DOUBLE IRISH, DUTCH SANDWICH: OVERCOMING HYBRID MISMATCH ARRANGEMENTS

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DOUBLE IRISH, DUTCH SANDWICH: OVERCOMING HYBRID MISMATCH ARRANGEMENTS

Severine Bateman[*]

Abstract

In 2013, the Organization for Economic Cooperation and Development ("OECD") released its report on Base Erosion and Profits Shifting (BEPS) of international tax revenue. In this report, OECD outlined 15 Actions that had contributed to trillions of dollars being lost from the tax revenue due to active tax avoidance strategies. The Second Action addressed hybrid mismatch arrangements, where companies used residencies in different countries to take advantage of double tax deductions or report results of no income. The most classic and best understood example of such a tax avoidance scheme is the Double Irish, Dutch Sandwich, which allowed companies that owed billions of dollars in corporate taxes to get away with paying well under that amount—and sometimes no income tax at all—by taking up residence in "tax havens." To combat this issue, OECD released recommendations for countries to follow that would reduce the likelihood of such tax avoidance schemes from being effective or possible. Following those recommendations, many countries, including Ireland and England, made efforts to prevent the use of such tax avoidance schemes. This paper serves three primary purposes. First, the paper analyses the recommendations made by OECD and determines whether they would be effective at preventing hybrid mismatching. Second, the paper analyses the Netherland's response to the tax scheme as well as the Double Irish, Dutch Sandwich tax scheme to see whether the OECD report was instrumental in preventing hybrid mismatching. Lastly, the paper analyses the new aggressive tax avoidance schemes that have been presented since the OECD report and how to best stop such schemes from reappearing as well as which type of regulations would best curtail the rise of hybrid mismatches.

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INTRODUCTION

Paying taxes is an economic burden that every person and corporation is met with at some point in their lives. Taxes are necessary for every country to fund the various programs run to help either secure the lives of the country's residents or to help provide necessary needs that cannot be taken care of on a smaller scale.[1] Some people enjoy paying taxes, taking note of how taxes are being used to provide necessities or make improvements in a country-wide scale.[2] Others do not enjoy paying taxes, viewing the government's acquisition of their hard-earned money as an invasion into their personal finances. However, no matter what one's views on taxes are, they still must be paid.

While taxes must be paid, the process of how they get paid differs from country to country. One country's definition of a nationwide necessity is different than another's, leading to lower taxes and instances where fewer government programs need to be funded. Other countries simply desire to place lower tax burdens on their residents, again resulting in lower taxes. Meanwhile, other countries have a lot of government programs to address the country's needs, resulting in higher taxes. While different countries might have different tax rates to address different needs, residents in other countries take note of these different tax rates and see an opportunity.

While it is true that taxes must be paid, a significant number of people and taxable entities do everything possible in their power to avoid paying them. In 2013, the Organization for Economic Cooperation and Development ("OECD") did a study on Base Erosion and Profit Shifting ("BEPS").[3] The study analyzed fifteen Actions taken by taxpaying entities that had resulted in significantly lower amounts of taxes being paid over extended periods of time than what would typically have been paid if these actions were not taken.[4] Of the fifteen Actions, Action 2 noted that through a system known as hybrid mismatch arrangements, corporations located around the world had been able to successfully shift money from one country with high corporate tax rates to another country with much lower tax rates, resulting in billions of dollars being withheld from tax collection every

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[1] *Taxes Are What We Pay for Civilized Society*, QUOTE INVESTIGATOR (Apr. 13, 2012), https://quoteinvestigator.com/2012/04/13/taxes-civilize/.

[2] *Id.*

[3] Org. for Econ. Coop. & Dev. [OECD], *Addressing Base Erosion and Profit Shifting*, at 5, (2013), https://doi-org.10.1787/9789264202719-en.

[4] *Id.* at 10.

year.[5] The most well-known and notorious hybrid mismatch scheme for helping corporations avoid paying taxes is the Double Irish with a Dutch Sandwich.[6] Under the scheme, corporations could funnel money through Ireland and the Netherlands before ending up in a country that had negligible tax rates.[7] With the help of the Double Irish with a Dutch Sandwich, major corporations such as Amazon and Facebook were able to avoid paying billions of dollars in taxes every year.[8]

Shortly after OECD published this report, OECD released an additional report filled with possible recommendations that could be taken by countries to help reduce the loss of taxes occurring with each Action.[9] This paper performs an analysis on how the publication of these recommendations related to hybrid mismatch arrangements had an effect on the Double Irish, Dutch Sandwich scheme and the two countries behind it, namely Ireland and the Netherlands. The analysis will be broken up into five parts. After this introduction to the topic, Part II discusses the history of hybrid mismatches and the Double Irish with a Dutch sandwich tax scheme, explaining how the BEPS Action is able to reduce a corporation's tax burden by billions of dollars. Part II also discusses OECD's recommendations proposed to counteract hybrid mismatch arrangements. Part III shows the effect the recommendations had on the Double Irish, Dutch Sandwich, along with the tax plan changes made in Ireland and the Netherlands. Part IV discusses the new hybrid mismatch arrangement schemes being used to avoid tax burdens, as well as possible actions to take to prevent the rise of such tax avoidance schemes in the future. Part V concludes this paper, emphasizing the next steps to be taken.

[5] OECD, *Action Plan on Base Erosion and Profit Shifting*, at 17, (2013), https://www.oecd.org/ctp/BEPSActionPlan.pdf.

[6] Jacob Fonseca, *ESG Investing: How Corporate Tax Avoidance Affects Corporate Governance & ESG Analysis*, 25 ILL. BUS. L.J. 9, 9 (2020).

[7] Danielle Thorne, The Double Irish and Dutch Sandwich Tax Strategies: Could a General Anti-Avoidance Rule Counteract the Problems Caused by the Utilisation of These Structures?, (2013) (LLM thesis, Victoria University of Wellington) (on file with the Victory University of Wellington Library).

[8] Jim Corkery et al., Taxes, the Internet and the Digital Economy, 23 REVENUE L.J. 4 (2013).

[9] OECD, *Neutralizing the Effects of Hybrid Mismatch Arrangements, Action 2-2015 Final Report*, at 11 (2015), https://doi.org/10.1787/9789264241138-en [hereinafter Action 2 Report].

I. TAXATION SCHEMES

A. History of Hybrid Mismatch

Hybrid mismatches became a much more common occurrence with the rise of a more global economy. Whereas taxes have been a fundamental part of virtually every society, determining the correct jurisdiction for an entity to pay taxes is a newer concept. As trade and travel between different countries and continents became easier and technologies developed that allowed money to be transferred instantaneously, countries found themselves tasked with taxing money that was hard to track.[10] Along with the transfer of money came the rise of corporations large enough that they had offices or some similar presence in multiple countries across the globe.[11] With the newfound placements in multiple countries, such corporations also found themselves with the ability to decide where they would be taxed, employing methods that would allow for the least amount of taxation possible.[12] One such method is hybrid mismatching.

A hybrid mismatch arrangement is a tax-avoidance maneuver that uses the different tax laws across different countries to pay substantially less in taxes or put off paying taxes for a long time.[13] Such a tax avoidance scheme is commonly used among multinational corporations, as a presence in another country is usually necessary to take advantage of the setup.[14] These multinational enterprises ("MNEs") make use of a related entity in another country, such as a subsidiary, or a tax instrument, such as a loan, to move money into different jurisdictions. These jurisdictions offer beneficial tax treatment of a chosen entity or instrument, allowing MNEs to pay less in taxes or avoid paying taxes all together.[15] When making use of another entity, it appears that money is being transferred from one country to another within the same MNE. When making use of a tax instrument, the process can be done within the same MNE or might appear as money being passed from an MNE to another institution, such as a bank. These transactions are called "hybrid" transactions because the entity or instrument changes tax status

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[10] Tyler Halloran, *A Brief History of The Corporate Form and Why It Matters*, FORDHAM J. OF CORP. & FIN. L. BLOG (Nov. 18, 2018), https://news.law.fordham.edu/jcfl/2018/11/18/a-brief-history-of-the-corporate-form-and-why-it-matters/.

[11] *Id.*

[12] *Id.*

[13] *See Action 2 Report*, *supra* note 10, at 11.

[14] *Id.*

[15] *Id.* at 147.

based on the jurisdiction.[16] In terms of an entity, the company is nonrelevant taxwise in one jurisdiction, but becomes a taxpayer in another jurisdiction.[17]

The money MNEs are able to divert from taxes, considered a tax mismatch, differs based on the kind of hybrid mismatch the MNE employed as well as the tax rules that exist in the country the money is headed to.[18] When the transfer of money results in a deduction in the jurisdiction of origin but is not included in the tax calculation in the second jurisdiction because of that jurisdiction's tax laws, the scheme is considered a deduction with no inclusion ("D/NI").[19] Another tax mismatch that arises from hybrid mismatching is where the MNE is able to receive a deduction for the money in the first jurisdiction while also receiving a deduction in the second, resulting in a double deduction ("DD") for the MNE.[20] Double deductions are often seen when an MNE uses a hybrid instrument, such as debt, to transfer money.[21]

B. Double Irish, Dutch Sandwich Scheme

One of the most well-known taxation schemes that follows the hybrid mismatch arrangement setups is the Double Irish with a Dutch Sandwich scheme. The Double Irish, Dutch Sandwich tax scheme came to fruition in the 1980s as multinational corporations started to become more prevalent and were able to communicate more easily with subsidiaries and other companies that were held around the globe.[22] By the 1990s, it was one of the most popular and well-known tax avoidance schemes in the world.[23] Up until the release of the OECD's BEPS report in 2013, the tax avoidance scheme was employed by many of the most prominent companies in Silicon Valley—Google, Apple, Facebook, and Microsoft

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[16] *Id.* at *95.*

[17] *Id.*

[18] Jones Day, *Hybrid Mismatches and the OECD Proposal: BEPS Action 2, Global Tax Update*, INSIGHTS (Sept. 2015), https://www.jonesday.com/en/insights/2015/09/hybrid-mismatches-and-the-oecd-proposal-beps-action-2-iglobal-tax-updatei.

[19] *Id.*

[20] *Id.*

[21] *Id.*

[22] Cyrus Farivar, *Silicon Valley fights to keep its Dutch Sandwich and Double Irish loopholes*, ARS TECHNICA (Jan. 20, 2014), https://arstechnica.com/information-technology/2014/01/silicon-valley-attempts-to-slow-new-global-tax-avoidance-reform-proposals.

[23] *Id.*

are just a few examples.[24] The tax strategy was also used by many other MNEs across the United States and the world.[25]

The best way to illustrate the workings of the Double Irish, Dutch Sandwich is through an example. To implement the tax strategy, CorpA, a US-based corporation, circumnavigates the U.S. corporate tax by either leasing necessary material or selling product from SubA, a subsidiary located in Ireland. Because of CorpA's leasing, all of the money made by CorpA related to the leased material is sent to SubA. Ireland's corporate tax rate, sitting at 12.5%, is much lower than the U.S. corporate tax rate was before 2015, which was 35%, making Ireland a much better place to pay taxes.[26] However, prior to 2015, Ireland had a tax law that allowed corporations to pay taxes at any location that the corporation had a managing presence in.[27] With this tax law, corporations could set up managing branches in tax havens, which are countries that are known for imposing little, if any, corporate taxes.[28] The income moved to these tax havens would then be considered "stateless" and not subject to taxes in Ireland.[29] By setting up a branch in a tax haven, such as Bermuda, CorpA is able to pay very little in taxes, with tax rates being able to go as low as 2%.

To prevent companies from taking advantage of such foreign tax laws, the U.S. and many other countries have implemented Controlled Foreign Corporation ("CFC") rules that allow the taxation of another entity outside the country if the entity is owned by a corporation within the home country.[30] In terms of the example, CorpA would have to pay taxes that have made their way to the tax haven country because SubA is owned by CorpA. To circumnavigate these laws, CorpA would establish a second subsidiary, SubB, in Ireland. SubB would be tasked with transferring funds to the tax haven. The transfer of funds within Ireland would avoid the CFC rules, resulting in CorpA obtaining a tax rate of 2% or lower for their earnings.[31]

To finish off the tax avoidance scheme, CorpA would need to transfer funds from SubA to a subsidiary in the Netherlands, DutchA, and then transfer the funds to SubB. CorpA could transfer the funds directly between the two companies, but

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[24] *Id.*

[25] *Id.*

[26] *The Double Irish Dutch Sandwich Finally Explained*, FINSHOTS (Jan. 3, 2020), https://finshots.in/archive/the-double-irish-dutch-sandwich/.

[27] *Id.*

[28] *Id.*

[29] *Id.*

[30] *Id.*

[31] *Id.*

then CorpA would have to pay a withholding tax on the funds before transferring the funds to the tax haven country.[32] Because of a tax treaty between Ireland and the Netherlands, no taxes would be extracted from the transfer of funds between the two countries.[33] In this way, DutchA allows CorpA to successfully transfer the funds to the tax haven without having to pay any extra tax except for the corporate tax in the tax haven.

When it was in force, this tax avoidance strategy resulted in a deduction of the income for the MNE in the U.S. and would be almost equivalent to having no inclusion in the tax haven country, resulting in the MNE sheltering large amounts of money from taxes in a D/NI scheme. The Double Irish, Dutch Sandwich resulted in billions of dollars escaping taxation annually.[34] The scheme is fairly popular among tech companies because the companies are built on easy-to-license-out patents and other technological goods. In 2015, Google and Apple used the Double Irish, Dutch Sandwich to successfully remove $20 billion from tax contributions.[35] Some of the tax havens used, such as the Cayman Islands, have no corporate tax rate which allowed Apple to pay only 2% in taxes for funds that passed through Ireland.[36] In 2016, Google was able to underpay taxes to the French government by €1 billion because of the Double Irish, Dutch Sandwich.[37]

While the Double Irish, Dutch Sandwich is one of the most famous hybrid mismatch arrangements, there are many more tax avoidance schemes around the world that use different tax laws and tax treaties to help MNEs pay as little in taxes as possible. The use of these tax schemes can be hard to track down because of differing treaty structures and tax laws between countries.

C. OECD Recommendations

With billions of dollars that should be collected in taxes being lost annually, the BEPS investigation done by OECD came up with various recommendations to

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[32] *Id.*

[33] *Id.*

[34] Anup Srivastava et al., *Doubling Down on Double Sandwich Tax Schemes*, CAL. MGMT. REV. (Mar. 30, 2020), https://cmr.berkeley.edu/2020/03/doubling-down/.

[35] *Id.*

[36] Hunter Snowden, *Apple's Double Irish with a Dutch Sandwich*, JURIS: DUKE'S UNDERGRADUATE LAW MAGAZINE (June 1, 2017), https://dukeundergraduatelawmagazine.org/2017/06/01/apples-double-irish-with-a-dutch-sandwich/.

[37] *Double Irish and Dutch Sandwich Saved Google $3.7bn in Tax in 2016*, IRISH TIMES (Jan. 2, 2018, 4:33 PM), https://www.irishtimes.com/business/economy/double-irish-and-dutch-sandwich-saved-google-3-7bn-in-tax-in-2016-1.3343205.

help negate the loss of taxable income around the world.[38] Of the twelve recommendations made by OECD, recommendations 1 through 8 give structured outlines for rules that countries could adapt to prevent hybrid mismatch arrangement tax avoidance.[39] Meanwhile, recommendations 9 through 12 give general definitions and implementation principles for recommendations 1 through 8.[40] For the more action-oriented recommendations 1 through 8, the recommendations can be separated into whether they address hybrid mismatches that cause D/NI tax breaks or DD tax breaks.[41] There is also a small subsection for mismatch arrangements that cause indirect D/NI tax breaks.[42]

i. Deduction with No Inclusion Mismatches

As the most common form of tax mismatch, recommendations 1 through 5 are designed to combat hybrid mismatch arrangements that result in a D/NI outcome, which is money being deductible in one tax jurisdiction yet not being included in another tax jurisdiction.[43] This is quite similar to the tax mismatch that is created by the Double Irish, Dutch Sandwich scheme. Recommendation 3, titled "Disregarded Hybrid Payments Rule," provides a structure that is similar to the other recommendations related to D/NI outcomes.[44] The recommendation is broken down into four parts.[45]

The recommendation first lays out steps a country can take to prevent any D/NI outcomes from a disregarded hybrid payment in section 3.1.[46] In order to neutralize the payment, the jurisdiction of the payer should "deny the deduction" of the payment if it would give rise to a D/NI outcome.[47] To go back to the example company CorpA, this would mean that the U.S. would deny the deduction CorpA would get for payment of a licensing fee to SubA.

Second, suppose the payer's tax jurisdiction does not implement the "Disregarded Hybrid Payments Rule." In that case, the jurisdiction of the payee must include the payment as "ordinary income to the extent the payment gives rise

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[38] *See Action 2 Report*, *supra* note 10.
[39] *See id.* at 23–91.
[40] *See id.* at 93–124.
[41] *See id.* at 23–91.
[42] *Id.* at 27.
[43] *See id.* at 23–65.
[44] *Action 2 Report*, *supra* note 10, at 50.
[45] *Id.* at 50–54.
[46] *Id.* at 50.
[47] *Id.*

to a D/NI outcome."[48] For CorpA, this would mean that if the U.S. did not tax the licensing payment, then Ireland would need to include the payment in SubA's ordinary income and tax it.

Thirdly, the hybrid mismatch rule will not apply "to the extent that the deduction is set-off against [dual-inclusion income]."[49] This point essentially means that the rule will not be enforced in cases where the deduction offered by the payer's country would essentially negate payments that would typically be considered income in both taxpayer jurisdictions.[50] For CorpA, this would mean that the U.S. would allow a deduction of a payment if it were offset by the inclusion of the payment as income in Ireland with SubA.

Lastly, any deduction that is in excess of the amount to be paid in dual-income inclusion is pushed off until another taxation period.[51] Therefore, if CorpA had a deduction in the U.S. greater than the amount applied in dual-income inclusion, the excess of the deduction would be pushed off until the next taxation period.

Sections 3.2 through 3.3 serve as descriptors for terms in section 3.1, defining what constitutes a hybrid payer, a disregarded payment, and what kind of payment would result in a hybrid mismatch.[52] Section 3.4 also states that the recommendation would only apply if the two parties in the transaction are "in the same control group" or if the payment is under a "structured arrangement" with the payer in the structured arrangement.[53] The rule was structured in order to capture taxable income that had been slipping through taxation schemes by hybrid mismatch arrangements, which is why the rule calls for at least one tax jurisdiction to implement the rule. However, OECD also recognized that strict guidelines with no leeway could lead to double taxation, which is why it recommends for allowable deductions if the income falls into dual-income inclusion categories.[54]

ii. <u>*Double Deduction Mismatches*</u>

OECD's recommendations 6 and 7 related to hybrid mismatch arrangements are meant to stop the procurement of double deductions during one taxation period. This would occur when a tax entity is able to procure deductions in the original tax

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[48] *Id.* at 49.
[49] *Id.* at 50.
[50] *See id.* at 43.
[51] *Id.* at 50.
[52] *Id.* at 53–54.
[53] *Id.* at 54.
[54] *See Action 2 Report, supra* note 10, at 52.

jurisdiction as well as another deduction in the secondary tax jurisdiction.[55] Recommendation 7, the "Dual-Resident Payer Rule," provides a solid structure to model the recommendation outline for double deduction tax mismatches.[56]

Recommendation 7.1 outlines the main suggested regulations for dual-residents, which are fairly similar to the outline provided in recommendation 3.[57] First off, the rule states that, in situations where a dual resident is entitled to deductions for a payment in both the payer jurisdiction and the payee jurisdiction, the resident jurisdiction is to deny such deductions.[58]

Secondly, "no mismatch will arise" to the level where the deduction would be set off against income that would be classified as dual-income inclusion.[59] This rule is implemented by strict protocols to follow when a deduction exceeds the maximum to prevent a mismatch from occurring.[60] For the Dual-Resident Payer Rule, the excess deduction is closely monitored to make sure it is only applied to income subject to dual-income inclusion if the deduction is to be applied to another tax period.[61]

Like recommendation 3, recommendation 7 sections 7.2 through 7.3 provide definitions for terms such as "dual resident" and "hybrid mismatch," as well as to which parties the rule applies.[62] However, section 7.4 points out that recommendation 7 has no limitations as to whom the rule could apply, making it a more generally applicable recommendation.[63]

Recommendations addressing double deductions made through hybrid mismatching were created due to the concern that income that should have been taxed was escaping taxation even though it was not income being transferred between two parties, essentially postulating that income which would not be considered dual-income inclusion income was being given deductions meant solely for dual-income inclusions.[64] However, while recommendation 7 is crafted for deductible payments, OECD goes even further to suggest that the

[55] *Id.* at 67–81.
[56] *Id.* at 77.
[57] *Id.* at 78.
[58] *Id.*
[59] *Id.* at 77.
[60] *Id.*
[61] *Id.*
[62] *Id.* at 80–81.
[63] *Id.* at 77.
[64] *Id.* at 78.

recommendation should be applied to all deductible items, providing a simpler tax plan for varying tax jurisdictions.[65]

iii. *Indirect Deduction with No Inclusion Mismatches*

Recommendation 8, the "Imported Mismatch" rule, is uniquely crafted to deal with attempts to circumnavigate the monitoring of hybrid mismatches.[66] The recommendation is made to address the possibility of entities entering into a hybrid mismatch transaction that does not trigger any deduction or inclusion issues but instead transfers funds from the transaction to a third tax jurisdiction that does result in a deduction or no inclusion mismatch.[67]

Section 8.1 of recommendation 8 sets forth that the jurisdiction of the payer should prohibit deductions that come from an imported mismatch if it rises to the level of "the payee treat[ing] that payment as a set-off against a hybrid deduction in the payee jurisdiction."[68]

Where sections 8.2 and 8.3 again provide definitions for terms such as "hybrid deductions" and "imported mismatch payments," section 8.4 lays out a scope of application similar to the scope provided in recommendation 3, with the rule applying only to transactions with both parties controlled by the same entity or a transaction with a structured arrangement for payment.[69]

The recommendation is made to catch taxation avoidance schemes that prevent a hybrid mismatch in the first transaction by shifting the mismatch to a secondary transaction.[70] The Double Irish, Dutch Sandwich would most likely fall within this group of indirect deductions and no inclusion schemes, as the no inclusion aspect does not really apply until the money is transferred to a tax haven.

II. REFORMATION OF THE DOUBLE IRISH, DUTCH SANDWICH

The final recommendations from OECD regarding hybrid mismatches were published in 2015, with OECD providing some guidance starting as early as 2013.[71] Since the guidelines have been published, action has been taken in both

[65] *Id.* at 79.
[66] *See id.* at 83.
[67] *Id.*
[68] *Id.* at 83.
[69] *Id.*
[70] *See Action 2 Report, supra* note 10, at 85.
[71] *See Action Plan*, *supra* note 6, at 15.

Ireland and the Netherlands to combat the effects of hybrid mismatch arrangements.

A. Reformation in Ireland

Reform came fairly swiftly for Ireland after the publication of OECD's BEPS report in 2013. By October of 2014, Ireland had experienced severe pressure from the European Commission to address its many tax regulations that had made the country a tax haven.[72] One of the measures Ireland took to satisfy the EU's requests was a change in the tax law that had made the Double Irish, Dutch Sandwich possible. Under the new law, companies that are located within Ireland will have to pay taxes in Ireland unless they're operating under a tax treaty Ireland has with another country.[73] Ireland gave all companies making use of the Double Irish, Dutch Sandwich until 2020 to close any use of the tax scheme.[74]

While Ireland's elimination of the Double Irish, Dutch Sandwich was in line with efforts to minimize hybrid mismatch arrangements across Europe, other tax reforms within Ireland are moving at varying speeds to fall in line with the EU's adoption of OECD guidelines.[75] Firstly, Ireland has announced no intention of moving away from its 12.5% corporate tax rate. Similarly, Ireland has been slow to adopt the EU's Anti-Tax Avoidance Directive, some of which contains proposed regulation related to hybrid mismatch arrangements.[76] While Ireland's main issue with the directive is the interest limitation section, the country has still been slow to adopt hybrid mismatch legislation.

Also, Ireland did not have any effective legislation in regard to reverse hybrid mismatches until January of 2022.[77] A report on the study of reverse hybrid mismatches in Ireland was not published and analyzed until the first quarter of 2021.[78] Ireland has also made small concessions on exemptions to their CFC rules through the EU's Finance Act of 2020.[79] Ireland's recent legislation has been

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[72] *See* Srivastava et al., *supra* note 35.

[73] Michael Pesta & Brian Barner, *Reports of the Double Irish's Death Are Greatly Exaggerated*, Tax Adviser, (April 30, 2015), https://www.thetaxadviser.com/issues/2015/may/tax-clinic-04.html.

[74] Srivastava et al., *supra* note 35.

[75] Ernst & Young Global Ltd., *Ireland Publishes Updated Corporation Tax Roadmap*, EY Global Tax Alert (Jan. 21, 2021), https://www.ey.com/en_gl/tax-alerts/ireland-publishes-updated-corporation-tax-roadmap.

[76] *Id.*

[77] *Id.*

[78] *Id.*

[79] *Id.*

proposed over five years from the publication of OECD's recommendations regarding hybrid mismatch arrangements.

B. Reformation in the Netherlands

The Netherlands has also been somewhat slow to adopt recommendations regarding hybrid mismatch arrangement tax avoidance schemes within the country, even though the country supported the findings of the OECD BEPS project from the beginning of the study.[80] With the introduction of the EU's Anti-Tax Avoidance Directive ("ATAD"), the Netherlands officially adopted the recommendations pushed by the U.S. in 2019, the deadline set by the EU for all member states to adopt the directive.[81] A second directive, ATAD II, also brought tax reform to the Netherlands, with the second reform having a heavier focus on addressing concerns with hybrid mismatch arrangements.[82]

The tax plans adopted in tandem with the provisions in ATAD and ATAD II attracted businesses and MNEs to the Netherlands while still collecting taxes.[83] This scheme included a reduction of the corporate income tax rate to 21% and the abolishment of the Dividend Withholding Act, which provided tax rates on dividends.[84] Meanwhile, the ATAD assisted with making the Netherlands less susceptible to hybrid mismatch schemes.[85] Under the directive, the Netherlands adopted tax rules fairly similar to the recommendations set forth in the OECD BEPS report.[86] However, while the OECD report limited the number of transactions that would need monitoring by providing detailed situations calling for hybrid mismatch analysis, most of the laws in the Netherlands' tax scheme, as

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[80] Jian-Cheng Ku & Rhys Bane, *Dutch Implementation Proposal on EU Anti-Hybrid Measures*, DLA PIPER (July 12, 2019), https://www.dlapiper.com/en/belgium/insights/publications/2019/07/global-tax-alert-dutch-implements-proposal-on-eu-anti-hybrid-measures/.

[81] Michael Molinaars et al., *Tax Alert: Adoption 2019 Tax Plan and ATAD 1 proposal by the Dutch Lower House of Parliament*, STIBBE (Nov. 16, 2018), https://www.stibbe.com/publications-and-insights/tax-alert-adoption-2019-tax-plan-and-atad-1-proposal-by-the-dutch-lower.

[82] Ku & Bane, *supra* note 81.

[83] *Id.*

[84] PricewaterhouseCoopers, *Dutch Government Provides Further Guidance on ATAD Implementation, Tax Avoidance Measures*, TAX INSIGHTS (Mar. 6, 2018), https://www.pwc.com/us/en/tax-services/publications/insights/assets/pwc-dutch-government-provides-further-guidance-on-atad-implementation.pdf.

[85] *Id.*

[86] *Id.*

well as the recommendations in the directive, do not specify certain situations which could potentially allow a transaction that appears to cause a double deduction or deduction with no income inclusion to be up for review within the country.[87] Apart from adopting ATAD II, the Netherlands still has many other tax plans that have made performing hybrid mismatch arrangements possible.

III. TAX ISSUES UNSOLVED

While tax reform in Ireland and the Netherlands was able to effectively shut down the Double Irish, Dutch Sandwich, new tax avoidance schemes came up in the jurisdictions fairly quickly. Even with all of the efforts made by the Netherlands to be less of a tax haven, struggles in the country have kept it high on the list of most tax haven-like countries in Europe. While there are still many issues with hybrid mismatch arrangements rising out of all the tax reforms, below are three proposed regulations that could assist in solving hybrid mismatch tax avoidance, following the highlighted struggles to adapt to OECD and EU recommendations in Ireland and the Netherlands.

A. New Tax Avoidance Schemes

As soon as the Double Irish, Dutch Sandwich scheme was effectively terminated, MNEs started looking for tax avoidance alternatives. While some of these MNEs, like Google, took a while before officially making a transfer to a new tax scheme, other companies, like Apple, made quicker work of the task.[88] Of the hybrid mismatch tax avoidance schemes that have become popular since the demise of the Double Irish, Dutch Sandwich, the Double Irish Single Malt and the Green Jersey are the most notable.

i. Double Irish Single Malt

The Double Irish Single Malt effectively worked as a substitute to the Double Irish, Dutch Sandwich, having a similar structure except for the elimination of the Netherlands and with the end location being in Malta.[89] The scheme was made possible under the tax treaty structure common between Ireland and many other countries. Under these treaties, Irish companies could move their

[87] *Id.*

[88] *See* Fonseca, *infra* note 90.

[89] Jacob Fonseca, *The Rise of ESG Investing: How Aggressive Tax Avoidance Affects Corporate Governance & ESG Analysis*, 25 ILL. BUS. L.J. 1, 13–14 (2020).

management location to any country that had a double tax treaty with Ireland.[90] This move to another country would allow the entity to pay taxes in the new jurisdiction.[91] To reuse CorpA, whose subsidiary SubB was an Irish company, CorpA would be able to transfer management of SubB to another country, that country being Malta, and pay taxes there.

In theory, CorpA's funds that were transferred to SubB would now be subject to Maltese tax laws. However, the Maltese tax code only requests taxes on payments that were remitted in Malta.[92] If the payments were not remitted in the country, then the funds would not be taxed. Such a scheme led to a double no inclusion format for companies like Apple that employed the tax avoidance strategy.[93] The strategy was very popular with U.S.-based technological companies, including Microsoft.[94]

As the Single Malt began to become more obvious, efforts were made to stop the use of this tax scheme. OECD released the Multilateral Instrument format shortly after the publication of its BEPS report.[95] The instrument's purpose is to help reduce the prevalence of treaty terms that allow for hybrid mismatch arrangements by pointing out such treaty terms to countries.[96] When the double non-taxation was made evident to Ireland and Malta, the two countries agreed to follow protocols or enact protocols that would cut off the possibility of such a tax avoidance scheme.[97] Since both countries have made efforts to deal with the Maltese tax avoidance schemes, the practice of the Single Malt has in theory been brought to a close as of 2019.[98] However, this was not the only tax avoidance scheme that arose after the announced closure of the Double Irish, Dutch Sandwich.

ii. The Green Jersey

While some companies attempted to use the Single Malt structure, other companies, like Apple, immediately made a shift to a tax structure known as the

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[90] *Id.*

[91] *Id.* at 14.

[92] *Id.*

[93] *Id.*

[94] *Id.*

[95] William Fogarty, *End of the "Single Malt" and Start of a New Era?*, MAPLES GRP. (Nov. 28, 2018), https://thoughts.maples.com/post/102f6gf/end-of-the-single-malt-and-start-of-a-new-era.

[96] *Id.*

[97] *Id.*

[98] *Id.*

Green Jersey. While all companies were made aware of the closing of the Double Irish, Dutch Sandwich scheme in 2014, Apple had more incentive to fix their taxation planning in Ireland.[99] In 2013, the EU launched an investigation into Apple's tax payments in Ireland. This investigation came about because of a noticeable lack of tax collection from Apple activity in Europe, activity that totaled over $30 billion in revenue in 2016. With an impending lawsuit and pressure from the EU to do away with the Double Irish, Dutch Sandwich scheme, Apple had to move its money to a new location or else pay the corporate tax rate in Ireland, incurring a tax bill close to $4 billion.[100]

To combat this problem, Apple started forum shopping for a new tax haven home. Apple's forum shopping brought them to Jersey, a small Island under the UK crown that is allowed to establish its own tax laws separate from Great Britain and that has an effective corporate tax rate of 0%.[101] Once the tax haven was found, Apple worked on transferring billions of dollars and the residencies of its Ireland subsidiaries to the island.[102] Some of the transfer was made through IP licensing arrangements, which was a popular transfer method under the Double Irish, Dutch Sandwich.[103] Another transfer method that Apple started using was debt. Apple would effectively take a loan from the corporation located in Jersey and pay it back at the end of the year with interest.[104] The payment and interest would be considered deductible in Ireland but would not be taxed upon arrival in Jersey.[105]

The tax rate Apple was able to enjoy from the scheme in the EU ranged somewhere between 1.7% and 8.8%.[106] However, some calculations suggest that Apple may have been able to enjoy a tax rate below 1% in the EU through the use of some other tax provisions.[107] Apple's use of this scheme became public knowledge because of leaked documents called the Paradise Papers.[108] The papers showed that Apple had been employing the Green Jersey tax avoidance scheme since 2015, as Apple was quick to move on from the Double Irish, Dutch

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[99] *See* Fonseca, *supra* note 90.

[100] Emma Clancy, *Apple, Ireland And The New Green Jersey Tax Avoidance Technique*, SOC. EUR. (July 4, 2018), https://www.socialeurope.eu/apple-ireland-and-the-new-green-jersey-tax-avoidance-technique.

[101] *Id.*

[102] *Id.*

[103] *Id.*

[104] *Id.*

[105] *Id.*

[106] *Id.*

[107] *Id.*

[108] *Id.*

Sandwich.[109] Apple is not the only corporation to apply the Green Jersey. Ireland has received harsh criticisms for having welcomed the incorporation of the tax scheme in Ireland, as it is a treaty with Jersey that has made the tax scheme possible.[110] It's important to note that Ireland also experienced an increase in GDP when Apple shifted its IP to the Irish companies, which is a possible reason Ireland has not effectively made tax strategies against the Green Jersey yet.[111]

Both the Single Malt and the Green Jersey are examples of how there is still a lot of room for improvement despite Ireland making some efforts to curtail hybrid mismatch arrangements. Most notably, the tax treaties Ireland has established with multiple other countries both within and outside of Europe often contain clauses that allow for situations like the Green Jersey or the Single Malt to come to fruition. As long as such tax treaties are in force, new tax avoidance schemes will keep popping up within Ireland and some other treaty-related countries. Because of these treaties and the slow uptake of recommendations from OECD and ATAD, Ireland has remained in the top ten in terms of countries operating as tax havens.

B. Issues in the Netherlands

While the Netherlands is no longer engaged in the notorious Double Irish, Dutch Sandwich tax avoidance scheme and has made significant moves to limit hybrid mismatch arrangements within the country, the Netherlands is still listed as one of the top ten tax havens in the world.[112] The Netherlands still holds such a title for various reasons.

Firstly, the Netherlands currently allows multinational corporations or other entities to negotiate with the Dutch government when it comes to taxable income on the corporate level.[113] For a company such as Walt Disney, this would be equivalent to Disney being able to approach Dutch officials and negotiate which parts of their profits would be subjectable to the corporate tax rate. The use of this system by Starbucks resulted in the sheltering of around €20 million before the EU, through the European Commission, found Starbuck's tax avoidance to be

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[109] *Id.*

[110] *Id.*

[111] *Id.*

[112] Samantha Dixon, *The Netherlands is a top-three tax haven for multinationals and the super-rich*, DUTCHREVIEW (Nov. 23, 2020), https://dutchreview.com/news/the-netherlands-is-a-top-three-tax-haven-for-multinationals-and-the-super-rich/.

[113] Iven De Hoon, *Is the Netherlands a tax haven?*, NO MORE TAX, https://nomoretax.eu/netherlands-tax-haven/ (last visited May 21, 2022).

illegal under State Aid Regulations.[114] While this issue might not relate directly to hybrid mismatch arrangements, it still shows profit-shifting mechanisms at work that attract companies trying to avoid paying taxes to the Netherlands.

Secondly, the Netherlands has a rather optimizable taxation scheme. This essentially allows companies to craft their tax liability in the country by making use of what have effectively been termed "mailbox companies," companies that essentially exist to shelter funds and work around the Netherland's tax code.[115] The country currently contains roughly 12,000 such companies that have allowed for the channeling of roughly €4 billion every year.[116] The country also has a subsidies system that allows companies to reduce their corporate tax rate for programs with economic benefits to the Netherlands, such as innovation.[117]

Perhaps most relevant to hybrid mismatch arrangements is the fact that the Netherlands provides no tax rate for certain hybrid financial instruments.[118] While the employed recommendations from the ATAD are meant to prevent any instances where a hybrid mismatch results in income not being included in taxation, the Netherlands has yet to provide any firm laws or instances proving that previously untaxed financial instruments are now subjected to taxation within the country.[119] All of these, as well as other tax schemes in the Netherlands, lands it in the top ten in the world for countries that operate as tax havens.

C. Proposed Reforms

While adoption of tax legislation similar to OECD's recommendations from their BEPS report has curtailed previously popular tax avoidance schemes such as the Double Irish, Dutch Sandwich, MNEs and other similar corporations have simply shifted to new tax avoidance schemes. In order for hybrid mismatch arrangements as tax avoidance mechanisms to be curtailed, adoption of the three recommended regulations below would be needed. Along with the adoption of an equalized tax rate across all international orders, enforcement of more equalized tax treaties would be needed along with a simpler information sharing system in order to prevent issues with double penalization and the like.

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[114] *Id.*
[115] *Id.*
[116] *Id.*
[117] *Id.*
[118] *Id.*
[119] *Id.*

i. Equalized Tax Rates Across the Globe

In order to reduce and even potentially end the loss of tax dollars through hybrid mismatch arrangements, an equalized tax rate would need to be established internationally. While such regulation might seem impossible and violative of independent national sovereignty, such legislation would need to be adopted in order to effectively curtail hybrid mismatch arrangements. Within months after the closing of the Double Irish, Dutch Sandwich, companies such as Apple and Google had found other means to avoid paying higher tax rates. While action has already been taken to curtail the effects of the Single Malt, the Green Jersey is still fairly unregulated. Many other avenues are still being taken to harbor money in tax havens, such as the islands of the Caribbean. As long as the tax rates differ to such an enormous extent, companies will keep trying to find ways to reduce their tax burden.

Such an equalized tax rate standard might seem like an impossible task. However, efforts from the EU have already shown that standardized tax plans are possible. Even though it took a few years, the EU was able to promote the ATAD and similar tax legislation among the organization's member states.[120] Ireland and the Netherlands, both notorious tax havens, are set to have ATAD II or similar legislation in place by 2022.[121] Along with the promotion of such tax standards, the EU has also been successful in curtailing the famous Double Irish, Dutch Sandwich. Other organizations are also making efforts to promote more standard tax schemes.

The best example of the EU's possible assistance in focusing on an equalized tax rate is its Common Consolidated Corporate Tax Base ("CCCTB") tax plan that it has aimed to implement since 2011.[122] Under the tax rules, companies involved in cross-border interactions will only need to submit to one set of taxation rules for all interactions with member-states of the EU.[123] When the CCCTB was initially proposed in 2011, sentiments amongst the EU's member states weren't in favor of the tax plan. However, a relaunch in 2016 has proven to be much more fruitful,

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[120] *See* Ernst & Young Global Ltd., *supra* note 76.

[121] *Id.*

[122] *Common Consolidated Corporate Tax Base (CCCTB)*, EUR. COMM'N, https://ec.europa.eu/taxation_customs/business/company-tax/common-consolidated-corporate-tax-base-ccctb_en (last visited Feb. 19, 2022).

[123] *Id.*

with key changes that are more likely to be a success.[124] One of those key changes would be for MNEs' participation in the tax plan to be mandatory.[125]

The creation of the CCCTB tax plan and the successful application of pressure to change tax loopholes by the European Commission are just a few examples of efforts in Europe to establish a continentally equalized tax plan that is still a good deal for corporations but prevents the loss of tax dollars through tax avoidance schemes. While there was decent pushback against the CCCTB in 2011, there has been less since its reintroduction. While independent national sovereignty is important, implementing a tax scheme that is more equalized across countries, and eventually the globe, will actually help all countries get more tax dollars that they should already be receiving from corporations.

ii. Rescission of Uneven Tax Treaties

Of all of the tax avoidance schemes mentioned in this paper, there is an obvious, dominating trend among them. Tax treaties that grant special tax privileges to corporations that interact with certain countries in certain ways allow corporations to reduce their tax burdens by up to nearly 100%. As long as such tax treaties are allowed to be made between countries, there will most likely be new tax avoidance schemes popping up in various tax haven locations.

In order to combat this issue, tax treaties that allow for a significant reduction in taxes, depending on the form the treaty takes, should be stopped. Tax treaties have long been operated to reduce tax burdens to the lowest percentage possible.[126] As such, any existence of a tax treaty with that aim will attract MNEs to the tax treaty's associated countries, as the results in Ireland have consistently shown. Recognizing that it would be highly improbable to completely remove all tax treaties worldwide, more focus could be given to simply reducing tax treaty clauses that allow for tax avoidance schemes to ensue. Most importantly, these tax treaties would need to be changed to make it impossible for income to go untaxed or for the same income to receive double deductions through the tax treaty.

Such a policy will quite likely have severe pushback by countries that have been able to make use of such treaties. While the pushback would be severe, obtaining more equitable terms in tax treaties should be possible under the same format as a global equitable tax rate. The EU has had much success in encouraging and enforcing equitable tax rates in Europe, evidenced by its successful

[124] *Id.*

[125] *Id.*

[126] Julie Roin, *Rethinking Tax Treaties in a Strategic World with Disparate Tax Systems*, 81 VA. L. REV. 1755 (1995).

involvement in encouraging change in the Irish and Dutch tax codes since the publication of OECD's report.[127] While tax treaties need not be completely abolished, organizations like the EU and other global organizations could encourage tax treaties that have clauses that would cause serious loss in tax revenue to be amended.

iii. Establish Simpler Information Reports

While the OECD recommendations given from the BEPS report aim to reduce tax avoidance, the recommendations often note that countries might need to implement simpler forms of the recommendations to make tracking potential hybrid mismatch arrangements easier.[128] Tracking the arrangements would be easiest by making use of an information system that is as simplified and as inclusive as possible.

Under the proposed OECD rules, countries have to be careful in tracking where a hybrid instrument is coming from and the rules of its payer jurisdiction to make sure that the payee jurisdiction does not allow a double deduction to occur.[129] However, the payer jurisdiction also has to be careful to track the payee jurisdiction's tax rules so the corporation is not double taxed on one hybrid instrument.[130] In order to avoid such mishaps, the OECD recommendations call for "appropriate tax filing and information reporting requirements" in order to properly determine the payment's taxability.[131] If every single country comes up with its own system to track such information, the amount of time spent in filling out such reports and the likelihood of mix-ups and confusion between reporting systems would likely cause great distress to corporations. It will also likely lead to corporations avoiding certain markets if the paperwork proves to be more of a bother than the market is worth.

A global reporting system with the same standards from country to country would overcome such a difficulty. Such a reporting system would also fit well with an equalized global tax plan, making information reporting easier and more accessible to corporations all over the world. Implementing such a system would be beneficial to all countries but would probably not be possible without the co-adoption of the equalized global tax plan.

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[127] *See* Fonseca, *supra* note 90.

[128] *See Action 2 Report*, *supra* note 9, at 195.

[129] *Id.*

[130] *Id.*

[131] *Id.* at 9.

iv. *Allow Tax Avoidance Schemes*

While OECD put together a report to help reduce tax base erosion and profit shifting, there is an argument for allowing tax avoidance schemes like the now-defunct Double Irish, Dutch Sandwich to exist. Such tax schemes have helped boost the economy of individual countries, as evidenced by Ireland's GDP spike after Apple's adoption of the Green Jersey.[132] While billions of dollars are being withheld from taxes because of hybrid mismatch arrangements, the countries harboring the money have been given more jobs and usually have some of that lost tax money filtering into their economies.

While tax haven countries might experience a benefit, that benefit would ultimately be offset by the corporations paying their taxes. Ireland's GDP did have a significant increase, but the country ultimately would have made more money if the corporations harbored in the country paid Ireland's corporate tax.[133] Instead, the money sat in offshore accounts or Jersey, with the corporations contributing very little to the countries that have made it possible for them to build their corporations. So, while these tax avoidance schemes could be left alone, it would ultimately be more beneficial internationally to stop the use of tax avoidance schemes and put an end to double deduction and non-inclusion tax outcomes.

CONCLUSION

Ultimately, the recommendations that came out of OECD'S BEPS report were somewhat useful in encouraging actions that helped reduce the occurrence of hybrid mismatch arrangements in Europe. The report led to the eventual closing of the Double Irish, Dutch Sandwich tax avoidance scheme and, since the report's publication, both Ireland and the Netherlands, along with multiple other countries within the EU and across the globe, have taken measures to reduce the number of hybrid mismatch arrangements that are resulting in corporations receiving double deductions on income or resulting in corporations avoiding the inclusion of income in their tax burdens altogether.

While the recommendations have spurred action, there is still much to be done to curtail hybrid mismatch arrangements as a way to avoid taxes. While new legislation has been adopted, multiple other tax avoidance schemes have come to fruition, some accomplishing the same level of tax avoidance as was possible under the Double Irish, Dutch Sandwich. Action has been taken against these tax avoidance schemes, but it seems a new scheme is bound to appear as soon as

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[132] *See* Clancy, *supra* note 101.

[133] *See id.*

legislation is adopted to end the old scheme. If countries around the globe truly wish to be successful at stopping the shirking of tax obligations by corporations, countries will have to move in the direction of adopting tax rules that will equalize the tax burdens implemented by countries globally. While this will not be an easy feat, it is accomplishable.