THE Coca-Cola COMPANY

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To: Michael Plowgian
Deputy Assistant Secretary
Office of Tax Policy
United States Treasury Department
1500 Pennsylvania Avenue, NW
Washington D.C. 20220
Submitted by email: OTP_Pillar1MLC@treasury.gov

Re: *The Coca-Cola Company* response to the October 11, 2023, U.S. Department of the Treasury request for public input on the draft OECD/G20 Inclusive Framework Multilateral Convention to Implement Amount A of Pillar One (Pillar One MLC) and accompanying documents.

Dear Mr. Plowgian:

The Coca-Cola Company is pleased to submit this response to the October 11, 2023, U.S. Department of the Treasury request for public input on the draft OECD/G20 Inclusive Framework Multilateral Convention to Implement Amount A of Pillar One (Pillar One MLC) and accompanying documents released on that date. We would be happy to discuss the contents of this comment letter should you want a further conversation.

Our submission is limited to commenting on the treatment of non-consolidated distributors in applying the Marketing and Distribution Safe Harbor (MDSH), which we believe cannot be justified given the purpose of Amount A and the MDSH. Nonetheless, we acknowledge that there are additional, notable challenges in the broader context of the MDSH.

The MDSH is a bedrock element of Amount A and Pillar One, expressly called for in both the July 1, 2021, and October 8, 2021, *Statements on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalization of the Economy* agreed to by over 135 members of the Inclusive Framework. It is incorporated in the Pillar One MLC.

Many businesses, including in the food and beverage industry, operate through distributors. Distributors may be wholly owned (consolidated), partially owned, or zero percent owned by the company for whom they distribute. However, assuming the economics are the same, the level of ownership in a distributor should not impact the tax treatment under Pillar One.

An underlying premise supporting Pillar One Amount A is that current international tax rules do not allocate sufficient residual profits to market jurisdictions. The MDSH is designed to reduce the Amount A allocation to a market jurisdiction in situations in which the jurisdiction already has taxing rights with respect to residual profits (i.e., an amount in excess of “routine profits”) in that jurisdiction. As described in the Pillar One MLC, the MDSH only applies in circumstances in which a Covered Group distributes products in a jurisdiction through an entity whose results are consolidated with the parent entity, thereby ignoring distribution through non-consolidated entities even when those non-consolidated entities earn similar or higher residual profits in the same jurisdiction. The result is a windfall for market jurisdictions in these circumstances, as well as the creation of significant economic distortions that result from taxing identical activity differently depending on whether a multinational operates through an integrated or non-integrated (“split”) supply chain. We do not believe this distinction is justified as a matter of sound tax policy.

A generally accepted tax policy premise is that the decision whether to operate all aspects of a business through related parties rather than through use of unrelated parties should be motivated by economic rather than tax considerations (i.e., the tax rules should seek to be neutral and equitable between those options). Put simply, taxpayers in similar situations involving similar transactions should be subject to similar levels of taxation. If this premise is not implemented in a given tax policy design, businesses may be compelled to conform their operations to the most efficient tax structure to remain competitive. The current design of the Pillar One MLC encourages companies to structure their operations so that they have sufficient ownership in their local distributors to consolidate the distributor's operations for financial accounting purposes. Only in that circumstance is the MNE Group able to use the MDSH and thereby minimize the likelihood of increased taxes allocable to the market jurisdiction pursuant to Amount A. These economically distortive rules will not provide a durable basis for the future of the international tax system and thus risk the overall operation and viability of Pillar One Amount A.

This issue is not unique to a particular type of business. A wide variety of businesses operate through split-supply chains, with traditional franchise models perhaps being the most prominent. In these models the entrepreneurial profit with respect to the market is negotiated between the MNE and the independent local entrepreneur. As in situations in which distributors are associated and therefore consolidated in the financial accounts of the parent entity, these returns may reward relatively routine or more extensive activities. We do not believe that policy makers intend to create the aforementioned distortions[1] in tax treatment based solely on whether a supply chain is wholly owned. Therefore, we suggest below that the Inclusive Framework implement mechanisms for eliminating such distortions. If not eliminated, this disparity in treatment could make tax considerations a major driver of business supply chain structuring decisions, contrary to sound tax policy.

Thirteen members of the U.S. Congress have also expressed their concern about this aspect of the Pillar One design in a July 31, 2023, letter (attached) to Secretary Yellen, in which they explained:

> *Furthermore, it is our understanding that Pillar One's marketing and distribution safe harbor (MDSH) is hardly safe for U.S. businesses operating under franchise or split-ownership structures. The failure to adequately account for all taxes paid in market jurisdictions under franchise or split-ownership structures would result in U.S. companies over-allocating profits to market jurisdictions with the same appalling result: U.S. businesses will pay more taxes to foreign jurisdictions, and the U.S. government will collect less in tax revenue.*

We suggest that Treasury should engage with the Inclusive Framework and seek to change the MDSH to adopt an approach that takes into account residual profits already in the market in the split supply chain model in order to eliminate the aforementioned distortions. We propose that the MDSH equally applies to split supply chain models that can be supported by reliable data to substantiate the fact that the local market already taxes residual, non-routine returns.

[1] The distortion arises in two directions. First, when the tax rate in the market(s) is higher than the tax rate in the relieving jurisdiction(s). This is generally the case because larger markets can sustain higher tax rates. Nonetheless, a distortion also arises when the tax rate in the market is lower than the tax rate in the principal jurisdiction. In this case, a non-integrated supply chain would bear a lower tax burden than an integrated one. In summary, a MDSH that discriminates between different types of value chains will be distortive, irrespective of the relationship between the tax rates in different jurisdictions.

Proposed Approach

Over the past three years we have spoken to various members of the OECD Secretariat as well as government representatives to explain the issues above. In those discussions, we found that parties were unable to articulate a principle that would cause related and unrelated distributors to be treated differently for purposes of Amount A and the application of the MDSH. Indeed, it was our impression that they were sympathetic to our position. However, for whatever reason, the issue has not been addressed in the Pillar One MLC.

We remain of the view that taxpayers should be entitled to apply the MDSH to split-ownership supply chains by presenting reliable evidence of residual profits already earned and taxed in the market, and we hope that Treasury will now advocate for this result. This could be done by identifying business models that engage in local markets through entrepreneurial local entities that derive market related returns and determining a method for crediting those returns based on the MDSH. If a clear demarcation is needed, the equity method of accounting relied on by Pillar 2 for other purposes could be referenced in determining the minimum threshold for the relationship between the MNE and its in-market affiliate. This issue is not unique to the food and beverage industry, and does occur in many forms of informal and formal franchise arrangements.

We look forward to ongoing discussions with you on this topic and are available to discuss our response, should you have any questions.

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