European Commission - Press release

State aid: Commission opens formal investigation into Luxembourg's tax treatment of McDonald's

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The Commission has opened a formal probe into Luxembourg's tax treatment of McDonald's.Its preliminary view is that a tax ruling granted by Luxembourg may have granted McDonald's an advantageous tax treatment in breach of EU State aid rules

In particular, the Commission will assess whether Luxembourg authorities selectively derogated from the provisions of their national tax law and the Luxembourg-US Double Taxation Treaty and thereby gave McDonald's an advantage not available to other companies in a comparable factual and legal situation.

Commissioner Margrethe Vestager, in charge of competition policy, stated: *"A tax ruling that agrees to McDonald's paying no tax on their European royalties either in Luxembourg or in the US has to be looked at very carefully under EU state aid rules. The purpose of Double Taxation treaties between countries is to avoid double taxation – not to justify double non-taxation."*

On the basis of two tax rulings given by the Luxembourg authorities in 2009, McDonald's Europe Franchising has paid no corporate tax in Luxembourg since then despite recording large profits (more than €250 million in 2013). These profits are derived from royalties paid by franchisees operating restaurants in Europe and Russia for the right to use the McDonald's brand and associated services. The company's head office in Luxembourg is designated as responsible for the company's strategic decision-making, but the company also has two branches, a Swiss branch, which has a limited activity related to the franchising rights, and a US branch, which does not have any real activities. The royalties received by the company are transferred internally to the US branch of the company.

The Commission requested information on the tax rulings in summer 2014 following press allegations of advantageous tax treatment of McDonald's in Luxembourg. Subsequently, trade unions presented additional information to the Commission. The Commission's assessment thus far has shown that in particular due to the second tax ruling granted to the company **McDonald's Europe Franchising has virtually not paid any corporate tax in Luxembourg nor in the US on its profits** since 2009. In particular, this was made possible because:

A **first tax ruling** given by the Luxembourg authorities in March 2009 confirmed that McDonald's Europe Franchising was not due to pay corporate tax in Luxembourg on the grounds that the profits were to be subject to taxation in the US. This was justified by reference to the Luxembourg-US Double Taxation Treaty. Under the ruling, McDonald's was required to submit proof every year that the royalties transferred to the US via Switzerland were declared and subject to taxation in the US and Switzerland.

However, contrary to the assumption of the Luxembourg tax authorities when they granted the first ruling, the profits were **not** to be subjected to tax in the US. While under the proposed reading of Luxembourg law, McDonald's Europe Franchising had a taxable presence in the US, it did not have any taxable presence in the US under US law. Therefore McDonald's could not provide any proof that the profits were subject to tax in the US, as required by the first ruling (see further details below).

McDonald's clarified this in a submission requesting a second ruling, insisting that Luxembourg should nevertheless exempt the profits not taxed in the US from taxation in Luxembourg. The Luxembourg authorities then issued a **second tax ruling** in September 2009 according to which McDonald's no longer required to prove that the income was subject to taxation in the US. This ruling confirmed that the income of McDonald's Europe Franchising was not subject to tax in Luxembourg even if it was confirmed not to be subject to tax in the US either.

With the second ruling, Luxembourg authorities accepted to exempt almost all of McDonald's Europe Franchising's income from taxation in Luxembourg.

McDonald's' arguments vis-à-vis the Luxembourg tax authorities

Companies are generally liable to pay corporate taxes on profits recorded in a country if they have a taxable presence in the country (a so-called "permanent establishment"). This requires the company to have a certain level of business activities there.

In their discussions with the Luxembourg authorities, McDonald's argued that the US branch of McDonald's Europe Franchising **constituted a "permanent establishment" under Luxembourg law**, because it had sufficient activities to constitute a real US presence. Simultaneously, McDonald's argued that its US-based branch **was not a "permanent establishment" under US law** because, from the perspective of the US tax authorities, its US branch did not undertake sufficient business or trade in the US.

As a result, the Luxembourg authorities **recognised** the McDonald's Europe Franchising's US branch as the place where most of their profits should be taxed, whilst US tax authorities **did not recognise** it. The Luxembourg authorities therefore exempted the profits from taxation in Luxembourg, despite knowing that they in fact were not subject to tax in the US.

The scope of the Commission's investigation

The Commission will now investigate further to see if its concerns are justified that in particular the second tax ruling provided McDonald's Europe Franchising with a favourable tax treatment in breach of EU state aid rules.

In particular, the Commission will assess whether Luxembourg authorities selectively derogated from the provisions of their national tax law and the Luxembourg-US Double Taxation Treaty and whether thereby the Luxembourg authorities gave McDonald's an advantage not available to other companies in a comparable factual and legal situation. This investigation does not call into question the general tax regime of Luxembourg.

The opening of an in-depth investigation gives interested third parties and the Member States concerned an opportunity to submit comments. It does not prejudge the outcome of the investigation.

Background

According to Article 107(1) of the Treaty on the Functioning of the European Union (TFEU), state aid which affects trade between Member States and threatens to distort competition by favouring certain undertakings is in principle incompatible with the EU Single Market.

Tax rulings as such are not a problem under EU state aid rules if they simply confirm that tax arrangements between companies within the same group comply with the relevant tax legislation. However, tax rulings that confer a selective tax advantage to specific companies, and so give them a subsidy, can seriously distort competition within the EU's Single Market and violate EU state aid rules.

Since June 2013, the Commission has been investigating the tax ruling practices of Member States. It extended this information inquiry to all Member States in December

2014. The Commission in October 2015 decided that tax rulings for Fiat in Luxembourg and Starbucks in the Netherlands granted illegal selective tax advantages to the companies in breach of EU state aid rules. The Commission also has ongoing in-depth state aid investigations into tax rulings concerning Apple in Ireland, Amazon in Luxembourg and Belgium's "excess profit" ruling system.

The non-confidential version of the decision to open the investigation will be made available under the case number SA.38945 in the State Aid Register on the competition website once any confidentiality issues have been resolved. New publications of state aid decisions on the internet and in the Official Journal are listed in the State Aid Weekly e-News.

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