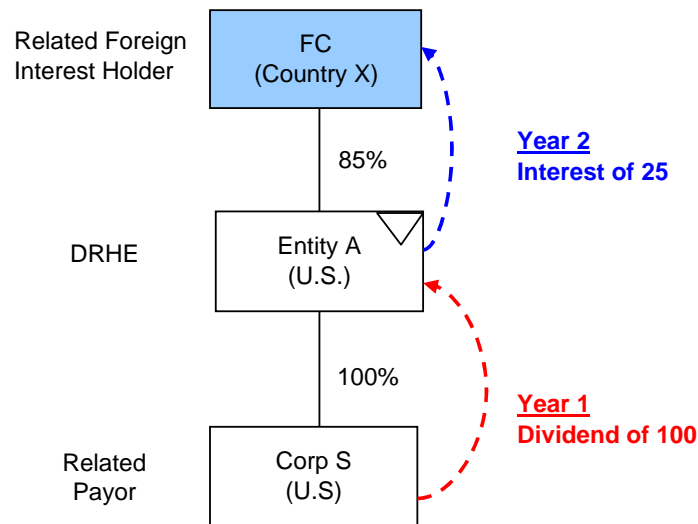


**Interest Paid by DRHE to
Related Foreign Interest Holder**



▽ Domestic reverse hybrid entity ("DRHE") - Not fiscally transparent (not "flow-thru") for U.S. tax purposes but fiscally transparent for foreign tax purposes.

The facts are the same as in Example 2, except the \$100 dividend income received by A in year 1 is from A's wholly-owned subsidiary, S. The analysis is the same as in Example 1 with respect to the \$100 dividend payment from S to A. However, the \$25 interest payment in year 2 by A to FC will be treated as a dividend to the extent the payment does not exceed FC's share of the \$100 dividend payment made by S to A (\$85). FC is entitled to the reduced rate applicable to dividends under the U.S.-Country X income tax treaty with respect to the \$25 payment. A is not entitled to an interest deduction.

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