual EU member states made or are expected to make, and responses are based on developments known as of January 2022. The responses reflect the views of Deloitte tax professionals to the extent they are aware of relevant developments in their jurisdictions.

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Introduction—ATAD measures to counter hybrid mismatch arrangements

- The ATAD is part of the [Anti-Tax Avoidance Package](#) that was presented by the European Commission in January 2016. The directive, formally adopted by the Economic and Financial Affairs Council of the EU on 12 July 2016, aims to provide a minimum level of protection for the internal market and ensure a harmonized and coordinated approach in the EU to the implementation of some of the recommendations under the [OECD BEPS project](#). The ATAD provides for the minimum harmonization of rules in the areas of controlled foreign corporations, hybrid mismatches, and interest deductions, and requires the introduction of a corporate general anti-abuse rule (GAAR) and an exit tax (the latter two measures are not part of the BEPS project).
- Hybrid mismatches are the consequence of differences in the legal characterization of payments (financial instruments) or entities that arise as a result of the interaction between the legal systems of two jurisdictions. The effect of such mismatches is often a double deduction (i.e., a deduction of the same expenses in more than one jurisdiction) or a “deduction without inclusion” (i.e., a deduction of the income in one state without the inclusion of the income in the tax base of the other state).
- The [EU Anti-Tax Avoidance Directive 2016/1164](#) (ATAD 1) contains measures to counter hybrid mismatch arrangements in situations where there are differences in the legal characterization of payments or entities between EU member states such that a double deduction or a deduction without inclusion arises. The deductibility of such payments is addressed in article 9 of ATAD 1:
 - In the case of a double deduction, a deduction is allowed only in the state of source of the payment; and
 - In the case of a deduction without inclusion, a deduction will not be allowed.
- ATAD 2, which amends ATAD 1, was adopted by the EU Council on 29 May 2017. In line with the recommendations outlined in the OECD BEPS report on action 2 (“[Neutralising the Effects of Hybrid Mismatch Arrangements](#)”), ATAD 2 expands the definition of a hybrid mismatch from a mismatch resulting from a double deduction or deduction without inclusion due to differences in legal characterizations in intra-EU situations to situations between EU member states and third countries (i.e., non-EU member states). ATAD 2 also introduces more detailed rules to neutralize hybrid mismatches and includes measures that address types of hybrid mismatches that do not fall within the scope of ATAD 1, such as hybrids involving permanent establishments (PEs), dual resident mismatches, imported mismatches, and reverse hybrids (article 9).
- The more extensive anti-hybrid rules in ATAD 2 replace the initial rules to counter hybrid mismatch arrangements in ATAD 1. Consequently, the ATAD 1 anti-hybrid rules no longer have to be implemented into the domestic law of the member states (even though some member states already have introduced such rules).

An example of a hybrid mismatch that is addressed by ATAD 1 would be a payment from country B to country A where country A treats the payment as a dividend (not taxed) and B treats the payment as interest (deductible).

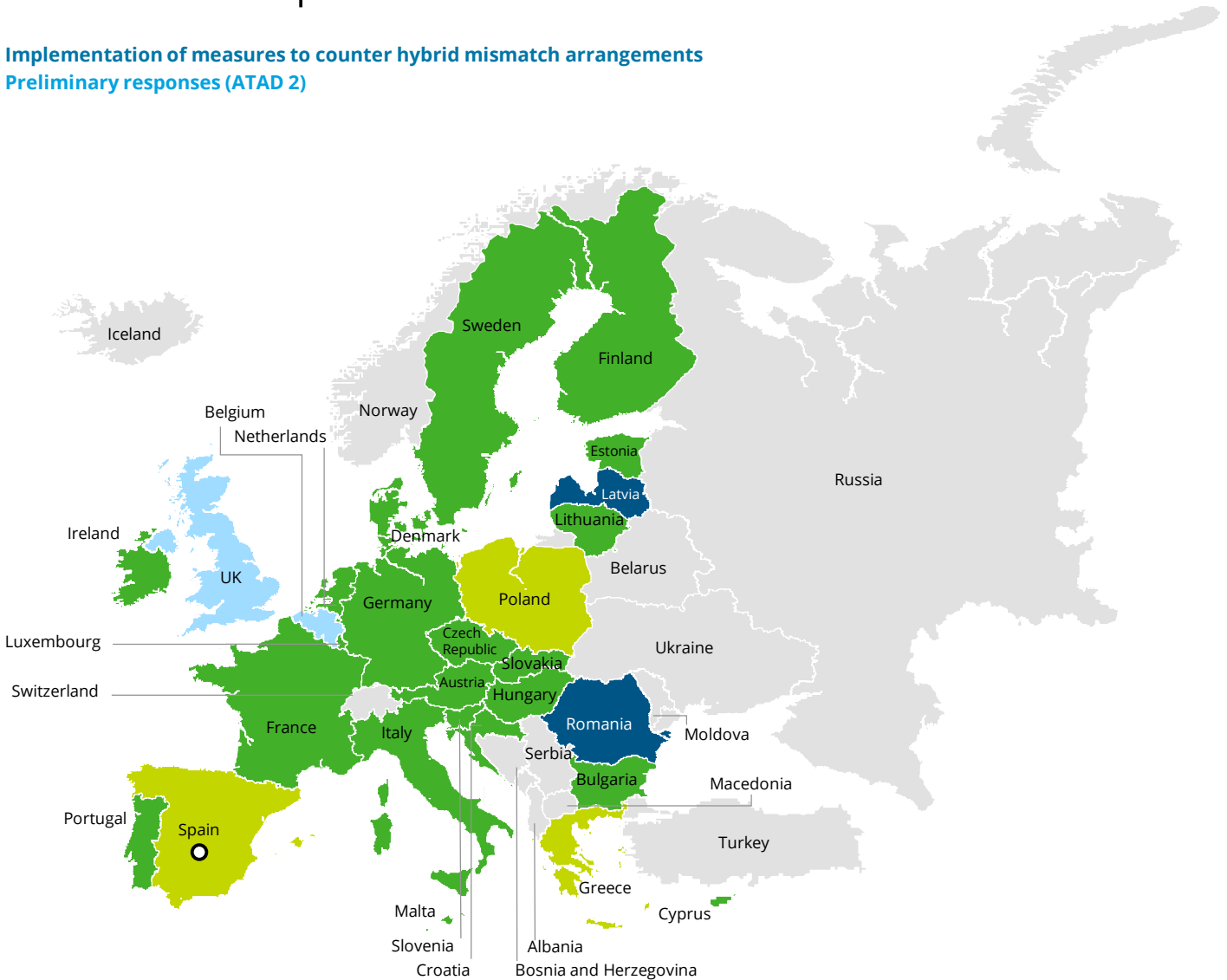
- ATAD 2 requires EU member states to implement rules that address the following types of arrangements:
 - A payment under a financial instrument that gives rise to a deduction without inclusion (including “hybrid transfers” where the underlying return on the transferred financial instrument is treated as derived simultaneously by more than one of the parties to the arrangement (e.g., certain repo transactions));
 - A payment to a hybrid entity that gives rise to a deduction without inclusion, and this mismatch arises due to differences in the allocation of the payment under the laws of the jurisdiction where the hybrid entity is established and the jurisdiction of any person with a participation in the hybrid entity;
 - A payment to an entity with one or more PEs that gives rise to a deduction without inclusion as a result of differences in the allocation of payments between the head office and a PE or between two or more PEs;
 - A payment that gives rise to a deduction without inclusion as a result of a payment to a disregarded PE;
 - A payment by a hybrid entity that gives rise to a deduction without inclusion and that mismatch arises because the payment is disregarded under the laws of the payee jurisdiction;
 - A deemed payment between a head office and a PE (or between two or more PEs) that gives rise to a deduction without inclusion and that mismatch arises because the payment is disregarded under the laws of the payee jurisdiction;
 - Situations with double deduction outcomes regardless of whether they arise as a result of payments, expenses that are not treated as payments under domestic law, or amortization or depreciation losses;
 - A payment made by a dual resident taxpayer that is deducted under the laws of both jurisdictions where the taxpayer is resident; and
 - A payment made to an intermediary that is not taxable on receipt due to a hybrid effect.
- ATAD 2 applies only where there is a sufficient “connection” between the parties. As a result, it applies to hybrid mismatches that arise between the taxpayer and its associated enterprises or between associated enterprises; hybrid mismatches that arise between a head office and a PE or between two or more PEs of the same entity; and mismatches resulting from a structured arrangement involving a taxpayer.
- The term “associated” generally covers direct and indirect interests of 25% or more (although the percentage is increased to 50% for certain types of mismatches). In addition, in certain situations, the directive deems the parties to be associated.

- The ATAD 2 provisions will neutralize arrangements through the disallowance of a deduction, the inclusion of income, or a limitation of tax relief at source. Most anti-hybrid provisions contain a primary rule and a secondary rule, i.e., the primary rule is that a tax deduction should be disallowed for a payment/expense and the secondary rule is that income should be taxed (e.g., where a non-EU country does not disallow a deduction). In principle, the primary rule is to be applied, but if that rule is not followed, the secondary rule is to be applied. This effectively results in an EU member state always resolving the hybrid mismatch where the third country has not done so. ATAD 2 allows a member state to decide not to apply the secondary rule, i.e., to decide not to require the income to be taxed for certain mismatches resulting in a deduction/non-inclusion, in particular for:
 - Payments to a hybrid entity resulting in allocation differences;
 - Payments to an entity where a mismatch results from allocation differences between a head office and a PE;
 - Payments to a disregarded PE; and
 - Deemed payments between a head office and a PE or between PEs and the payment is disregarded in the payee's jurisdiction.
- If the character of a payment under a hybrid instrument qualifies it for double tax relief under the laws of the payee jurisdiction, such as an exemption from tax, a reduction in the rate of tax, or a credit or refund of tax, the payment should be treated as giving rise to a hybrid mismatch to the extent of the resulting undertaxed amount.
- Situations can arise where there is a hybrid mismatch arrangement between two countries without anti-hybrid rules and the benefit of that tax mismatch is transferred or "imported" to a third country using an arrangement that does not give rise to a hybrid mismatch. ATAD 2 includes rules to neutralize such imported mismatches and requires member states to disallow a deduction for any payment that directly or indirectly funds a hybrid mismatch through a transaction or series of transactions.
- EU member states should use the applicable explanations and examples in the OECD BEPS action 2 report to aid in the interpretation of the directive (to the extent those are consistent with the provisions of ATAD 2 and EU law).
- The simplified anti-hybrid rules under ATAD 1 had to be implemented into domestic tax law by 31 December 2018 and applied as from 1 January 2019. As noted above, the more extensive anti-hybrid rules introduced by ATAD 2 replace the initial rules to counter hybrid mismatch arrangements that were set out in ATAD 1; thus, the ATAD 1 anti-hybrid rules no longer have to be implemented into domestic law (although some member states did so). EU member states had until 31 December 2019 to transpose the ATAD 2 provisions into national law so that the rules apply by 1 January 2020 (except for reverse hybrid rules, which must be transposed into domestic law by 31 December 2021 and applicable by 1 January 2022). EU member states are permitted to adopt the measures at an earlier date if they wish to do so.

- Not all EU member states fully transposed the ATAD 2 into their domestic law by 31 December 2019. If a member state fails to comply with EU law, the European Commission may open an infringement procedure, and if necessary, it may bring the case before the Court of Justice of the European Union. The European Commission initially launched infringement procedures against seven member states for failure to fully/correctly implement the directive.
- Some EU member states already had rules to counter hybrid mismatch arrangements before the ATAD was adopted. It should be noted that EU directives set a minimum level of protection that EU member states are required to implement but they are free to introduce or retain rules that are more stringent than the rules prescribed in the directives, provided the rules do not otherwise offend EU law. As a result, where a member state already has rules to counter hybrid mismatch arrangements, those rules have to be amended to the extent they do not meet the minimum requirement prescribed by the ATAD. Rules that are stricter than the ATAD measures do not have to be modified.
- The UK withdrew from the EU on 31 January 2020 and following the end of the EU-UK withdrawal agreement's transition period on 31 December 2020, EU law generally no longer applies to the UK. However, as the UK was a member state at the time of ATAD 2, and was subject to obligations for the timely transposition of the ATAD 2 into domestic law, this slide deck continues to comment on the status of the anti-hybrid rules under UK domestic law. Changes to EU law (e.g., revisions to the Directive) with an implementation date on or after 1 January 2021 will not result in an obligation for the UK to make changes to its domestic law.

ATAD 2 implementation

Implementation of measures to counter hybrid mismatch arrangements Preliminary responses (ATAD 2)



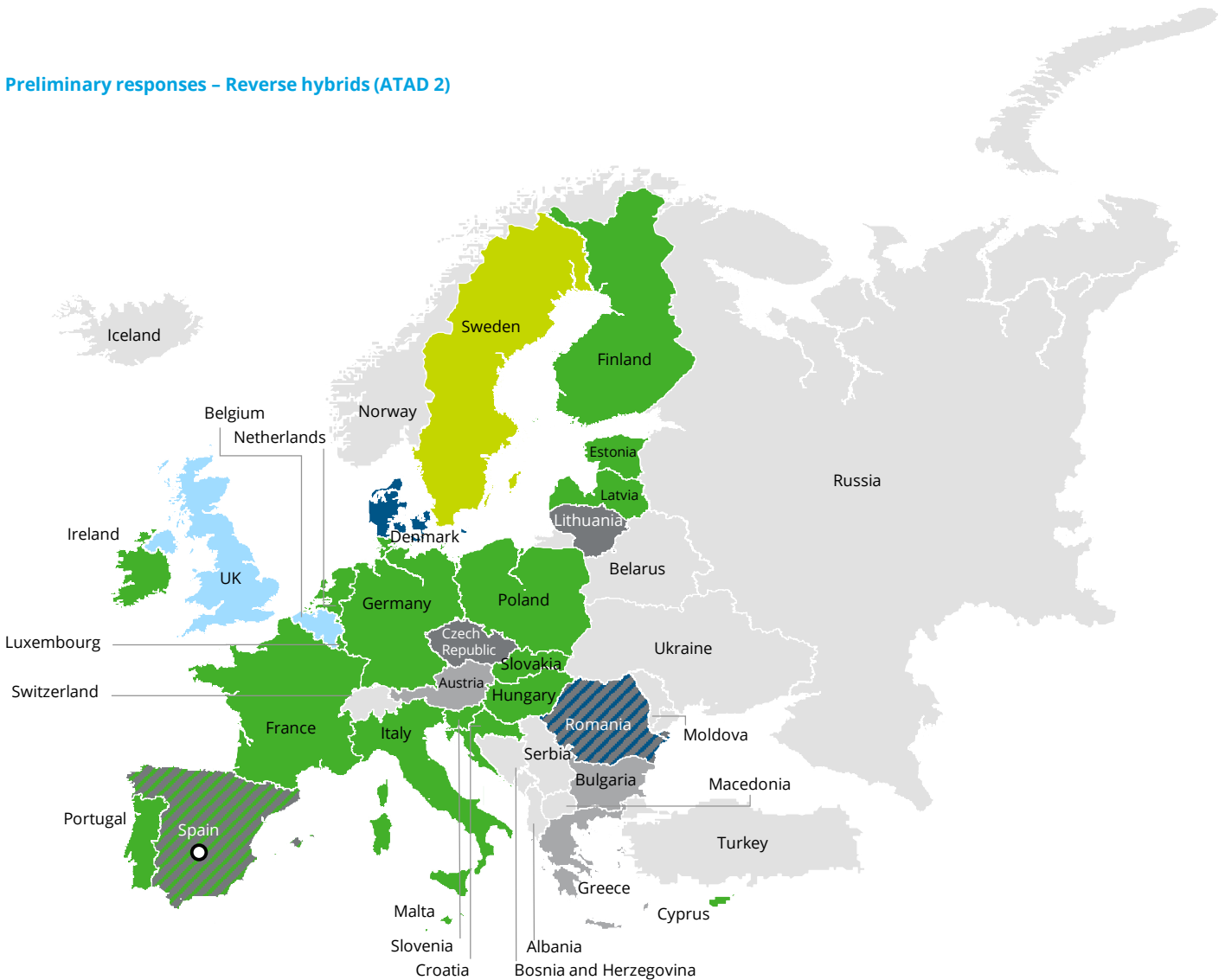
EU member states must apply the anti-hybrid measures in ATAD 2 as from 1 January 2020 but were permitted to adopt measures at an earlier date.

Legend:

- 2** ATAD 2 anti-hybrid rules already applied before 1 January 2020
- 21** ATAD 2 anti-hybrid rules apply as from 1 January 2020
- 2** ATAD 2 anti-hybrid rules apply as from 3 or 12 February 2020
- 3** ATAD 2 anti-hybrid rules apply as from 1 January 2021

○ The Spanish anti-hybrid rules are applicable to fiscal years beginning on, or after 1 January 2020 insofar as such fiscal years have not been concluded on the date of entry into force of the Spanish implementation law (11 March 2021). Therefore, for entities which fiscal year coincides with the calendar year, the anti-hybrid rules will be applicable as from 1 January 2021.

Preliminary responses – Reverse hybrids (ATAD 2)



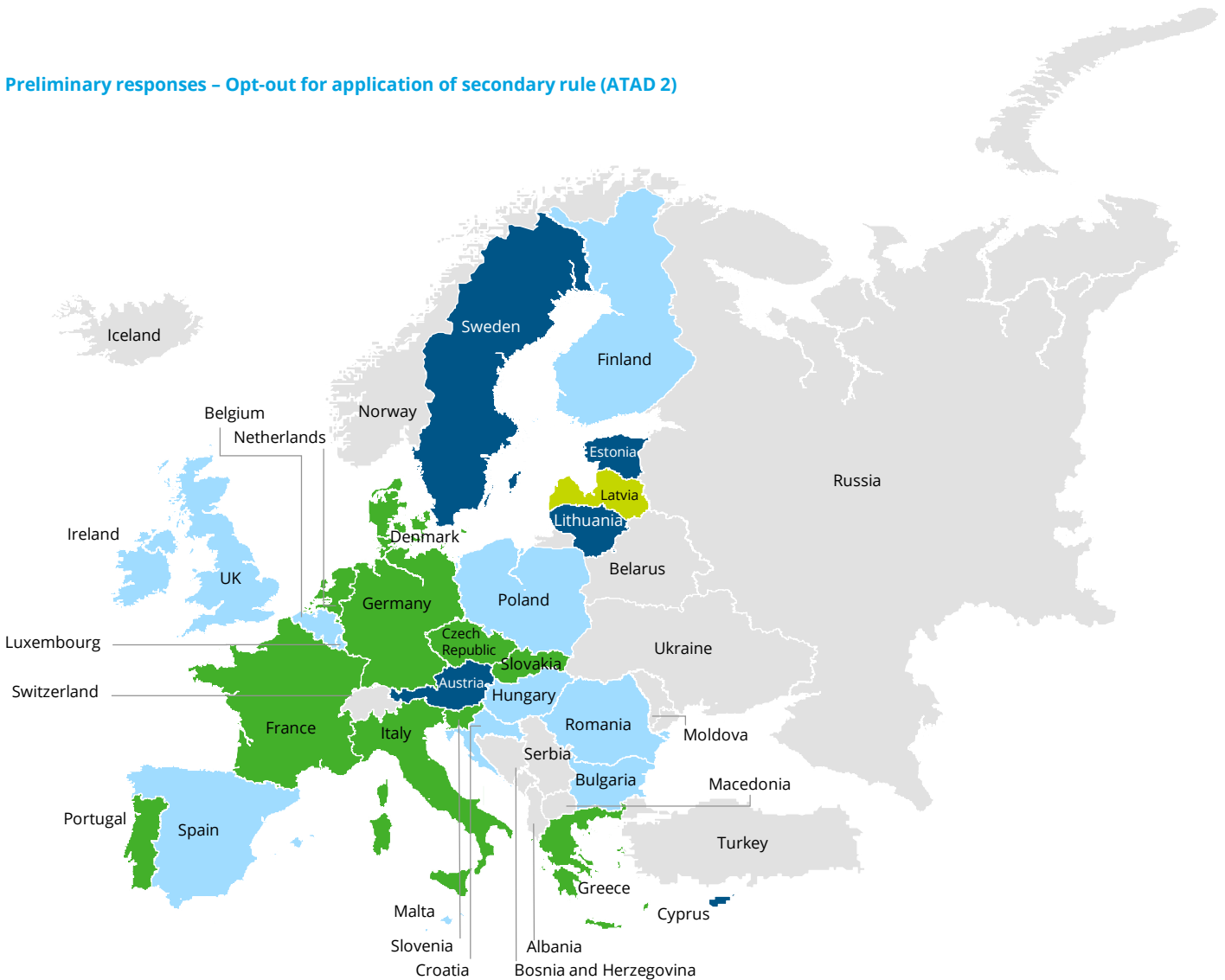
EU member states must apply the rules targeting reverse hybrid mismatches as from 1 January 2022 but were permitted to adopt measures at an earlier date.

Legend:

- 2 Rules countering reverse hybrids already applied before 1 January 2020
- 1 Rules countering reverse hybrids apply as from 1 January 2020
- 1 Rules countering reverse hybrids apply as from 3 February 2020
- 1 Rules countering reverse hybrids apply as from 1 January 2021
- 1 Rules countering reverse hybrids apply as from 1 July 2021
- 17 Rules countering reverse hybrids apply as from 1 January 2022
- 3 Not yet implemented
- 2 No rules countering reverse hybrids will be implemented

○ The Spanish anti-hybrid rules are applicable to fiscal years beginning on, or after 1 January 2020 insofar as such fiscal years have not been concluded on the date of entry into force of the Spanish implementation law (11 March 2021). Therefore, for entities which fiscal year coincides with the calendar year, the reverse hybrid rules will be applicable as from 1 January 2021.

Preliminary responses – Opt-out for application of secondary rule (ATAD 2)

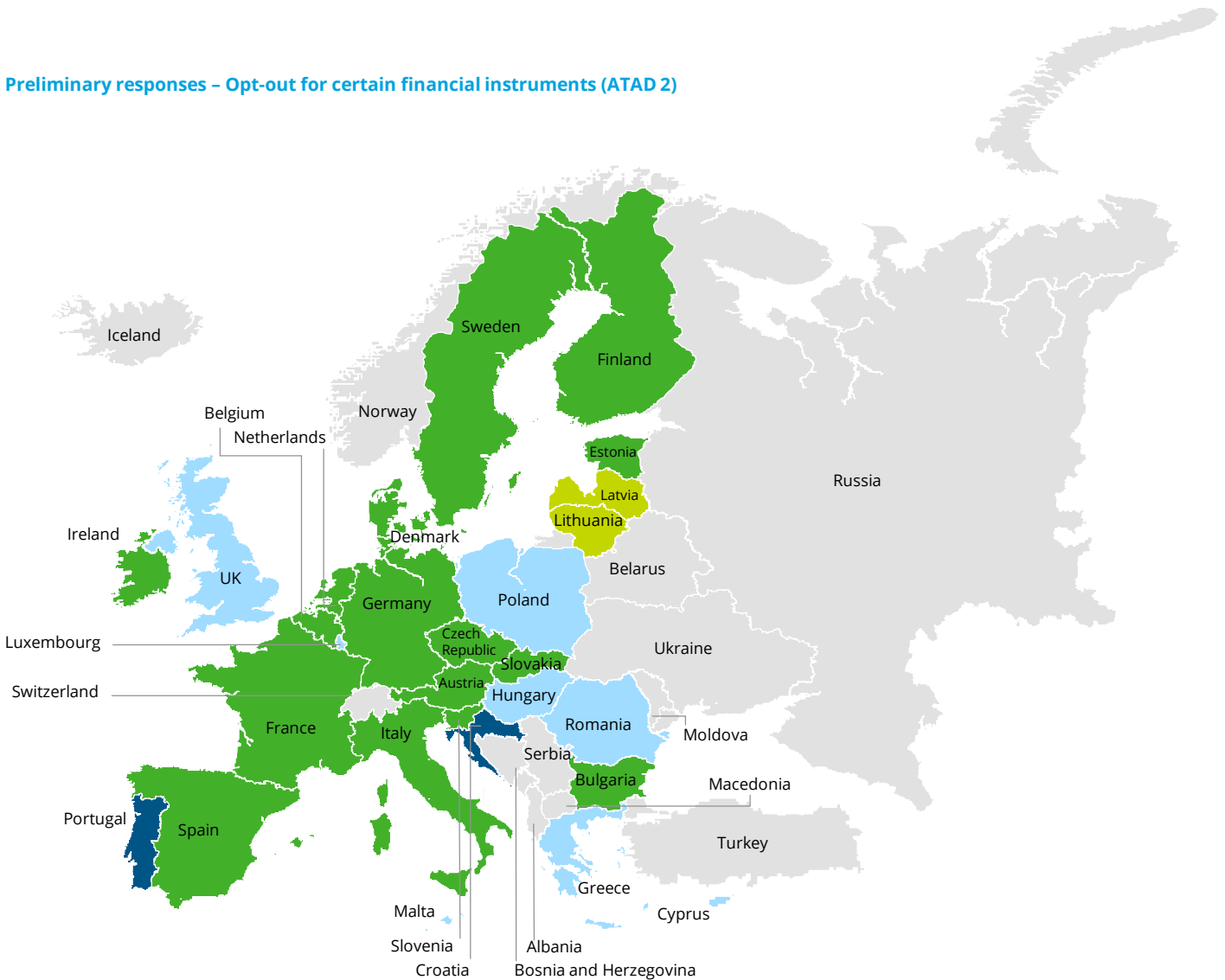


Article 9, paragraph 4, sub a of ATAD 2 allows a member state to decide not to apply the secondary rule, i.e., to decide not to require the income to be taxed for certain mismatches resulting in a deduction/non-inclusion, in particular for:

- Payments to a hybrid entity resulting in allocation differences;
- Payments to an entity where a mismatch results from allocation differences between a head office and a PE;
- Payments to a disregarded PE; and
- Deemed payments between a head office and a PE or between PEs, while the payment is disregarded in the payee's jurisdiction.

| Legend: | |
|---------|--|
| 12 | (Partial) application of opt-out |
| 5 | Potential (partial) application of opt-out |
| 10 | No opt-out |
| 2 | Potentially no opt-out |

Preliminary responses – Opt-out for certain financial instruments (ATAD 2)



Article 9, paragraph 4, sub b of ATAD 2 allows a member state to exclude certain financial instruments from the application of the anti-hybrid rules.

| Legend: | |
|---------|----------------------------------|
| 8 | Application of opt-out |
| 2 | Potential application of opt-out |
| 16 | No opt-out |
| 2 | Potentially no opt-out |



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