

## Amendments 17 to 42 to Clause 36 and Schedule 7: Hybrid and other mismatches

### Summary

1. These amendments to Clause 36 and Schedule 7 follow engagement with stakeholders since the publication of Finance (No. 2) Bill and will ensure the changes in this Bill have the intended effect, whilst also removing potential unintended consequences of the legislation

### Details of the amendments

2. Amendment 17 removes the amendment at Paragraph 2 to Schedule 7 of the Finance Bill 2021 which was to be made in relation to the definition of “hybrid entity” and “investor” at section 259BE of Tax (International and Other Provisions) Act (“TIOPA”) 2010. The deletion follows stakeholder engagement in which it became clear that the existing draft had unintended consequences. A revised provision dealing with the underlying issue is intended to be included in the next Finance Bill, with the same effective date.
3. Amendment 18 is relevant to Paragraph 6 of Schedule 7 and introduces replacement wording for new subsection 259NEF(3) TIOPA 2010 which make a minor clarification to the corporate rescue conditions outlined in that subsection.
4. Amendment 19 and Amendment 20 alter the order of wording in new subsection 259EC(7)(a) TIOPA 2010, introduced by Paragraph 11 of Schedule 7, for readability.
5. Amendments 21 to 26 all remove the words “or body” from text introduced by Paragraph 11 of Schedule 7 which provides for new subsections to section 259EC TIOPA 2010. The words “or body” are being removed to ensure consistency with existing provisions within Part 6A TIOPA 2010.
6. Amendment 27 introduces a new subsection 259EC(9A) TIOPA 2010, which follows from the introduction of other new subsections to 259EC TIOPA made by Paragraph 11 of Schedule 7. New subsection (9A) imports existing subsection 259B(5) of TIOPA 2010 into the new subsection 259EC(7)(b) to determine residence where no concept of tax residence exists.
7. Amendment 28 removes the words “or body” from new subsection 259EC(10) TIOPA 2010, which was introduced by Paragraph 11 to Schedule 7, to ensure consistency with existing provisions within Part 6A of TIOPA 2010.
8. Amendments 29 and 30 alter the order of wording in new subsection 259ICA(2)(a)

TIOPA 2010, introduced by Paragraph 13 of Schedule 7, for readability.

9. Amendments 31 to 36 all remove the words “or body” from text introduced by Paragraph 13 of Schedule 7 which provides for the insertion of new section 259ICA TIOPA 2010. The words “or body” are being removed to ensure consistency with existing provisions within Part 6A TIOPA 2010.
10. Amendment 37 introduces a new subsection (4A) to new section 259ICA TIOPA 2010, which was introduced by Paragraph 13 of Schedule 7. New subsection (4A) imports existing subsection 259B(5) of TIOPA 2010 into the new subsection 259ICA(2)(b) to determine residence where no concept of tax residence exists.
11. Amendment 38 removes the words “or body” from new subsection 259ICA(5) TIOPA 2010, which was introduced by Paragraph 13 to Schedule 7, to ensure consistency with existing provisions within Part 6A of TIOPA 2010.
12. Amendment 39 inserts a replacement new section 259KA(7) into Chapter 11 Part 6A TIOPA 2010. It replaces the existing Condition E necessary for Chapter 11 to make a counteraction, which addresses situations where jurisdictions which have implemented the OECD’s recommendations on hybrid instruments are involved in a payment chain which eventually gives rise to a hybrid mismatch.
13. New subsection 259KA(7) provides that Condition E is that it is reasonable to suppose that the relevant mismatch is not capable of counteraction.
14. New subsection 259KA(7A) provides that a relevant mismatch is capable of counteraction to the extent it is capable of being considered, for the purposes of determining the tax treatment of a person other than P, under the law of a territory that is OECD mismatch compliant. This language is intended to address an ambiguity in the existing legislation, and make it clear that it is not necessary for a counteraction to be made in a relevant territory which has adopted the OECD recommendations in order for Condition E not to be met. It is sufficient that the relevant territory is OECD mismatch compliant, and so it has OECD derived law which addresses the question of whether a hybrid counteraction might arise.
15. New subsection 259KA(7B) provides for the possibility of a proportionate satisfaction of Condition E, where only a proportion of the relevant mismatch is capable of counteraction in a territory that is OECD mismatch compliant. This is to prevent Chapter 11 being fully disapplied in circumstances where funding for only part of the relevant mismatch passes via a territory that is OECD mismatch compliant.
16. New section 259KA(7C) provides that any determination of proportionality for the purposes of new section 259KA(7B) is to be done on a just and reasonable basis. By way of example, assume a UK company paid 100 to a company in a non-OECD mismatch compliant jurisdiction, that company then paid 90 to a company in another non-OECD mismatch compliant jurisdiction and 10 to a company in an OECD

mismatch compliant jurisdiction, and then those two payee companies paid 90 and 10 respectively to a company in a non-OECD mismatch compliant jurisdiction which was the payer in relation to a relevant mismatch of 100. The combined effect of new subsections 259KA(7B) and (7C) is that only 10 of the relevant mismatch would be treated as capable of counteraction, and Condition E would be treated as satisfied in respect of a relevant mismatch of 90.

17. New subsection 259KA(7D) defines what is meant by a territory being OECD mismatch compliant. This status is achieved by a territory if its law gives effect to the OECD report on hybrid mismatches. It is not necessary for the territory's law to deliver the same outcome as the UK's hybrid rules would in any given situation as long as the territory can be said to have given effect to the report.
18. Amendment 40 amends new subsection 259ZMB(9) TIOPA 2010, which was introduced by Paragraph 36 of Schedule 7, to ensure that both subsections (4) and (7) of section 1122 CTA 2010 are ignored for the purposes of establishing whether one person is connected to another.
19. Amendment 41 corrects for the omission of the word "entity" in new subsection 259MC(1(a)) TIOPA 2010, which was introduced by Paragraph 39 to Schedule 7
20. Amendment 42 provides for a replacement new subsection 259MC(1)(c) TIOPA 2010, which was introduced by Paragraph 36 to Schedule 7. The amendment is to allow the provision to apply where the relevant fund holds an indirect interest in the hybrid entity making the doubly deductible payment via another entity that is not a transparent fund.

## Background note

21. Clause 36 and schedule 7 of Finance (No. 2) Bill introduce several amendments to the Corporation Tax rules for hybrid and other mismatches. These rules have been in effect since 1 January 2017 and implement action 2 of the OECD's Base Erosion and Profit Shifting Project. The changes in Clause 36 and Schedule 7 are being made, following consultation, to ensure the rules operate proportionately and as intended and to alleviate instances of economic double taxation.
22. Following publication of Finance (No. 2) Bill and subsequent engagement with stakeholders, the Government are tabling a number of largely technical amendments to ensure the changes in Finance (No. 2) Bill have the intended effect and to remove some potential unintended consequences that have been identified.