HIGH COURT OF AUSTRALIA

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Details of Filing

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IN THE HIGH COURT OF AUSTRALIA
MELBOURNE REGISTRY

M98, M100 and M101 of 2024

BETWEEN:

COMMISSIONER OF TAXATION
Appellant
and
PEPSICO, INC.
Respondent

M99, M102 and M103 of 2024

BETWEEN:

COMMISSIONER OF TAXATION
Appellant
and
STOKELY VAN CAMP, INC.
Respondent

RESPONDENTS' OUTLINE OF ORAL SUBMISSIONS

PART I – Certification

1. It is certified that this outline of oral submissions is in a form suitable for publication on the Internet.

PART II – Outline of oral submissions

The PepsiCo Group business model

2. Since the early 1900s, the PepsiCo Group has operated under a business model whereby it enters into exclusive bottling appointments (**EBAs**) with local distributors which bottle, market and sell its beverages in a territory. Under the model, the bottler purchases beverage concentrate manufactured by the PepsiCo Group using its highly guarded and valuable beverage formulations and converts it into finished product through what is known as a "cold fill" process.

3. The model drives value for both the bottler and the PepsiCo Group. From the PepsiCo Group's perspective, the group gains access to the bottler's investment in bottling and distribution equipment and its capabilities, including its distribution network, sales force, leadership, and relationships with the trade and local regulatory authorities.

4. The EBAs are generally long term and contain joint commitments by both the PepsiCo Group and the bottler to shared marketing responsibilities to increase volume and market share. In particular, the bottler is required to invest in local advertising and implement that part of the brand building strategy which has been allocated to it.

5. The EBA between **PepsiCo**, Inc. and Schweppes Australia Pty Ltd (**SAPL**) (**PepsiCo EBA**) and the EBA between Stokely-Van Camp, Inc. (**SVC**) and SAPL (**SVC EBA**) conformed to this model. Under each of them, SAPL was required to maximise sales of PepsiCo and SVC products and amplify the brands in the Australian market.

6. Moshinsky J (at first instance, TJ[248]) and Colvin J (on appeal, FFC[195]) erred in approaching the matter on the basis that, because the intellectual property owned by PepsiCo and SVC was valuable, SAPL should be assumed to have paid a monetary amount for the use of it. This erroneous assumption infected their Honours' reasons in respect of both the royalty withholding tax and diverted profits tax cases. It is maintained by the Commissioner in his appeal to this Court (AS[29]-[30]).

Royalty withholding tax

7. To be liable to royalty withholding tax under s 128B of the *Income Tax Assessment Act 1936* (Cth) (**ITAA 1936**), PepsiCo and SVC must have derived income consisting of a royalty paid to them. The amounts the subject of the notices of withholding tax issued to PepsiCo and SVC were: a) not paid to PepsiCo/SVC; b) not income derived by them; and c) not a royalty. The payments were made for concentrate which was converted into finished product.

8. The mechanics of the concentrate sales were as follows. SAPL agreed under the EBAs to purchase its concentrate requirements from PepsiCo/SVC, or a subsidiary which they might cause to sell the concentrate. PepsiCo and SVC nominated PepsiCo Beverages Singapore Pty Ltd (**PBS**) to sell the concentrate. SAPL placed purchase orders with PBS for the purchase of concentrate. PBS had title to the concentrate which it sold to SAPL in satisfaction of the purchase orders. PBS invoiced SAPL for the goods. SAPL paid PBS in accordance with the invoices.

9. PBS did not sell the concentrate as agent or trustee for PepsiCo or SVC. SAPL owed the purchase price for the concentrate to PBS as seller and not to PepsiCo or SVC. None of the provisions of the EBAs upon which the Commissioner relies disturbs that proposition. It follows that neither PepsiCo nor SVC had a beneficial entitlement to the payments SAPL made to PBS. That is not a matter of characterisation, but a legal conclusion. The payments were therefore not income derived by them.

10. The cases of *Dick Smith Electronics Holdings Pty Ltd* (2005) 221 CLR 496 and *Commissioner of State Revenue (Vic) v Lend Lease Development Pty Ltd* (2014) 254 CLR 142 do not govern the meaning of the expression "consideration for" as it appears in the definition of "royalty" in s 6(1) of the ITAA 1936. Those cases concern provisions which impose a charge on a transaction and look to what was received by the vendor so as to move the transfer of property under that transaction. That test is inapplicable to the definition of "royalty" in s 6(1) which asks what a payment is "for".

11. The correct approach is that adopted by Bennett J in *International Business Machines Corporation v Commissioner of Taxation* (2011) 83 ATR 32 where her Honour answered the question what a payment was for by construing the agreement giving rise to it.

12. The promise SAPL made under the EBAs was to purchase concentrate from PepsiCo/SVC or their nominated "Seller" at certain prices. The transactions giving rise to the payments were the sales themselves (see FFC[13]).

13. Whether one treats the PepsiCo/SVC EBAs as the source of the obligation to make the payments to PBS or the sale contracts between PBS and SAPL evidenced by purchase orders and invoices, there is no ambiguity in any of those agreements. They specified that the amounts were to be paid as the price for the concentrate.

Diverted profits tax

14. **Tax benefit:** Each of the schemes identified by the Commissioner was entry into the EBA on terms that did not provide for a royalty. Any postulate involving entry into the EBAs in a form which provided for a royalty is: a) unreasonable in that it is nothing more than a possibility; and b) would not correspond with the substance of the scheme (s 177CB(4)(a)(i) of the ITAA 1936) (FFC[86]-[87]). In respect of b), the Commissioner's assertion of correspondence between form and substance rests on the false assumption referred to above that SAPL should have paid, or did pay as a matter of economic substance, a royalty for the use of intellectual property.

15. **Purpose:** The Commissioner's alternative postulates are otherwise presented by him as being commercially neutral. On that basis they represent, at best, merely another means of achieving the same or similar commercial outcomes as the schemes. It should not be concluded for the purposes of s 177J(1)(b) of the ITAA 1936 that PepsiCo or SVC entered into the EBAs in the form they took for the principal purpose of obtaining a tax benefit simply because they could have entered into a different form of EBA which would have achieved the same commercial outcomes but would have subjected them to additional tax.

16. The "manner" in which the schemes were entered into or carried out materially replicated a product distribution model deployed by the PepsiCo Group (and others in the industry) for over 100 years. The other nine matters referred to in s 177J(2) are neutral. The Commissioner's assertion of a disparity between the "form and substance" of the scheme rests on the same false assumption referred to above.

Dated: 2 April 2025

E F Wheelahan KC **C M Pierce SC** **A M Haskett**