

PEPSICO V ATO



CASE SUMMARY

FACTS

PepsiCo and its subsidiary entered into exclusive bottling agreements with Schweppes Australia. The agreements included payments from Schweppes to purchase concentrate, and to be appointed an exclusive license to bottle, sell and distribute PepsiCo branded beverages in Australia.

ISSUES

The Federal Court had to consider:

1. Whether the payments made under these agreements included an embedded royalty for the use of PepsiCo's intellectual property and should be subject to royalty withholding tax.
2. Whether the arrangement also triggered diverted profits tax (DPT).

JUDGMENT

A 2-1 majority of the Full Federal Court ruled in favour of PepsiCo, finding that the payments under the agreement did not include an embedded royalty, and that the payments were for the supply of concentrate and not "consideration for" the use of trademarks or intellectual property. The Court also ruled that the DPT provisions did not apply. The Commissioner's proposed alternative was rejected as failing to reflect the commercial and economic reality of the transaction.

EFFECT

The decision may affect Australian businesses with agreements involving foreign intellectual property, especially where no explicit payments for IP use are made. It also challenges the ATO's draft ruling (TR 2024/D1), which assumes embedded royalties exist in such agreements, potentially requiring the ATO to reconsider its position.

NOTE: At time of writing, the High Court has granted the Commissioner special leave to appeal the Full Federal Court's decision.