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## Amendment to the Parent Subsidiary Directive 2011/96/EU (PSD) for hybrid financing arrangements.

### INTRODUCTION

On 8 July 2014, the European Union's Council of Economic and Financial Affairs (ECOFIN) formally adopted an amendment to EU tax rules to prevent double non-taxation of dividends distributed within corporate groups deriving from hybrid loan arrangements (i.e. financial instruments that have characteristics of both debt and equity).

The aim of this amendment was to close a loophole allowing corporate groups to exploit mismatches between national tax rules so as to avoid paying taxes on some types of profits distributed within the group.

The adoption of this amendment follows the political agreement reached at the Council's meeting on 20 June 2014.

## **GENERAL TAX CONSEQUENCES OF THE AMENDMENT**

The amendment to the PSD will prevent cross-border companies from planning their intra-group payments so as to result in double non taxation where hybrid loans arrangements are involved.

**The member states of the parent company should henceforth refrain from taxing profits from the subsidiary only to the extent that such profits are not deductible by the latter. As a consequence, if the profits distributions are tax deductible in the Member State of the subsidiary, then the profits distributions received by the parent company cannot be tax exempt in the Member State of the parent company.**

However, it has been explicitly stipulated in the Commission statements to the Council that the proposed amendments are not intended to be applicable if there is no double non-taxation or if their application would lead to double taxation of the profits distributions between parent and subsidiary companies.

Member states will have until 31 December 2015 to transpose the amendment into their national laws.

## **TAX CONSEQUENCES ON LUXEMBOURG STRUCTURES**

A Luxembourg parent company may benefit from the Luxembourg participation exemption regime on payments deductible in another Member State if those payments are considered as profits distributions for Luxembourg tax purpose under the “substance over the form” principle.

This tax treatment is nevertheless quite rare in practice and consequently should not have a huge impact on Luxembourg parent companies.

Furthermore, the deductibility of the payments made under the hybrid instruments issued by Luxembourg companies should not be refused under the amended PSD.

**Nevertheless, it is recommended to check the impact of this amendment of the PSD on a case by case basis when interest payments made by a Luxembourg subsidiary to a parent company located in another Member State are exempted under the participation exemption regime of this other Member State.**