

# TABLE OF CONTENTS

---

Foreword .....	11
Abbreviations .....	13

## I. Introduction

1. Overview .....	17
2. Hybrid mismatch rules .....	17
<b>Scope of the hybrid mismatch rules</b> .....	17
<b>Tax treatment of hybrid mismatches</b> .....	18
3. Reverse hybrid mismatch rule .....	19

## II. The Hybrid Mismatch Rules

1. Overview .....	23
2. Scope of the hybrid mismatch rules .....	23
<b>2.1. Opening comments</b> .....	23
<b>2.2. Personal scope of application</b> .....	24
<b>2.3. Mismatch outcomes</b> .....	24
<b>2.4. Related party test</b> .....	26
2.4.1. Definition of associated enterprises .....	26
2.4.2. Aggregation of interests .....	27
2.4.3. Investments funds .....	29
<b>2.5. Hybrid mismatches</b> .....	34
2.5.1. Payments under a financial instrument .....	34
2.5.2. Payments to a hybrid entity .....	36
2.5.3. Payments to an entity with one or more PEs .....	38
2.5.4. Payments to a disregarded PE .....	39
2.5.5. Payments by a hybrid entity .....	40
2.5.6. Deemed payments between the head office and a PE .....	41
2.5.7. Double deductions .....	42

2.6. Hybrid transfers .....	43
2.7. Tax residency mismatches .....	44
2.8. Structured arrangements .....	45
2.9. Imported hybrid mismatches .....	48
2.10. Limits of the hybrid mismatch rules .....	51
3. Tax treatment of hybrid mismatches .....	58
3.1. Opening comments .....	58
3.2. Double deductions .....	59
3.3. Deductions without inclusions .....	60
3.4. Imported hybrid mismatches .....	62
3.5. Income derived through a disregarded PE .....	64
3.6. Tax residency mismatches .....	65
3.7. Hybrid transfers .....	65
4. Cooperation duties of the taxpayer .....	65
5. Checklists .....	66
1. Checklist: Related party test (Article 168ter (1) No. 18 of the LITL) .....	67
2. Checklist: Deduction without inclusion (D/NI) outcome (Article 168ter (1) No. 6 of the LITL) .....	68
3. Checklist: Payments under a financial instrument (Article 168ter (1) No. 2 a) of the LITL) .....	69
4. Checklist: Payments to a hybrid entity (Article 168ter (1) No. 2 b) of the LITL) .....	70
5. Checklist: Payments to an entity with one or more PEs (Article 168ter (1) No. 2 c) of the LITL) .....	71
6. Checklist: Payments to a disregarded PE (Article 168ter (1) No. 2 d) of the LITL) .....	72
7. Checklist: Payments by a hybrid entity (Article 168ter (1) No. 2 e) of the LITL) .....	73
8. Checklist: Deemed payments between the head office and a PE (Article 168ter (1) No. 2 f) of the LITL) .....	74
9. Checklist: Double deductions (Article 168ter (1) No. 2 g) of the LITL) .....	75
10. Checklist: Tax adjustments in case of double deductions (Article 168ter (3) No. 1 of the LITL) .....	76
11. Checklist: Tax adjustments in case of a deduction without inclusion (Article 168ter (3) No. 2 of the LITL) .....	77
12. Checklist: Structured arrangements (Article 168ter (1) No. 2 a) of the LITL) .....	78

### III. Impact of the Hybrid Mismatch Rules on Alternative Investments

1. Introduction.....	81
2. Typical Investment Structures.....	81
3. Scope and limits of the hybrid mismatch rules .....	83
<b>3.1. Overview</b> .....	83
<b>3.2. Mismatch outcomes</b> .....	84
<b>3.3. Most relevant hybrid mismatches</b> .....	88
3.3.1. Payments under a financial instrument .....	88
3.3.2. Payments to a hybrid entity .....	90
3.3.3. Payments by a hybrid entity.....	92
<b>3.4. Related party test</b> .....	93
3.4.1. Definition of associated enterprises .....	93
3.4.2. Aggregation of interests .....	94
3.4.3. Investments funds .....	95
<b>3.5. Limits of the hybrid mismatch rules</b> .....	102
4. Tax treatment of hybrid mismatches.....	105
5. Managing the impact of the hybrid mismatch rules .....	107
<b>5.1. Overview</b> .....	107
<b>5.2. Corporate fund vehicles</b> .....	108
<b>5.3. Corporate blockers</b> .....	109
<b>5.4. Interest-free debt funding</b> .....	111
6. Burden of proof.....	113
7. Checklists .....	114
<b>7.1. Checklist: Luxembourg funds as hybrid entities</b> .....	114
<b>7.2. Checklist: Hybrid mismatch rules in case of new funds –         The exclusion principle</b> .....	116

### IV. The Reverse Hybrid Mismatch Rule

1. Overview .....	119
2. Scope of the reverse hybrid mismatch rule.....	119
<b>2.1. Related party test</b> .....	119
<b>2.2. Aggregation of interests</b> .....	120
<b>2.3. Investments funds</b> .....	120
3. Tax treatment of reverse hybrid mismatches .....	122
<b>3.1. Corporate income tax</b> .....	122
3.1.1. Application of the reverse hybrid mismatch rule .....	122
3.1.2. Determination of the tax base of the reverse hybrid entity.....	123
3.1.3. Investment funds .....	126

3.2. Withholding tax .....	128
3.3. Municipal business tax .....	128
3.4. Net wealth tax .....	129
3.5. Transparency for tax purposes .....	129
4. Cooperation duties of the taxpayer .....	129
5. Checklists .....	130
5.1. Checklist: Scope of the reverse hybrid mismatch rule .....	130
5.2. Checklist: Application of the reverse hybrid mismatch rule .....	131

## V. Case studies

1. A group of companies .....	135
1.1. Payments under a financial instrument .....	135
1.2. Payments under a financial instrument II .....	136
1.3. Payment to a (reverse) hybrid entity .....	137
1.4. Payment by a hybrid entity .....	138
1.5. Payment to a disregarded PE .....	139
1.6. Double deductions .....	140
2. Alternative Investments .....	141
2.1. The Luxembourg private equity (PE) fund .....	141
2.1.1. Opening comments .....	141
2.1.2. The <i>de minimis</i> rule .....	142
2.1.3. Associated enterprises investing in the fund .....	145
2.1.4. Different investor profiles in the fund .....	146
2.1.5. The feeder fund .....	149
2.1.6. The corporate feeder fund .....	152
2.2. The foreign real estate fund .....	153
2.2.1. Opening comments .....	153
2.2.2. The <i>de minimis</i> rule .....	154
2.2.3. Investors with 10% or more investments .....	156
3. The investment partnership .....	158

## Appendix:

Appendix 1: Text of the law .....	163
Appendix 2: Unofficial translation of the text of the law .....	171
Appendix 3: Important definitions .....	177
Appendix 4: Anti-Tax Avoidance Directive 2 .....	179
Appendix 5: Final Report on BEPS Action 2 (Extract) .....	193