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ATAD Implementation – Hybrids Feedback Statement
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ATAD Implementation Anti-Hybrid Rules Feedback Statement

Dear Sir/Madam

We welcome the publication of the Department of Finance ATAD Implementation Anti-Hybrid Rules Feedback Statement ("the Feedback Statement"), to provide stakeholders with the opportunity to give their input on the proposed implementation of the complex anti-hybrid rules under the EU Anti-Tax Avoidance Directives, ATAD[1] and ATAD2[2], into Irish law.

The discussions that have taken place since the Feedback Statement was released, at the TALC BEPS Implementation Sub-Committee ("TALC BEPS") between tax practitioners and Revenue officials, have proven to be very useful in assessing the potential impact of the proposed provisions in practice.

During these deliberations, it has become clear that amendments are necessary to the draft provisions contained in the Feedback Statement, to ensure that the new rules operate as policymakers intended. Given the complexity of the anti-hybrid rules, it is essential that a further opportunity is provided, through the TALC BEPS forum, to review the revised draft legislation to ensure that there are no unintended consequences when applied in practice.

We have summarised below the technical issues that our members have raised on the proposed anti-hybrid rules contained in the Feedback Statement. These are

[1] Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

[2] Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.

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1. Definitions

Meaning of 'entity'

The definition of entity is a core definition to the operation of the anti-hybrid rules. It should be evident for the purposes of the anti-hybrid rules that an entity must be a taxable person that is subject to corporate tax in Ireland and/or the counterparty jurisdiction. Article 1 of ATAD2 clearly states that the rules to address hybrid mismatches *apply to "all taxpayers that are subject to corporate tax in one or more Member States, including permanent establishments in one or more Member States of entities resident for tax purposes in a third country."*

Whilst we understand that the intention is to define "*entity"* broadly, so as to include taxable persons with and without legal personality, the proposed wording of the definition refers to "*a person*" which would include individuals. The definition should exclude individuals and should expressly state that an entity must be subject to corporate tax to be within the scope of the anti-hybrid rules.

The definition of entity also includes "*a trust including legal arrangements having a function or structure similar to trusts"*. We would suggest that consideration be given to excluding bare trusts from the scope of this definition, as they are effectively ignored for tax purposes.

Furthermore, the definition for an entity includes "*any other agreement or arrangement"*. This is extremely broad, and therefore, it may be more appropriate to confine the scope of this clause to any other agreement or arrangement related to the collective ownership of assets.

Meaning of 'associated entities' (pages 5-7 of the Feedback Statement)

The anti-hybrid rules will apply to transactions between associated entities. The definition of "*associated entities*" seeks to identify the scope of the taxable persons to which hybrid mismatch measures apply and sets out the percentage ownership thresholds that must be met.

The definition of associated entities, as currently drafted, gives rise to a number of issues. These are:

- As outlined above, the meaning of entity should be confined to persons other than natural persons. However, it should be clear that the ownership tests are applied by reference to the holdings of persons, which comprise both natural persons and entities. For example, persons holding interests in capital. This would allow the tracing of common relationships through ownership held by natural persons, but it would confine the meaning of entities to persons other than natural persons.

- Subsection (1)(a)(ii) refers to ownership of "*an interest*" in an entity other than a body corporate. We would suggest that this should be expanded to confirm that an interest in an entity other than a body corporate is confined to a capital or equity type interest.

  Subsection (2) states that the rights of any entities *"who act together in respect of the voting rights of ownership of an entity"* shall for the purposes of determining whether they are associated entities, be treated as being rights of all such entities.

  We understand from discussions at TALC BEPS that guidance will issue regarding the meaning of the provision and that only those partners actively working together in the exercise of their voting rights or ownership would be deemed to *"act together"*. We would suggest that the wording of the provision could be amended to refer to entities acting together in "*the exercise"* of voting rights rather than the current wording which refers to acting together "*in respect of"* voting rights.

- Subsection (4)(c) states *"…an entity shall also be an associated entity of any entity over the management of which it exercises significant influence, within the meaning of international accounting standards, or which exercises significant influence over its management. "*

  We understand from the discussions at TALC BEPS that this provision will be amended to remove the reference to international accounting standards and instead, define "s*ignificant influence*" by reference to "who *controls the majority of the board"*.

  As currently drafted, the provision could potentially include fund managers, who manage the day to day running of a fund. We understand that it is not intended that such fund managers would be included within the scope of the rules. Therefore, we would suggest that the provision "*or which exercises significant influence over its management*" should also be deleted.

- Subsection (5)(b) refers to the time when the transactions or arrangements between the associated entities were "*formed*". As such a scenario is already covered by the provisions of subsection (5)(a) and (c), which refer to the time when transactions or arrangements are entered into or when a payment arises, we would suggest that subsection 5(b) should be deleted.

Meaning of 'payment' (page 8 of the Feedback Statement)

We understand that the term "*deemed equity deduction"* in subsection (ii) should in fact refer to *"deduction on equity"* and therefore, the provision includes notional deductions on equity.

The definition of payment expressly excludes transfer pricing adjustments, equity deductions (as noted above) and some foreign exchange movements. It is understood that the policy intention is to exclude notional deductions where there is no payment, as well as differences in tax outcomes that are solely attributable to the value ascribed to a payment, in accordance with ATAD2.[3]

In addition, in the case of financial instruments, ATAD2 is clear that only mismatches that are attributable to different treatments due to the legal character of the instruments and payments on shares should only be within the scope of the anti-hybrid rules to the extent that they represent a return on the instrument. Therefore, it should be clear in the legislation in the context of financial instruments, that the meaning of payment should only extend to so much of the payment that represents a financing return.

However, as drafted, the definition of payment in subsection (iii) includes foreign exchange movements on some financial instruments[4], but excludes foreign exchange movements on shares and securities[5].

If the legislation reflects the general principle that the anti-hybrid rules are not intended to capture exchange rate movements or valuations, it should be possible to help taxpayers identify the range of financial instruments that could fall within the subparagraph (c) category in practice, with Revenue guidance. Difficulties could arise in identifying the amount of a payment potentially within scope when applying the anti-hybrid rules in number of situations, such as derivatives, Islamic financing and interest rate hedging, without such guidance.

Meaning of 'deduction' (page 8 of the Feedback Statement)

It is understood that the reference in subsection (ii) to an allowance for capital expenditure, includes capital expenditure on the purchase of an asset which is deducted on the computation of a subsequent capital gain and also deductions in the nature of depreciation or amortisation (including capital allowances).

We understand from discussions at TALC BEPS that the phrase *"on which tax fall to be borne"* applies to each of the scenarios at (i), (ii) and (iii) and therefore should be moved to after these three scenarios in the final legislation.

[3] Recital 22, ATAD 2 Differences in tax outcomes that are solely attributable to differences in the value ascribed to a payment, including through the application of transfer pricing, should not fall within the scope of a hybrid mismatch.

[4] See paragraph (c) of the definition of financial instruments, page 17.

[5] See paragraphs (a) and (b) of the definition of financial instruments, page 17.

As the definition of foreign tax refers to a tax "*that is similar to a domestic tax*", it is important that the definition of domestic tax is sufficiently broad.

Consideration should be given to including non-refundable Irish tax in the definition of foreign tax. For example, interest withholding tax imposed under section 246 TCA 1997, paid to a payee in a nil tax jurisdiction is not covered by the definition of foreign tax, even though the payee entity has clearly been taxed (and the income included).

It would also be necessary to clarify that a "*deduction*" does not include a payment which is offset against tax exempt income, as such a payment does not reduce income that is taxable.

Meaning of 'double deduction' (page 9 of the Feedback Statement)

In general, double deductions only give rise to an adjustment under anti-hybrid rules where the deduction is against income that is not dual inclusion income. The meaning of inclusion and dual inclusion income is very important and therefore, it should encompass the range of outcomes that have the same economic impact as taxing a payment including; disregarding a payment, ignoring a loss and income taxed under Controlled Foreign Company rules or similar regimes, such as GILTI in the US.

Meaning of "investor territory" (page 9 of the Feedback Statement)

The definition of "*investor territory*" specifically excludes "*payer territory*". Payer territory includes any territory where a payment giving rise to a deduction is "*incurred, sourced or made*". Concerns have been raised that the definition as currently drafted may give rise to issues in practice. For example, if an Irish company has a foreign branch that makes a payment of interest, that payment would likely be regarded as *"incurred, sourced or made"* in both Ireland and the branch jurisdiction. Therefore, both jurisdictions would be considered payer territories and neither would be considered an investor territory.

We would suggest that consideration could be given to revising the definition to more closely reflect the wording included in ATAD 2 (in the definition of 'double deduction') as follows:

> *"investor territory means:*
>
> *(a) in the case of a payment by a hybrid entity, the territory whether the hybrid entity is established;*
> *(b) in the case of a permanent establishment means the place where the permanent establishment is established under the laws of any territory,*
>
> *and investor shall be construed accordingly"*

Meaning of 'inclusion' (page 9 & 10 of the Feedback Statement)

ATAD2 does not seek to counteract deduction non-inclusion outcomes that arise because of another country's tax system or from transfer pricing adjustments. However, it is unclear that the definition of inclusion, as currently drafted, covers circumstances where the hybridity arises solely as a result of another country's tax system, for example, as a result of the application of a strictly territorial regime.

Subsection (c) refers to nil tax regimes and provides that a payment which is treated "*under the laws of that territory, as arising or accruing to the entity"* will be considered to be included. Concerns have been raised that it may not be possible to confirm that payments received by entities in nil tax jurisdictions are treated as arising or accruing to those entities "*under the laws of that territory*". We would suggest that consideration could be given to amending the clause as follows:

> *"where the payee is established or resident in a territory that does not impose a tax, the profits or gains are treated,* ***in the financial statements of that entity****, as arising or accruing to the entity;"*

Subsection (d) refers to *"a charge similar to a controlled foreign company charge."* We understand that this is intended to refer to regimes, such as the GILTI in the US, however it is unclear whether the wording of the provision achieves this intended result. We believe it would be important that clarification is provided in the legislation to ensure that comparable regimes, which result in a payment being included, are clearly stated within the scope of the definition of "*inclusion*".

Meaning of 'payee' (**page 10 of the Feedback Statement)**

It is necessary to identify the *"payee"* in order to establish whether there is a deduction or non-inclusion outcome. In doing so, it is critical to ensure that income received by one entity, which is taxed on its parent entity (or partner), that the parent entity (or partner) will be considered a payee and therefore, can meet the inclusion test for the purposes of the anti-hybrid rules.

Different jurisdictions use various methodologies to determine income and/or profits taxable on partners/owners. In Ireland, taxable income is firstly computed at partnership level and then assessed on each partner separately. However, for capital gains tax purposes, the partners are deemed to own partnership assets directly and the taxable gain is assessed on each partner. The definition of payee, as currently drafted, does not look at the character of the payment. This is relevant in the context of an Irish partnership, where the entity that receives the payment may be the partnership, but it is the partner who is subject to tax on the income.

We believe that the reference in the definition to '*without the payment passing through the hands of another entity'* could cause confusion and should be deleted, as income may pass through an entity, such as a partnership, but the income will be assessed on the partners directly.

***Meaning of 'dual inclusion income' (*page 10 & 11 of the Feedback Statement)**

We understand that the policy objective of the proposed provision on page 11 of the Feedback Statement is to ensure that only actual mismatch outcomes are subject to an adjustment under the anti-hybrid rules and that transactions that do not give rise to a hybrid mismatch outcome in reality are not captured.

It is vital to ensure that an adjustment under the anti-hybrid rules does not apply where the resulting economic impact is the same as taxing a payment. For example, disregarding a payment, denying a loss or income taxed under controlled foreign company (CFC) rules. This is particularly relevant in the context of branches that are taxed in the head office jurisdiction and also for disregarded entities.

For example, take an Irish section 110 company that is a disregarded entity for US tax purposes and is treated as a "*branch*" of its US parent company for US tax purposes. Interest payable on a loan advanced by the US parent company is deducted against income of the section 110 company for Irish tax purposes. It is a disregarded payment for US tax purposes; however, the income of the section 110 company is taxed as income of the US parent company. The disregarded payment should not be treated as resulting in a deduction without inclusion mismatch outcome under ATAD2, as the payment is not offset against income taxed in the US, which has the same economic effect as including the payment as income in the US[6]

A suggested revised provision was discussed at TALC BEPS which we believe would ensure the provision achieves its intended policy aim. We have included the wording of this revised provision in the Appendix.

Referring to similar rules in foreign territories (paragraph 2.3, page 12 of the Feedback Statement)

The Feedback Statement includes a provision to define when another country's primary rules may be treated as having neutralised a mismatch outcome and therefore, prevent the Irish defensive rules applying when the mismatch outcome has already been neutralised.

The scope of the phrase *"counteract mismatch outcomes*" is unclear. For example, does this also include counteracting measures that are not specifically labelled as anti-hybrid rules but target the same outcome? Whilst it may not be possible to provide an exhaustive list of all measures covered in legislation, it would be crucial for Revenue guidance to include examples of the type of measures it is intended to cover, in order to provide taxpayers with the necessary certainty.

[6] Recital 20, Article 2(9)(e) and Article (2) (9), 2nd (c), ATAD2.

2. The anti-hybrid rules

2.1 The rule against double deductions

The normal rule (pages 13 & 14 of the Feedback Statement)
A double deduction mismatch outcome is defined as arising where it would be “*reasonable to conside*r” that there is a double deduction, to the extent the payment is not deductible against dual inclusion income. We understand that the phrase “*reasonable to consider*” is intended to capture circumstances, such as the emergence of a new type of financial instrument, which does not fall within the scope of a particular Member State’s anti-hybrid rules. However, the use of the phrase “*reasonable to consider*” poses difficulties in practice and is likely to result in uncertainty where it must be applied across different jurisdictions.

We have suggested that consideration could be given to amending the wording of the definition of “investor territory”. If that definition were amended, we would suggest that the rule against double deductions may also need to be amended to reflect the change in the meaning of ‘investor’. This could be achieved by amending the first line of the subsection(2)(b) to provide that “*where the State is the payer **territory and not the investor territory** and a deduction has not been denied in the investor territory…*”

2.2 Deduction without inclusion outcomes *(page 17 of the Feedback Statement)*

2.2.1 Financial instruments (Page 17 – 19 of the Feedback Statement)

The definition of financial instruments includes securities, shares, other arrangements with returns equivalent to the lending of money and transactions and hybrid transfers. Subsection (c) on page 17 includes within the definition of financial instrument *“other arrangements where it is reasonable to consider that such arrangements are, in substance, equivalent to a transaction for the lending of money, or money’s worth, at interest”.*

It is understood that the policy intent is to exclude from the scope of the anti-hybrid rules differences in the value ascribed to a payment in accordance with ATAD2, for example, due to exchange rate fluctuations.[7]

Subsection (b)(i) on page 18 provides that a payment shall not be treated as included if *“the payment has not been included in a tax period which commences within twelve months of the tax period in which the deduction occurred*.” We would suggest amending

[7] Recital 22, ATAD 2 Differences in tax outcomes that are solely attributable to differences in the value ascribed to a payment, including through the application of transfer pricing, should not fall within the scope of a hybrid mismatch.

this wording to confirm that the payment must be included within twelve months of "**the end of"** the tax period in which the deduction occurred.

2.2.3 Hybrid Entities

Foreign Entity Classification (Paragraph 3.2.3.1 of the Feedback Statement)
The draft provisions propose an entirely new approach to foreign entity classification, to replace the existing approach that is based on case law. The new approach would consider the tax treatment under the laws of the territory in which the foreign entity is established, as opposed to the current approach, which considers the legal characterisation of the foreign entity under Irish law.

The proposed approach in the Feedback Statement raised serious concerns amongst our members and other practitioners at TALC BEPS. We understand from the most recent discussions at TALC BEPS that the current approach to foreign entity classification, based on existing case law, will now be maintained and that guidance on the matter will be developed by Revenue next year, with input from practitioners, via the TALC forum.

Definition of 'hybrid entity' (page 20 of the Feedback Statement)
We understand that the meaning of hybrid entity is intended to include entities that one country views as opaque and another country views as transparent. Under ATAD2, the rules to prevent a deduction without inclusion outcome in respect of payments to a hybrid entity apply in the first instance to deny a deduction and as a secondary defence measure, to include the income.[8]

Anti-hybrid rules (page 22 & 23 of the Feedback Statement)
We note that the wording of the draft provisions in respect of payments to and from hybrid entities differs from ATAD2, which may impact the application of the rules. For instance, subsection (1)(b) refers to the deduction without inclusion outcome being attributable to "*differences in the characterisation of the hybrid entity in the payee and payer territories*." This can be contrasted with the wording of ATAD2, which refers to the deduction without inclusion outcome resulting in *"differences in the allocation of payments made to the hybrid entity under the laws of the jurisdiction where the hybrid entity is established or registered*".

It is evident from ATAD2 that there must be a clear causal link between the payment to or by a hybrid entity and the deduction without inclusion outcome. For example, ATAD2 specifies that a hybrid mismatch will arise where "*a payment by a hybrid entity gives rise to a deduction without inclusion and that mismatch is the result of the fact that the payment is disregarded under the laws of the payee jurisdiction.*"[9]

[8] Article 9(2) ATAD
[9] Article 2(9)(e) ATAD

Such a causal link is not apparent in the draft provisions contained in the Feedback Statement, however, we appreciate that this causal link may become clear when the full legislative provisions are published.

In Ireland, hybrid entity mismatch outcomes are most likely to arise in the context of international fund structures and entities with a US parent company. However, it is unclear that the provisions, as currently drafted, achieve their stated objective of ensuring that only actual mismatch outcomes are subject to an adjustment under the anti-hybrid rules[10] in the context of such entities.

Consideration should be given to amending the wording of the proposed anti-hybrid rules in the Feedback Statement, as currently drafted, because the rules do not appear to reflect the outcome envisaged by ATAD2. We believe that the suggested revised wording set out in the Appendix, in respect of disregarded payments would address a number of these scenarios.

One such example would be a US parented company which effectively ignores payments between subsidiaries, which are treated as disregarded entities for US tax purposes and therefore, are taxed as foreign branches of the US company. Such ‘branches’ are treated as a single foreign branch for US tax purposes.

In a case where a UK company which is treated as a branch for US tax purposes pays interest to an Irish company, which is also treated as a ‘branch’ for US tax purposes, the net result is that there is no net tax benefit in US, as both the Irish income and UK expense are ignored. The wording suggested in the Appendix would mean that such a scenario should not come within the scope of the Irish anti-hybrid rules as the economic effect of the disregarded payments in not reducing the taxable measure of US taxed income is recognised as dual inclusion income (i.e. included both in the US parent company and in Ireland, in the case of the Irish company).

A possible solution to address such a scenario would be to provide as per the wording in the Appendix that where there is an expense deductible by a hybrid entity, which transacts with other hybrid entities of the same parent entity, then the disregarded payment should be treated as included in income in the investor territory, when determining if there is dual inclusion income.

2.2.4 The rule against disregarded permanent establishments (paragraph 3.2.4 of the Feedback Statement)

Due to Ireland’s worldwide system of taxation, an Irish tax resident company cannot have a disregarded permanent establishment (PE) in another jurisdiction. It is possible

[10] Page 11, Feedback Statement

however for a company to have a disregarded PE in Ireland, where that company is established in another jurisdiction, which has a territorial system of taxation.

In order to prevent disregarded PEs being located in Ireland, it is proposed that Ireland implements a defensive rule which recognises the income from a disregarded PE, as though it was an Irish resident company, using the PE definition contained in the 2017 OECD Model Tax Convention.

Sections 747G and section 1035A TCA1997 are intended to provide assurance to agents acting in the financial services sector that the non-resident entity for whom they act should not have a taxable presence in Ireland. This is considered to achieve a tax neutral outcome, as the agents' fees are taxable in Ireland and would be expected to equate to the measure of taxable income of the non-resident attributable to these activities. Consideration should be given to include an express exclusion for such agents from the scope of the measures relating to disregarded PEs. This would provide certainty to the financial services sector that no inadvertent double taxation may arise.

3. Anti-avoidance rules

Imported mismatches (Paragraph 4.1 of the Feedback Statement)

An imported mismatch can arise in circumstances where an Irish taxpayer does not enter into a hybrid transaction but enters into one of a series of transactions that gives rise to a hybrid mismatch outside of Ireland, the benefit of which is imported into Ireland.[11] The rule provides for a proportionate restriction in the deduction to the extent that the mismatch has not been counteracted in the mismatch jurisdiction.

The proposed provision refers to an arrangement giving rise to a *"mismatch outcome",* whereas ATAD2 refers to a payment by a taxpayer which directly or indirectly funds a *"hybrid mismatch."* As "*mismatch outcome*" has a different and wider meaning than "*hybrid mismatch*", it would be essential that the provision is amended to ensure that the imported mismatch rule only applies in circumstances where there is a hybrid mismatch.

Under the rule, the test to be applied is an objective test of whether it "*would be reasonable to consider."* Consideration must also be given to whether an arrangement *"directly or indirectly funds*" the mismatch outcome. However, the linkage required in respect of the flows of funds for the purposes of the application of the rules is unclear. Therefore, it would be necessary to ensure that Revenue guidance provides clarification, using practical examples, as to how these concepts will be applied in practice.

The proposed rules provide that where an imported mismatch arises, a deduction will not be allowed for "*so much of the payment as corresponds to the mismatch outcome which has not been neutralised in another territory."* In practice, it may be difficult to determine

[11] Page 27, Feedback Statement

the extent to which the mismatch has not been counteracted in the mismatch jurisdiction and calculate the proportionate restriction in the deduction.

A range of scenarios were discussed at TALC BEPS, relating to jurisdictions with nil tax regimes, jurisdictions with purely territorial regimes, transparent entities and entities subject to "check the box" elections in the US. It was very evident from the discussions, that difficulties will arise in identifying the relevant jurisdiction to be considered, when seeking to determine if the imported mismatch rules apply.

Undoubtedly, applying and monitoring a rule that denies deductions for imported mismatches on payments made to EU and Non-EU recipients will be extremely difficult and may result in double taxation, given the implementation of ATAD anti-hybrid rules across the EU. It is unclear where the adjustment should be made in circumstances where there is more than one EU payer in a series of transactions. Indeed provisions that deny deductions for payments by a taxpayer to recipients in another EU Member State can be problematic from an EU law perspective.[12]

The preferable approach would be to only apply the rule to payments made to Non-EU recipients, in order to avoid the risk of double taxation. When considering a payment which originates in an EU Member State and is paid through one or more other EU Member States, before being paid to a third country, it should only be necessary for the last EU Member State in a chain to determine if the imported mismatch rules apply.

Furthermore, it is critical that the order of priority of the application of the relevant rules should be confirmed.

Structured arrangements (paragraph 4.2 of the Feedback Statement)

The proposed structured arrangement provisions apply to transactions between non-associated entities (third parties), where the mismatch outcome is priced into the terms of the arrangement or the arrangement was designed to produce a hybrid mismatch outcome.

The proposed provisions refer to an arrangement giving rise to a "*mismatch outcome*" whereas ATAD2 refers to an arrangement giving rise to a "*hybrid mismatch*." As "*mismatch outcome"* has a different and wider meaning than "*hybrid mismatch*", we would recommend for the provision to be amended to ensure the scope of the structured arrangement rule is not extended beyond the standard required in the Directive.

In implementing the rule, the provisions require that the standard of knowledge to be applied is what the taxpayer would "*reasonably be expected to be aware*". In order to

[12] In the case of SIAT SA v État belge (C-318/10) a provision of Belgian law that denied a deduction for a payment to a Luxembourg company was held to breach the free movement of services guaranteed by Article 49 EC.

provide clarity, it would be useful if Revenue guidance, included practical examples on the application of this provision.

As you can appreciate from the matters outlined above, that many issues and difficulties have been raised regarding the proposed implementation of these very complex rules in this year's Finance Bill. It is evident that a number of amendments are required to the draft provisions contained in the Feedback Statement, to ensure that the new rules operate as policymakers intended.

Given the complexity of the anti-hybrid rules, we would urge that there is further consultation with stakeholders on the revised draft legislation, through the TALC BEPS forum, in advance of the publication of the Finance Bill, to ensure there are no unintended consequences of the new rules when applied in practice.

If you wish to discuss any aspect of this submission, please do not hesitate to contact Anne Gunnell at agunnell@taxinstitute.ie.

Yours truly

Marie Bradley

Marie Bradley
Institute President

Appendix

Suggested revised wording for the draft provision outlined on page 11 of the Feedback Statement, which was discussed at TALC BEPS:

Disregarded payments

(1) This section applies where under the law of a territory (referred to in this section as the "first mentioned territory"), an entity (in this paragraph referred to as a "responsible entity") ~~body corporate~~ is treated under the law of that territory as including in its taxable *profits and gains ~~in the investor or payee territory, as appropriate~~ on all or part of the consolidated or aggregate profits and aggregate gains, of that entity and one or more other entities (in this section referred to as the "consolidated entities"), [(whether by means of the other entities being treated as a branch of the responsible entity, or as a consequence of an election made by any of the entities, or as a result of the application of controlled foreign company or similar rules, or otherwise)] ~~its worldwide profits~~* such *that payments arising from transactions* between *two or more of the consolidated entities are*

~~(a) a permanent establishment of the body corporate established in another jurisdiction and the head office of the body corporate, or~~

~~(b) between two permanent establishments of the body corporate,~~

~~are~~ disregarded (referred to in this section as "disregarded payments") *when computing the taxable profits of ~~the~~ a responsible entity ~~body corporate~~ in the first mentioned territory, ~~under a provision the effect of which is similar to section 26(1)(a).~~.*

(2) Where this section applies, and

(a) a payment is treated as deductible against income in both a payer territory and in the first mentioned territory, but

(b) the income against which it is deductible in the payer territory arises from a ~~is~~ disregarded payment ~~in the first mentioned jurisdiction~~,

then, notwithstanding anything else in this Part, the disregarded payment referred to in paragraph (b) shall be treated as included in the income, profits, or gains (as appropriate) of a responsible entity ~~first mentioned territory,~~ for the purpose of determining under this Part if a payment has been deducted against dual inclusion income.

(3) Where this section applies, and

(a) a disregarded payment made by one or more of the consolidated entities is treated as deductible in the payer territory but is not treated as included in the income, profits, or gains (as appropriate)

of a responsible entity under the laws of the first mentioned territory, but

(b) the income against which it is treated as deductible in the payer territory is included in the income, profits, or gains (as appropriate) of a responsible entity under the laws of the first mentioned territory or is treated as so included under subsection (2),

then, notwithstanding anything else in this Part, the disregarded payment referred to in paragraph (b) shall not be treated as a deduction without inclusion mismatch outcome.