

COCA COLA CO  
Form 10-Q  
July 28, 2016

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended July 1, 2016

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File No. 001-02217

(Exact name of Registrant as specified in its Charter)

Delaware 58-0628465

(State or other jurisdiction of (IRS Employer  
incorporation or organization) Identification No.)

One Coca-Cola Plaza 30313  
Atlanta, Georgia (Zip Code)

(Address of principal executive offices)

Registrant's telephone number, including area code: (404) 676-2121

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

Indicate by check mark if the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

Class of Common Stock	Outstanding as of July 25, 2016
\$0.25 Par Value	4,316,029,450 Shares

THE COCA-COLA COMPANY AND SUBSIDIARIES

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#### FORWARD-LOOKING STATEMENTS

This report contains information that may constitute "forward-looking statements." Generally, the words "believe," "expect," "intend," "estimate," "anticipate," "project," "will" and similar expressions identify forward-looking statements, which generally are not historical in nature. However, the absence of these words or similar expressions does not mean that a statement is not forward-looking. All statements that address operating performance, events or developments that we expect or anticipate will occur in the future — including statements relating to volume growth, share of sales and earnings per share growth, and statements expressing general views about future operating results — are forward-looking statements. Management believes that these forward-looking statements are reasonable as and when made. However, caution should be taken not to place undue reliance on any such forward-looking statements because such statements speak only as of the date when made. Our Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. In addition, forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our Company's historical experience and our present expectations or projections. These risks and uncertainties include, but are not limited to, those described in Part II, "Item 1A. Risk Factors" and elsewhere in this report and in our Annual Report on Form 10-K for the year ended December 31, 2015, and those described from time to time in our future reports filed with the Securities and Exchange Commission.

## Part I. Financial Information

## Item 1. Financial Statements (Unaudited)

THE COCA-COLA COMPANY AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME  
(UNAUDITED)

(In millions except per share data)

	Three Months Ended		Six Months Ended	
	July 1, 2016	July 3, 2015	July 1, 2016	July 3, 2015
NET OPERATING REVENUES	\$11,539	\$12,156	\$21,821	\$22,867
Cost of goods sold	4,471	4,748	8,540	8,851
GROSS PROFIT	7,068	7,408	13,281	14,016
Selling, general and administrative expenses	3,912	4,204	7,673	8,283
Other operating charges	297	669	608	902
OPERATING INCOME	2,859	2,535	5,000	4,831
Interest income	164	149	308	304
Interest expense	162	128	303	575
Equity income (loss) — net	305	200	397	202
Other income (loss) — net	1,133	1,605	791	1,580
INCOME BEFORE INCOME TAXES	4,299	4,361	6,193	6,342
Income taxes	839	1,250	1,240	1,665
CONSOLIDATED NET INCOME	3,460	3,111	4,953	4,677
Less: Net income (loss) attributable to noncontrolling interests	12	3	22	12
NET INCOME ATTRIBUTABLE TO SHAREOWNERS OF THE COCA-COLA COMPANY	\$3,448	\$3,108	\$4,931	\$4,665
BASIC NET INCOME PER SHARE <sup>1</sup>	\$0.80	\$0.71	\$1.14	\$1.07
DILUTED NET INCOME PER SHARE <sup>1</sup>	\$0.79	\$0.71	\$1.13	\$1.06
DIVIDENDS PER SHARE	\$0.35	\$0.33	\$0.70	\$0.66
AVERAGE SHARES OUTSTANDING	4,323	4,355	4,325	4,360
Effect of dilutive securities	54	53	54	55
AVERAGE SHARES OUTSTANDING ASSUMING DILUTION	4,377	4,408	4,379	4,415

<sup>1</sup> Calculated based on net income attributable to shareowners of The Coca-Cola Company.

Refer to Notes to Condensed Consolidated Financial Statements.

THE COCA-COLA COMPANY AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (UNAUDITED)  
 (In millions)

	Three Months Ended July 1, July 3, 2016 2015		Six Months Ended July 1, July 3, 2016 2015	
CONSOLIDATED NET INCOME	\$3,460	\$3,111	\$4,953	\$4,677
Other comprehensive income:				
Net foreign currency translation adjustment	606	(792 )	329	(2,278 )
Net gain (loss) on derivatives	(138 )	(33 )	(565 )	301
Net unrealized gain (loss) on available-for-sale securities	109	(882 )	161	(1,093 )
Net change in pension and other benefit liabilities	58	40	89	105
TOTAL COMPREHENSIVE INCOME (LOSS)	4,095	1,444	4,967	1,712
Less: Comprehensive income (loss) attributable to noncontrolling interests	11	3	15	6
TOTAL COMPREHENSIVE INCOME (LOSS) ATTRIBUTABLE TO SHAREOWNERS OF THE COCA-COLA COMPANY	\$4,084	\$1,441	\$4,952	\$1,706

Refer to Notes to Condensed Consolidated Financial Statements.

THE COCA-COLA COMPANY AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (UNAUDITED)

(In millions except par value)

	July 1, 2016	December 31, 2015
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$9,647	\$ 7,309
Short-term investments	11,755	8,322
<b>TOTAL CASH, CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS</b>	<b>21,402</b>	<b>15,631</b>
Marketable securities	2,673	4,269
Trade accounts receivable, less allowances of \$354 and \$352, respectively	4,768	3,941
Inventories	3,005	2,902
Prepaid expenses and other assets	3,332	2,752
Assets held for sale	693	3,900
<b>TOTAL CURRENT ASSETS</b>	<b>35,873</b>	<b>33,395</b>
<b>EQUITY METHOD INVESTMENTS</b>	<b>16,215</b>	<b>12,318</b>
<b>OTHER INVESTMENTS</b>	<b>1,284</b>	<b>3,470</b>
<b>OTHER ASSETS</b>	<b>4,370</b>	<b>4,110</b>
PROPERTY, PLANT AND EQUIPMENT, less accumulated depreciation of \$10,469 and \$9,783, respectively	12,663	12,571
TRADEMARKS WITH INDEFINITE LIVES	6,038	5,989
BOTTLERS' FRANCHISE RIGHTS WITH INDEFINITE LIVES	5,616	6,000
GOODWILL	11,204	11,289
<b>OTHER INTANGIBLE ASSETS</b>	<b>831</b>	<b>854</b>
<b>TOTAL ASSETS</b>	<b>\$94,094</b>	<b>\$ 89,996</b>
<b>LIABILITIES AND EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable and accrued expenses	\$10,235	\$ 9,660
Loans and notes payable	13,901	13,129
Current maturities of long-term debt	4,895	2,676
Accrued income taxes	375	331
Liabilities held for sale	138	1,133
<b>TOTAL CURRENT LIABILITIES</b>	<b>29,544</b>	<b>26,929</b>
<b>LONG-TERM DEBT</b>	<b>29,252</b>	<b>28,311</b>
<b>OTHER LIABILITIES</b>	<b>3,963</b>	<b>4,301</b>
<b>DEFERRED INCOME TAXES</b>	<b>4,497</b>	<b>4,691</b>
<b>THE COCA-COLA COMPANY SHAREOWNERS' EQUITY</b>		
Common stock, \$0.25 par value; Authorized — 11,200 shares; Issued — 7,040 and 7,040 shares, respectively	1,760	1,760
Capital surplus	14,710	14,016
Reinvested earnings	66,921	65,018
Accumulated other comprehensive income (loss)	(10,153)	(10,174)
Treasury stock, at cost — 2,725 and 2,716 shares, respectively	(46,601)	(45,066)
<b>EQUITY ATTRIBUTABLE TO SHAREOWNERS OF THE COCA-COLA COMPANY</b>	<b>26,637</b>	<b>25,554</b>
<b>EQUITY ATTRIBUTABLE TO NONCONTROLLING INTERESTS</b>	<b>201</b>	<b>210</b>
<b>TOTAL EQUITY</b>	<b>26,838</b>	<b>25,764</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$94,094</b>	<b>\$ 89,996</b>

Refer to Notes to Condensed Consolidated Financial Statements.

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THE COCA-COLA COMPANY AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (UNAUDITED)  
 (In millions)

	Six Months Ended	
	July 1, 2016	July 3, 2015
<b>OPERATING ACTIVITIES</b>		
Consolidated net income	\$4,953	\$4,677
Depreciation and amortization	903	961
Stock-based compensation expense	119	117
Deferred income taxes	(178)	)643
Equity (income) loss — net of dividends	(224)	)(44 )
Foreign currency adjustments	118	(144 )
Significant (gains) losses on sales of assets — net	(762)	)(1,346 )
Other operating charges	210	609
Other items	(125)	)609
Net change in operating assets and liabilities	(1,194)	)(964 )
Net cash provided by operating activities	3,820	5,118
<b>INVESTING ACTIVITIES</b>		
Purchases of investments	(9,045)	)(6,981 )
Proceeds from disposals of investments	9,518	6,316
Acquisitions of businesses, equity method investments and nonmarketable securities	(723)	)(2,284 )
Proceeds from disposals of businesses, equity method investments and nonmarketable securities	420	413
Purchases of property, plant and equipment	(1,085)	)(1,114 )
Proceeds from disposals of property, plant and equipment	41	33
Other investing activities	(63)	)(139 )
Net cash provided by (used in) investing activities	(937)	)(3,756 )
<b>FINANCING ACTIVITIES</b>		
Issuances of debt	15,947	24,878
Payments of debt	(12,750)	(22,358)
Issuances of stock	1,108	410
Purchases of stock for treasury	(2,156)	)(1,298 )
Dividends	(3,017)	)(2,877 )
Other financing activities	85	115
Net cash provided by (used in) financing activities	(783)	)(1,130 )
<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>	238	(385 )
<b>CASH AND CASH EQUIVALENTS</b>		
Net increase (decrease) during the period	2,338	(153 )
Balance at beginning of period	7,309	8,958
Balance at end of period	\$9,647	\$8,805

Refer to Notes to Condensed Consolidated Financial Statements.



THE COCA-COLA COMPANY AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. They do not include all information and notes required by generally accepted accounting principles for complete financial statements. However, except as disclosed herein, there has been no material change in the information disclosed in the Notes to Consolidated Financial Statements included in the Annual Report on Form 10-K of The Coca-Cola Company for the year ended December 31, 2015.

When used in these notes, the terms "The Coca-Cola Company," "Company," "we," "us" or "our" mean The Coca-Cola Company and all entities included in our condensed consolidated financial statements. In the opinion of management, all adjustments (including normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six months ended July 1, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. Sales of our nonalcoholic ready-to-drink beverages are somewhat seasonal, with the second and third calendar quarters accounting for the highest sales volumes. The volume of sales in the beverage business may be affected by weather conditions.

Each of our interim reporting periods, other than the fourth interim reporting period, ends on the Friday closest to the last day of the corresponding quarterly calendar period. The second quarter of 2016 and 2015 ended on July 1, 2016 and July 3, 2015, respectively. Our fourth interim reporting period and our fiscal year end on December 31 regardless of the day of the week on which December 31 falls.

Effective January 1, 2016, we transferred Coca-Cola Refreshments' ("CCR") bottling and associated supply chain operations in the United States and Canada from our North America segment to our Bottling Investments segment. Accordingly, all prior period segment information presented herein has been adjusted to reflect this change in our organizational structure.

Advertising Costs

The Company's accounting policy related to advertising costs for annual reporting purposes, as disclosed in Note 1 of our 2015 Annual Report on Form 10-K, is to expense production costs of print, radio, television and other advertisements as of the first date the advertisements take place. All other marketing expenditures are expensed in the annual period in which the expenditure is incurred.

For interim reporting purposes, we allocate our estimated full year marketing expenditures that benefit multiple interim periods to each of our interim reporting periods. We use the proportion of each interim period's actual unit case volume to the estimated full year unit case volume as the basis for the allocation. This methodology results in our marketing expenditures being recognized at a standard rate per unit case. At the end of each interim reporting period, we review our estimated full year unit case volume and our estimated full year marketing expenditures in order to evaluate if a change in estimate is necessary. The impact of any changes in these full year estimates is recognized in the interim period in which the change in estimate occurs. Our full year marketing expenditures are not impacted by this interim accounting policy.

Hyperinflationary Economies

A hyperinflationary economy is one that has cumulative inflation of 100 percent or more over a three-year period. In accordance with U.S. GAAP, local subsidiaries in hyperinflationary economies are required to use the U.S. dollar as their functional currency and remeasure the monetary assets and liabilities not denominated in U.S. dollars using the rate applicable to conversion of a currency for purposes of dividend remittances. All exchange gains and losses resulting from remeasurement are recognized currently in income.

Venezuela has been designated as a hyperinflationary economy. In February 2015, the Venezuelan government announced that the two previously used currency conversion mechanisms had been merged into a single mechanism called SICAD and introduced a new open market exchange rate system, SIMADI. Management determined that the

SIMADI rate was the most appropriate legally available rate and remeasured the net monetary assets of our Venezuelan subsidiary, resulting in a charge of \$27 million recorded in the line item other income (loss) — net in our condensed consolidated statement of income during the six months ended July 3, 2015.

In addition to the foreign currency exchange exposure related to our Venezuelan subsidiary's net monetary assets, we also sell concentrate to our bottling partner in Venezuela from outside the country. These sales are denominated in U.S. dollars. During the six months ended July 3, 2015, as a result of the continued lack of liquidity and our revised assessment of the U.S. dollar value we expected to realize upon the conversion of Venezuelan bolivars into U.S. dollars by our bottling partner to pay our concentrate sales receivables, we recorded a write-down of \$56 million in the line item other operating charges in our condensed consolidated statement of income.

We also have certain U.S. dollar denominated intangible assets associated with products sold in Venezuela. As a result of the Company's revised expectations regarding the convertibility of the local currency, we recognized an impairment charge of \$52 million during the six months ended July 3, 2015, recorded in the line item other operating charges in our condensed consolidated statement of income.

During the six months ended July 1, 2016, the Venezuelan government devalued its currency and changed its official and most preferential exchange rate, which should be used for purchases of certain essential goods, to 10 bolivars per U.S. dollar from 6.3. The official and most preferential rate is now known as DIPRO and the SICAD rate has been eliminated. The Venezuelan government also announced that the SIMADI rate would be replaced by the DICOM rate, which will be allowed to float freely and is expected to fluctuate based on supply and demand. As a result, management determined that the DICOM rate was the most appropriate legally available rate to remeasure the net monetary assets of our Venezuelan subsidiary. As of July 1, 2016, the combined carrying value of the net monetary assets of our Venezuelan subsidiary, the receivables from our bottling partner in Venezuela and the intangible assets associated with products sold in Venezuela was \$149 million.

Despite the additional currency conversion mechanisms, the Company's ability to pay dividends from Venezuela is still restricted due to the low volume of U.S. dollars available for conversion. As a result of the newly announced floating DICOM rate, the Company expects to continue to record losses on foreign currency exchange, may incur additional write-downs of receivables or impairment charges and will continue to record our proportionate share of any charges recorded by our equity method investee that has operations in Venezuela.

#### Recently Issued Accounting Guidance

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers, which will replace most existing revenue recognition guidance in U.S. GAAP and is intended to improve and converge with international standards the financial reporting requirements for revenue from contracts with customers. The core principle of ASU 2014-09 is that an entity should recognize revenue for the transfer of goods or services equal to the amount that it expects to be entitled to receive for those goods or services. ASU 2014-09 also requires additional disclosures about the nature, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments. ASU 2014-09 allows for both retrospective and prospective methods of adoption and will be effective for the Company beginning January 1, 2018. In March 2016, the FASB issued ASU 2016-08, Revenue from Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net), which clarifies the guidance in ASU 2014-09 and has the same effective date as the original standard. During the three months ended July 1, 2016, the FASB issued ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing; ASU 2016-11, Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting; and ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients. These amendments are intended to improve and clarify the implementation guidance of ASU 2014-09 and have the same effective date as the original standard. The Company is currently evaluating the impact that the adoption of these standards will have on our consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The standard was retrospectively adopted by the Company on January 1, 2016. As a result, \$96 million and \$1 million of debt issuance costs at December 31, 2015, were reclassified from other assets to long-term debt and current maturities of long-term debt, respectively.

In November 2015, the FASB issued ASU 2015-17, Income Taxes: Balance Sheet Classification of Deferred Taxes. The amendments in this update simplify the presentation of deferred income taxes and require that deferred tax liabilities and assets be classified as noncurrent in a consolidated statement of financial position. These amendments may be applied either prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. The amendments will be effective for the Company beginning January 1, 2017. Earlier application is permitted for all entities as of the beginning of an interim or annual reporting period.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments — Overall: Recognition and Measurement of Financial Assets and Financial Liabilities, which addresses certain aspects of the recognition, measurement, presentation and disclosure of financial instruments. The amendment will be effective for the Company beginning January 1, 2018 and we are currently evaluating the impact that ASU 2016-01 will have on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases, which requires lessees to recognize on the balance sheet a right-of-use asset, representing their right to use the underlying asset for the lease term, and a lease liability for all leases with terms greater than 12 months. The guidance also requires qualitative and quantitative disclosures designed to assess the amount, timing and uncertainty of cash flows arising from leases. The standard requires the use of a modified retrospective transition approach, which includes a number of optional practical expedients that entities may elect to apply. ASU 2016-02 is effective for the Company beginning January 1, 2019 and we are currently evaluating the impact that ASU 2016-02 will have on our consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, Compensation — Stock Compensation: Improvements to Employee Share-Based Payment Accounting. The standard is intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. ASU 2016-09 is effective for the Company beginning January 1, 2017 and we are currently evaluating the impact that ASU 2016-09 will have on our consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments — Measurement of Credit Losses on Financial Instruments, which requires measurement and recognition of expected credit losses for financial assets held. ASU 2016-13 is effective for the Company beginning January 1, 2020 and we are currently evaluating the impact that ASU 2016-13 will have on our consolidated financial statements.

#### NOTE 2: ACQUISITIONS AND DIVESTITURES

##### Acquisitions

During the six months ended July 1, 2016, our Company's acquisitions of businesses, equity method investments and nonmarketable securities totaled \$723 million, which primarily related to our acquisition of Xiamen Culiangwang Beverage Technology Co., Ltd. ("China Green"), a maker of plant-based protein beverages in China, and a minority investment in CHI Limited ("CHI"), a Nigerian producer of value-added dairy and juice beverages, which is accounted for under the equity method of accounting. Under the terms of the agreement for our investment in CHI, the Company is obligated to acquire the remaining ownership interest from the existing shareowners in 2019 based on an agreed-upon formula.

During the six months ended July 3, 2015, our Company's acquisitions of businesses, equity method investments and nonmarketable securities totaled \$2,284 million, which primarily related to our strategic partnership with Monster Beverage Corporation ("Monster") and an investment in a bottling partner in Indonesia that is accounted for under the equity method of accounting. The bottling partner in Indonesia is a subsidiary of Coca-Cola Amatil Limited, an equity method investee. We also acquired the remaining outstanding shares of a bottling partner in South Africa ("South African bottler"), which was previously accounted for as an equity method investment. We remeasured our previously held equity interest in the South African bottler to fair value upon the close of the transaction and recorded a loss on the remeasurement of \$19 million during the six months ended July 3, 2015. This bottler will be included in the Coca-Cola Beverages Africa Limited transaction discussed further below.

##### Monster Beverage Corporation

On August 14, 2014, the Company and Monster entered into definitive agreements for a long-term strategic relationship in the global energy drink category. The transaction contemplated under these agreements ("Monster Transaction") closed on June 12, 2015. As a result of the Monster Transaction, (1) the Company purchased newly issued shares of Monster common stock representing approximately 17 percent of the outstanding shares of Monster common stock (after giving effect to the new issuance); (2) the Company sold its global energy drink business (including NOS, Full Throttle, Burn, Mother, Play and Power Play, and Relentless) to Monster, and the Company acquired Monster's non-energy drink business (including Hansen's Natural Sodas, Peace Tea, Hubert's Lemonade and Hansen's Juice Products); and (3) the parties amended their distribution coordination agreements to expand distribution of Monster products into additional territories pursuant to long-term agreements with the Company's

existing network of Company-owned or -controlled bottling operations and distribution partners. The Coca-Cola system also became Monster's preferred global distribution partner. The Company made a net cash payment of \$2,150 million to Monster, of which \$125 million was being held in escrow, subject to release upon achievement of milestones relating to the transfer of Monster's distribution rights to our distribution network. The escrow was released in June 2016 upon the expiration of the escrow term as certain milestones relating to the transfer of Monster's domestic distribution rights to our distribution network had not been achieved. However, due to the probability that these milestones will be achieved at a future date, the Company has accrued \$125 million related to these future payments to Monster.

The Monster Transaction consisted of multiple elements including the purchase of common stock, the acquisition and divestiture of businesses and the expansion of distribution territories. When consideration transferred is not solely in the form of cash, measurement is based on either the cost to the acquiring entity (the fair value of the assets given) or the fair value of the assets acquired, whichever is more clearly evident and, thus, more reliably measurable. As the majority of the consideration transferred was cash, we believe the fair value of the consideration transferred is more reliably measurable. The consideration transferred consisted of \$2,150 million of cash (including \$125 million initially held in escrow) and the fair value of our global energy business of \$2,046 million, which we determined using discounted cash flow analyses, resulting in total consideration transferred of \$4,196 million. As such, we have allocated the total consideration transferred to the individual assets and business acquired based on a relative fair value basis, using the closing date fair values of each element, as follows (in millions):

	June 12, 2015
Equity investment in Monster	\$3,066
Expansion of distribution territories	1,035
Monster non-energy drink business	95
Total assets and business acquired	\$4,196

In addition to our ownership interest in Monster's outstanding common stock, the Company is represented by two directors on Monster's 10 member Board of Directors. Based on our equity ownership percentage, the significance that our expanded distribution and coordination agreements have on Monster's operations, and our representation on Monster's Board of Directors, the Company is accounting for its interest in Monster as an equity method investment. As a result of the Monster Transaction, the North America Coca-Cola system obtained the right to distribute Monster products in territories for which it was not previously the authorized distributor ("expanded territories"). These distribution rights are governed by an agreement with an initial term of 20 years, after which it will continue to remain in effect unless otherwise terminated by either party and there are no future costs of renewal. As such, these rights were determined to be indefinite-lived intangible assets and are classified in the line item bottlers' franchise rights with indefinite lives in our condensed consolidated balance sheet. CCR is the distributor in the majority of the expanded territories. The remainder of the territories are serviced by independent bottling partners. Of the \$1,035 million allocated to the expanded distribution rights, the Company derecognized \$341 million related to the expanded territories serviced by the independent bottling partners upon the close of the transaction. As consideration for these rights, the Company received an upfront payment of \$28 million related to these territories, and we will receive a payment per case on all future sales made by these independent bottlers for the duration of the distribution agreements. As these payments are dependent on future sales, they are a form of contingent consideration. We elected to account for this consideration in the same manner as the contingent consideration to be received in the North America refranchising, discussed below. This resulted in a net loss of \$313 million recorded in the line item other income (loss) — net in our condensed consolidated statement of income during the three and six months ended July 3, 2015.

During the three and six months ended July 3, 2015, the Company recognized a gain of \$1,715 million on the sale of our global energy drink business, primarily due to the difference in the recorded carrying value of the assets transferred, including an allocated portion of goodwill, compared to the value of the total assets and business acquired. After considering the loss resulting from the derecognition of the expanded territory rights serviced by the independent bottling partners, the net gain recognized on the Monster Transaction was \$1,402 million, which was recorded in the line item other income (loss) — net in our condensed consolidated statement of income. Additionally, under the terms of the Monster Transaction, we were required to discontinue selling energy products under certain trademarks, including one trademark in the glacéau portfolio. The Company recognized an impairment charge of \$380 million upon closing, primarily related to the discontinuation of the energy products in the glacéau portfolio, which was recorded in the line item other operating charges in our condensed consolidated statement of income.

During the three and six months ended July 3, 2015, based on the relative fair values of the total assets and business acquired, \$1,620 million of the \$2,150 million cash payment made was classified in the line item acquisitions of businesses, equity method investments and nonmarketable securities in our consolidated statement of cash flows. The remaining \$530 million was classified in the line item other investing activities in our consolidated statement of cash flows.

Divestitures

During the six months ended July 1, 2016, proceeds from disposals of businesses, equity method investments and nonmarketable securities totaled \$420 million, primarily related to proceeds from the refranchising of certain of our territories in North America.



During the six months ended July 3, 2015, proceeds from disposals of businesses, equity method investments and nonmarketable securities totaled \$413 million, related to proceeds from the refranchising of certain of our territories in North America and proceeds from the sale of a 10 percent interest in a Brazilian bottling partner as a result of the majority owners exercising their right to acquire additional shares from us.

#### Coca-Cola European Partners

In August 2015, the Company entered into an agreement to merge our German bottling operations with Coca-Cola Enterprises, Inc. ("CCE") and Coca-Cola Iberian Partners, S.A.U., formerly known as Coca-Cola Iberian Partners, S.A. ("CCIP"), to create Coca-Cola European Partners plc ("CCEP"). As of December 31, 2015, our German bottling operations were classified as held for sale. On May 28, 2016, the transaction closed and we exchanged our German bottling operations for an 18 percent interest in CCEP. As a result of recording our interest in CCEP at fair value based on its quoted market price, the deconsolidation of our German bottling operations, and the related reversal of its cumulative translation adjustments, we recognized a gain of \$1,400 million. This gain was partially offset by a \$77 million loss incurred as a result of reclassifying losses related to our net investment hedges of our German bottling operations from AOCI into earnings as well as transaction costs incurred resulting in a net gain of \$1,292 million during the three and six months ended July 1, 2016. Refer to Note 8. With the exception of the transaction costs, the net gain was recorded in the line item other income (loss) — net in our condensed consolidated statement of income. The Company accounts for its 18 percent interest in CCEP as an equity method investment based on our equity ownership percentage, our representation on CCEP's Board of Directors and other governance rights.

#### Keurig Green Mountain, Inc.

In February 2014, the Company purchased newly issued shares in Keurig Green Mountain, Inc. ("Keurig") for \$1,265 million, including transaction costs of \$14 million. In May 2014, the Company purchased additional shares of Keurig in the market for \$302 million, which represented an additional 2 percent equity position in Keurig. Subsequent to these purchases, the Company entered into an agreement with Credit Suisse Capital LLC ("CS") to purchase additional shares of Keurig which would increase the Company's equity position to a 16 percent interest based on the total number of issued and outstanding shares of Keurig as of May 1, 2014. Under the agreement, the Company was to purchase from CS, on a date selected by CS no later than February 2015, the lesser of (1) 6.5 million shares of Keurig or (2) the number of shares that shall cause our ownership to equal 16 percent. The purchase price per share was the average of the daily volume-weighted average price per share from May 15, 2014, to the date selected by CS, as adjusted in certain circumstances specified in the agreement. CS had exclusive ownership and control over any such shares until delivered to the Company. In February 2015, the Company purchased 6.4 million shares from CS under this agreement for a total purchase price of \$830 million. As this agreement qualified as a derivative, we recognized a loss of \$58 million in the line item other income (loss) — net in the condensed consolidated statement of income during the six months ended July 3, 2015. The Company recognized a cumulative loss of \$47 million in the line item other income (loss) — net in the condensed consolidated statements of income over the term of the agreement. The purchases of the shares were included in the line item purchases of investments in our condensed consolidated statement of cash flows, net of any related derivative impact. The Company accounted for the investment in Keurig as an available-for-sale security, which was included in the line item other investments in our condensed consolidated balance sheet.

In March 2016, a JAB Holding Company-led investor group acquired Keurig for \$92 per share. The Company received proceeds of \$2,380 million, which were recorded in the line item proceeds from disposals of investments in our condensed consolidated statement of cash flows, and recorded a gain of \$18 million related to the disposal of our shares of Keurig in the line item other income (loss) — net in our condensed consolidated statement of income during the six months ended July 1, 2016.

#### North America Refranchising

In conjunction with implementing a new beverage partnership model in North America, the Company refranchised territories that were previously managed by CCR to certain of our unconsolidated bottling partners. These territories generally border these bottlers' existing territories, allowing each bottler to better service local customers and provide more efficient execution. By entering into comprehensive beverage agreements ("CBAs") with each of the bottlers, we granted certain exclusive territory rights for the distribution, promotion, marketing and sale of Company-owned and

licensed beverage products as defined by the CBA. In some cases, the Company has entered into, or agreed to enter into, manufacturing agreements that authorize certain bottlers that have executed a CBA to manufacture certain beverage products. If a bottler has not entered into a specific manufacturing agreement, then under the CBA for these territories, CCR retains the rights to produce these beverage products and the bottlers will purchase from CCR (or other Company-authorized manufacturing bottlers) substantially all of the related finished products needed in order to service the customers in these territories.

Each CBA generally has a term of 10 years and is renewable, in most cases by the bottler and in some cases by the Company, indefinitely for successive additional terms of 10 years each. Under the CBA, the bottlers will make ongoing quarterly payments to the Company based on their gross profit in the refranchised territories throughout the term of the CBA, including renewals, in exchange for the grant of the exclusive territory rights.

Contemporaneously with the grant of these rights, the Company sold the distribution assets, certain working capital items, and the exclusive rights to distribute certain beverage brands not owned by the Company, but distributed by CCR, in each of these territories to the respective bottlers in exchange for cash. These rights include, where applicable, the distribution rights acquired from Monster in 2015 for the respective territories. During the six months ended July 1, 2016 and July 3, 2015, cash proceeds from these sales totaled \$404 million and \$216 million, respectively. Included in the cash proceeds for the six months ended July 1, 2016 and July 3, 2015 was \$181 million and \$51 million, respectively, from Coca-Cola Bottling Co. Consolidated ("CCBCC"), an equity method investee. Under the applicable accounting guidance, we were required to derecognize all of the tangible assets sold as well as the intangible assets transferred, including distribution rights, customer relationships and an allocated portion of goodwill related to these territories.

Additionally, in September 2015, the Company announced the formation of a new National Product Supply System ("NPSS") which will facilitate optimal operation of the U.S. product supply system. Under the NPSS, the Company and several of its existing independent producing bottlers will administer key national product supply activities for these bottlers, which currently represent approximately 95 percent of the U.S. produced volume. As part of the NPSS, it is anticipated that each of these bottlers will acquire certain production facilities from CCR in exchange for cash, subject to the parties reaching definitive agreements.

We recognized noncash losses of \$199 million and \$12 million during the three months ended July 1, 2016 and July 3, 2015, respectively. During the six months ended July 1, 2016 and July 3, 2015, we recognized noncash losses of \$568 million and \$33 million, respectively. These losses primarily related to the derecognition of the intangible assets transferred or reclassified as held for sale and were included in the line item other income (loss) — net in our condensed consolidated statements of income. See further discussion of assets and liabilities held for sale below. We expect to recover the value of the intangible assets transferred to the bottlers under the CBAs through the future quarterly payments; however, as the payments for the territory rights are dependent on the bottlers' future gross profit in these territories, they are considered a form of contingent consideration.

There is diversity in practice as it relates to the accounting for contingent consideration by the seller. The seller can account for the future contingent payments received as a gain contingency, recognizing the amounts in the income statement only after the related contingencies are resolved and the gain is realized, which in this arrangement will be quarterly as the bottlers earn gross profit in the transferred territories. Alternatively, the seller can record a receivable for the contingent consideration at fair value on the date of sale and record any future differences between the payments received and this receivable in the income statement as they occur. We elected the gain contingency treatment since the quarterly payments will be received throughout the terms of the CBAs, including all subsequent renewals, regardless of the cumulative amount received as compared to the value of the intangible assets transferred.

#### Assets and Liabilities Held for Sale

##### North America Refranchising

As of July 1, 2016, the Company had entered into agreements, or otherwise approved plans, to refranchise additional territories in North America. For territories that met the criteria to be classified as held for sale, we were required to record their assets and liabilities at the lower of carrying value or fair value less any costs to sell based on the agreed-upon sale price. The Company expects that these territories will be refranchised within the next 12 months.

##### Coca-Cola Beverages Africa Limited

In November 2014, the Company, SABMiller plc and Gutsche Family Investments entered into an agreement to combine the bottling operations of each of the parties' nonalcoholic ready-to-drink beverage businesses in Southern and East Africa. Upon completion of the proposed merger, the Company will have an ownership of 12 percent in the bottler, which will be called Coca-Cola Beverages Africa Limited, and an ownership of 3 percent in the bottler's South African subsidiary. The Company will also acquire or license several brands in exchange for cash as a result of the transaction. As of July 1, 2016, our South African bottling operations and related equity method investment met the

criteria to be classified as held for sale, but we were not required to record these assets and liabilities at fair value less any costs to sell because their estimated fair value exceeded our carrying value. Based on the proposed governance structure, the Company expects to account for its resulting interest in the new entity as an equity method investment. The transaction closed on July 2, 2016. Refer to Note 16.

The following table presents information related to the major classes of assets and liabilities that were classified as held for sale in our condensed consolidated balance sheets (in millions):

	July 1, 2016	December 31, 2015	
Cash, cash equivalents and short-term investments	\$ 14	\$ 143	
Trade accounts receivable, less allowances	51	485	
Inventories	45	276	
Prepaid expenses and other assets	8	83	
Equity method investments	83	92	
Other assets	14	25	
Property, plant and equipment — net	316	2,021	
Bottlers' franchise rights with indefinite lives	302	1,020	
Goodwill	132	333	
Other intangible assets	70	115	
Allowance for reduction of assets held for sale	(342 )	(693 )	
Total assets	\$ 693 <sup>1</sup>	\$ 3,900 <sup>3</sup>	
Accounts payable and accrued expenses	\$ 21	\$ 712	
Current maturities of long-term debt	—	12	
Accrued income taxes	1	4	
Long-term debt	46	74	
Other liabilities	2	79	
Deferred income taxes	68	252	
Total liabilities	\$ 138 <sup>2</sup>	\$ 1,133 <sup>4</sup>	

<sup>1</sup> Consists of total assets relating to North America refranchising of \$317 million, Coca-Cola Beverages Africa Limited of \$338 million and other assets held for sale of \$38 million, which are included in the Bottling Investments, Eurasia and Africa, and Corporate operating segments.

<sup>2</sup> Consists of total liabilities relating to North America refranchising of \$67 million and Coca-Cola Beverages Africa Limited of \$71 million, which are included in the Bottling Investments and Eurasia and Africa operating segments.

<sup>3</sup> Consists of total assets relating to CCEP of \$2,894 million, North America refranchising of \$589 million, Coca-Cola Beverages Africa Limited of \$398 million and other assets held for sale of \$19 million, which are included in the Bottling Investments, Eurasia and Africa, and Corporate operating segments.

Consists of total liabilities relating to CCEP of \$924 million, North America refranchising of \$123 million and

<sup>4</sup> Coca-Cola Beverages Africa Limited of \$86 million, which are included in the Bottling Investments and Eurasia and Africa operating segments.

We determined that the operations included in the table above did not meet the criteria to be classified as discontinued operations under the applicable guidance.

#### NOTE 3: INVESTMENTS

Investments in debt and marketable securities, other than investments accounted for under the equity method, are classified as trading, available-for-sale or held-to-maturity. Our marketable equity investments are classified as either trading or available-for-sale with their cost basis determined by the specific identification method. Our investments in debt securities are carried at either amortized cost or fair value. Investments in debt securities that the Company has the positive intent and ability to hold to maturity are carried at amortized cost and classified as held-to-maturity. Investments in debt securities that are not classified as held-to-maturity are carried at fair value and classified as either trading or available-for-sale. Realized and unrealized gains and losses on trading securities and realized gains and losses on available-for-sale securities are included in net income. Unrealized gains and losses, net of deferred taxes, on available-for-sale securities are included in our consolidated balance sheets as a component of accumulated other comprehensive income (loss) ("AOCI"), except for the change in fair value attributable to the currency risk being hedged. Refer to Note 5 for additional information related to the Company's fair value hedges of available-for-sale

securities.

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## Trading Securities

As of July 1, 2016 and December 31, 2015, our trading securities had a fair value of \$365 million and \$322 million, respectively, and consisted primarily of equity securities. The Company had net unrealized gains on trading securities of \$28 million and \$19 million as of July 1, 2016 and December 31, 2015, respectively.

The Company's trading securities were included in the following line items in our condensed consolidated balance sheets (in millions):

	July 1, December 31,	
	2016	2015
Marketable securities	\$ 265	\$ 229
Other assets	100	93
Total	\$ 365	\$ 322

## Available-for-Sale and Held-to-Maturity Securities

As of July 1, 2016 and December 31, 2015, the Company did not have any held-to-maturity securities. As of July 1, 2016, available-for-sale securities consisted of the following (in millions):

	Gross Unrealized		Estimated Fair Value
	Cost	Gains/Losses	
Available-for-sale securities: <sup>1</sup>			
Equity securities	\$ 1,260	\$ 603 (47 )	\$ 1,816
Debt securities	3,476	109 (5 )	3,580
Total	\$ 4,736	\$ 712 (52 )	\$ 5,396

<sup>1</sup> Refer to Note 14 for additional information related to the estimated fair value.

As of December 31, 2015, available-for-sale securities consisted of the following (in millions):

	Gross Unrealized		Estimated Fair Value
	Cost	Gains/Losses	
Available-for-sale securities: <sup>1</sup>			
Equity securities	\$ 3,573	\$ 485 (84 )	\$ 3,974
Debt securities	4,593	64 (25 )	4,632
Total	\$ 8,166	\$ 549 (109)	\$ 8,606

<sup>1</sup> Refer to Note 14 for additional information related to the estimated fair value.

The sale and/or maturity of available-for-sale securities resulted in the following realized activity (in millions):

	Three Months Ended		Six Months Ended	
	July 1, 2016	July 3, 2015	July 1, 2016	July 3, 2015
Gross gains	\$ 10	\$ 7	\$ 110	\$ 41
Gross losses	(6 )	(5 )	(36 )	(12 )
Proceeds	2,301	1,862	6,817	2,304

As of July 1, 2016 and December 31, 2015, the Company had investments classified as available-for-sale in which our cost basis exceeded the fair value of our investment. Management assessed each of the available-for-sale securities that were in a gross unrealized loss position on an individual basis to determine if the decline in fair value was other than temporary. Management's assessment as to the nature of a decline in fair value is based on, among other things, the length of time and the extent to which the market value has been less than our cost basis; the financial condition and near-term prospects of the issuer; and our intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in market value. As a result of these assessments, management determined that

the decline in fair value of these investments was not other than temporary and did not record any impairment charges.

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The Company uses two of its insurance captives to reinsure group annuity insurance contracts that cover the pension obligations of certain of our European and Canadian pension plans. In accordance with local insurance regulations, our insurance captives are required to meet and maintain minimum solvency capital requirements. The Company elected to invest its solvency capital in a portfolio of available-for-sale securities, which are classified in the line item other assets in our condensed consolidated balance sheets because the assets are not available to satisfy our current obligations. As of July 1, 2016 and December 31, 2015, the Company's available-for-sale securities included solvency capital funds of \$954 million and \$804 million, respectively.

The Company's available-for-sale securities were included in the following line items in our condensed consolidated balance sheets (in millions):

	July 1, December 31,	
	2016	2015
Cash and cash equivalents	\$ 793	\$ 361
Marketable securities	2,408	4,040
Other investments	1,099	3,280
Other assets	1,096	925
Total	\$5,396	\$ 8,606

The contractual maturities of these available-for-sale securities as of July 1, 2016 were as follows (in millions):

	Estimated	
	Cost	Fair Value
Within 1 year	\$1,270	\$ 1,270
After 1 year through 5 years	1,763	1,825
After 5 years through 10 years	129	146
After 10 years	314	339
Equity securities	1,260	1,816
Total	\$4,736	\$ 5,396

The Company expects that actual maturities may differ from the contractual maturities above because borrowers have the right to call or prepay certain obligations.

#### Cost Method Investments

Cost method investments are initially recorded at cost, and we record dividend income when applicable dividends are declared. Cost method investments are reported as other investments in our condensed consolidated balance sheets, and dividend income from cost method investments is reported in other income (loss) — net in our condensed consolidated statements of income. We review all of our cost method investments quarterly to determine if impairment indicators are present; however, we are not required to determine the fair value of these investments unless impairment indicators exist. When impairment indicators exist, we generally use discounted cash flow analyses to determine the fair value. We estimate that the fair values of our cost method investments approximated or exceeded their carrying values as of July 1, 2016 and December 31, 2015. Our cost method investments had a carrying value of \$185 million and \$190 million as of July 1, 2016 and December 31, 2015, respectively.

#### NOTE 4: INVENTORIES

Inventories consist primarily of raw materials and packaging (which include ingredients and supplies) and finished goods (which include concentrates and syrups in our concentrate operations and finished beverages in our finished product operations). Inventories are valued at the lower of cost or market. We determine cost on the basis of the average cost or first-in, first-out methods. Inventories consisted of the following (in millions):

	July 1, December 31,	
	2016	2015
Raw materials and packaging	\$1,655	\$ 1,564
Finished goods	1,034	1,032
Other	316	306
Total inventories	\$3,005	\$ 2,902



**NOTE 5: HEDGING TRANSACTIONS AND DERIVATIVE FINANCIAL INSTRUMENTS**

The Company is directly and indirectly affected by changes in certain market conditions. These changes in market conditions may adversely impact the Company's financial performance and are referred to as "market risks." When deemed appropriate, our Company uses derivatives as a risk management tool to mitigate the potential impact of certain market risks. The primary market risks managed by the Company through the use of derivative and non-derivative financial instruments are foreign currency exchange rate risk, commodity price risk and interest rate risk.

The Company uses various types of derivative instruments including, but not limited to, forward contracts, commodity futures contracts, option contracts, collars and swaps. Forward contracts and commodity futures contracts are agreements to buy or sell a quantity of a currency or commodity at a predetermined future date, and at a predetermined rate or price. An option contract is an agreement that conveys the purchaser the right, but not the obligation, to buy or sell a quantity of a currency or commodity at a predetermined rate or price during a period or at a time in the future. A collar is a strategy that uses a combination of options to limit the range of possible positive or negative returns on an underlying asset or liability to a specific range, or to protect expected future cash flows. To do this, an investor simultaneously buys a put option and sells (writes) a call option, or alternatively buys a call option and sells (writes) a put option. A swap agreement is a contract between two parties to exchange cash flows based on specified underlying notional amounts, assets and/or indices. We do not enter into derivative financial instruments for trading purposes. The Company may also designate certain non-derivative instruments, such as our foreign-denominated debt, in hedging relationships.

All derivative instruments are carried at fair value in our condensed consolidated balance sheets in the following line items, as applicable: prepaid expenses and other assets; other assets; accounts payable and accrued expenses; and other liabilities. The carrying values of the derivatives reflect the impact of legally enforceable master netting agreements and cash collateral held or placed with the same counterparties, as applicable. These master netting agreements allow the Company to net settle positive and negative positions (assets and liabilities) arising from different transactions with the same counterparty.

The accounting for gains and losses that result from changes in the fair values of derivative instruments depends on whether the derivatives have been designated and qualify as hedging instruments and the type of hedging relationships. Derivatives can be designated as fair value hedges, cash flow hedges or hedges of net investments in foreign operations. The changes in the fair values of derivatives that have been designated and qualify for fair value hedge accounting are recorded in the same line item in our condensed consolidated statement of income as the changes in the fair values of the hedged items attributable to the risk being hedged. The changes in the fair values of derivatives that have been designated and qualify as cash flow hedges or hedges of net investments in foreign operations are recorded in AOCI and are reclassified into the line item in our condensed consolidated statement of income in which the hedged items are recorded in the same period the hedged items affect earnings. Due to the high degree of effectiveness between the hedging instruments and the underlying exposures being hedged, fluctuations in the values of the derivative instruments are generally offset by changes in the fair values or cash flows of the underlying exposures being hedged. The changes in fair values of derivatives that were not designated and/or did not qualify as hedging instruments are immediately recognized into earnings.

For derivatives that will be accounted for as hedging instruments, the Company formally designates and documents, at inception, the financial instrument as a hedge of a specific underlying exposure, the risk management objective and the strategy for undertaking the hedge transaction. In addition, the Company formally assesses, both at inception and at least quarterly thereafter, whether the financial instruments used in hedging transactions are effective at offsetting changes in either the fair values or cash flows of the related underlying exposures. Any ineffective portion of a financial instrument's change in fair value is immediately recognized into earnings.

The Company determines the fair values of its derivatives based on quoted market prices or pricing models using current market rates. Refer to Note 14. The notional amounts of the derivative financial instruments do not necessarily represent amounts exchanged by the parties and, therefore, are not a direct measure of our exposure to the financial risks described above. The amounts exchanged are calculated by reference to the notional amounts and by other terms of the derivatives, such as interest rates, foreign currency exchange rates or other financial indices. The Company does

not view the fair values of its derivatives in isolation but rather in relation to the fair values or cash flows of the underlying hedged transactions or other exposures. Virtually all of our derivatives are straightforward over-the-counter instruments with liquid markets.

The following table presents the fair values of the Company's derivative instruments that were designated and qualified as part of a hedging relationship (in millions):

Derivatives Designated as Hedging Instruments	Balance Sheet Location <sup>1</sup>	Fair Value <sup>1,2</sup>	
		July 2016	December 31, 2015
<b>Assets:</b>			
Foreign currency contracts	Prepaid expenses and other assets	\$452	\$ 572
Foreign currency contracts	Other assets	146	246
Commodity contracts	Prepaid expenses and other assets	1	1
Interest rate contracts	Prepaid expenses and other assets	3	20
Interest rate contracts	Other assets	307	62
<b>Total assets</b>		<b>\$909</b>	<b>\$ 901</b>
<b>Liabilities:</b>			
Foreign currency contracts	Accounts payable and accrued expenses	\$242	\$ 51
Foreign currency contracts	Other liabilities	77	75
Interest rate contracts	Accounts payable and accrued expenses	297	53
Interest rate contracts	Other liabilities	71	231
<b>Total liabilities</b>		<b>\$687</b>	<b>\$ 410</b>

<sup>1</sup> All of the Company's derivative instruments are carried at fair value in our condensed consolidated balance sheets after considering the impact of legally enforceable master netting agreements and cash collateral held or placed with the same counterparties, as applicable. Current disclosure requirements mandate that derivatives must also be disclosed without reflecting the impact of master netting agreements and cash collateral. Refer to Note 14 for the net presentation of the Company's derivative instruments.

<sup>2</sup> Refer to Note 14 for additional information related to the estimated fair value.

The following table presents the fair values of the Company's derivative instruments that were not designated as hedging instruments (in millions):

Derivatives Not Designated as Hedging Instruments	Balance Sheet Location <sup>1</sup>	Fair Value <sup>1,2</sup>	
		July 2016	December 31, 2015
<b>Assets:</b>			
Foreign currency contracts	Prepaid expenses and other assets	\$236	\$ 105
Foreign currency contracts	Other assets	1	241
Commodity contracts	Prepaid expenses and other assets	19	2
Commodity contracts	Other assets	5	1
Other derivative instruments	Prepaid expenses and other assets	7	17
Other derivative instruments	Other assets	—	3
<b>Total assets</b>		<b>\$268</b>	<b>\$ 369</b>
<b>Liabilities:</b>			
Foreign currency contracts	Accounts payable and accrued expenses	\$105	\$ 59
Foreign currency contracts	Other liabilities	6	9
Commodity contracts	Accounts payable and accrued expenses	75	154
Commodity contracts	Other liabilities	1	19
Interest rate contracts	Other liabilities	1	1
Other derivative instruments	Accounts payable and accrued expenses	2	5
Other derivative instruments	Other liabilities	3	2
<b>Total liabilities</b>		<b>\$193</b>	<b>\$ 249</b>

<sup>1</sup> All of the Company's derivative instruments are carried at fair value in our condensed consolidated balance sheets after considering the impact of legally enforceable master netting agreements and cash collateral held or placed with the same counterparties, as applicable. Current disclosure requirements mandate that derivatives must also be

disclosed without reflecting the impact of master netting agreements and cash collateral. Refer to Note 14 for the net presentation of the Company's derivative instruments.

<sup>2</sup> Refer to Note 14 for additional information related to the estimated fair value.

### Credit Risk Associated with Derivatives

We have established strict counterparty credit guidelines and enter into transactions only with financial institutions of investment grade or better. We monitor counterparty exposures regularly and review any downgrade in credit rating immediately. If a downgrade in the credit rating of a counterparty were to occur, we have provisions requiring cash collateral for substantially all of our transactions. To mitigate presettlement risk, minimum credit standards become more stringent as the duration of the derivative financial instrument increases. In addition, the Company's master netting agreements reduce credit risk by permitting the Company to net settle for transactions with the same counterparty. To minimize the concentration of credit risk, we enter into derivative transactions with a portfolio of financial institutions. Based on these factors, we consider the risk of counterparty default to be minimal.

### Cash Flow Hedging Strategy

The Company uses cash flow hedges to minimize the variability in cash flows of assets or liabilities or forecasted transactions caused by fluctuations in foreign currency exchange rates, commodity prices or interest rates. The changes in the fair values of derivatives designated as cash flow hedges are recorded in AOCI and are reclassified into the line item in our condensed consolidated statement of income in which the hedged items are recorded in the same period the hedged items affect earnings. The changes in fair values of hedges that are determined to be ineffective are immediately reclassified from AOCI into earnings. The maximum length of time for which the Company hedges its exposure to future cash flows is typically three years.

The Company maintains a foreign currency cash flow hedging program to reduce the risk that our eventual U.S. dollar net cash inflows from sales outside the United States and U.S. dollar net cash outflows from procurement activities will be adversely affected by fluctuations in foreign currency exchange rates. We enter into forward contracts and purchase foreign currency options (principally euros and Japanese yen) and collars to hedge certain portions of forecasted cash flows denominated in foreign currencies. When the U.S. dollar strengthens against the foreign currencies, the decline in the present value of future foreign currency cash flows is partially offset by gains in the fair value of the derivative instruments. Conversely, when the U.S. dollar weakens, the increase in the present value of future foreign currency cash flows is partially offset by losses in the fair value of the derivative instruments. The total notional values of derivatives that were designated and qualified for the Company's foreign currency cash flow hedging program were \$8,291 million and \$10,383 million as of July 1, 2016 and December 31, 2015, respectively. The Company uses cross-currency swaps to hedge the changes in cash flows of certain of its foreign currency denominated debt due to changes in foreign currency exchange rates. For this hedging program, the Company records the change in carrying value of the foreign currency denominated debt due to changes in exchange rates into earnings each period. The changes in fair value of the cross-currency swap derivatives are recorded in AOCI with an immediate reclassification into earnings for the change in fair value attributable to fluctuations in foreign currency exchange rates. During the six months ended July 3, 2015, the Company discontinued the cash flow hedge relationships related to swaps that had a notional amount of \$2,590 million. Upon discontinuance, the Company recognized a loss of \$92 million in other comprehensive income ("OCI"), which will be reclassified from AOCI into interest expense over the remaining life of the debt, a weighted-average period of approximately 10 years. The Company did not discontinue any cash flow hedging relationships during the three and six months ended July 1, 2016. The total notional values for the Company's cross-currency swaps were \$1,294 million and \$566 million as of July 1, 2016 and December 31, 2015, respectively.

The Company has entered into commodity futures contracts and other derivative instruments on various commodities to mitigate the price risk associated with forecasted purchases of materials used in our manufacturing process. These derivative instruments have been designated and qualify as part of the Company's commodity cash flow hedging program. The objective of this hedging program is to reduce the variability of cash flows associated with future purchases of certain commodities. The total notional values of derivatives that were designated and qualified for the Company's commodity cash flow hedging program were \$5 million and \$8 million as of July 1, 2016 and December 31, 2015, respectively.

Our Company monitors our mix of short-term debt and long-term debt regularly. From time to time, we manage our risk to interest rate fluctuations through the use of derivative financial instruments. The Company has entered into interest rate swap agreements and has designated these instruments as part of the Company's interest rate cash flow

hedging program. The objective of this hedging program is to mitigate the risk of adverse changes in benchmark interest rates on the Company's future interest payments. The total notional value of the interest rate swap agreements that were designated and qualified for the Company's interest rate cash flow hedging program was \$3,328 million as of July 1, 2016 and December 31, 2015.



The following table presents the pretax impact that changes in the fair values of derivatives designated as cash flow hedges had on AOCI and earnings during the three months ended July 1, 2016 (in millions):

Gain (Loss) Recognized in OCI	Location of Gain (Loss) Recognized in Income <sup>1</sup>	Gain (Loss) Reclassified from AOCI into Income (Effective Portion)	Gain (Loss) Recognized in Income (Ineffective Portion and Amount Excluded from Effectiveness Testing)
Foreign currency contracts \$ 46	Net operating revenues	\$ 138	\$ (1 )
Foreign currency contracts (19)	)Cost of goods sold	13	(1 )
Foreign currency contracts —	Interest expense	(2)	)—
Foreign currency contracts (53)	)Other income (loss) — net	45	)—
Interest rate contracts (95)	)Interest expense	(2)	)—
Commodity contracts 1	Cost of goods sold	—	—
Total		\$ 102	\$ (2 )

<sup>1</sup> The Company records gains and losses reclassified from AOCI into income for the effective portion and the ineffective portion, if any, to the same line items in our condensed consolidated statements of income.

The following table presents the pretax impact that changes in the fair values of derivatives designated as cash flow hedges had on AOCI and earnings during the six months ended July 1, 2016 (in millions):

Gain (Loss) Recognized in OCI	Location of Gain (Loss) Recognized in Income <sup>1</sup>	Gain (Loss) Reclassified from AOCI into Income (Effective Portion)	Gain (Loss) Recognized in Income (Ineffective Portion and Amount Excluded from Effectiveness Testing)
Foreign currency contracts \$ (300)	)Net operating revenues	\$ 278	\$ (1 )
Foreign currency contracts (43)	)Cost of goods sold	33	(1 )
Foreign currency contracts —	Interest expense	(4)	)—
Foreign currency contracts (11)	)Other income (loss) — net	2	)—