

# PHILIP MORRIS ASIA LIMITED (HONG KONG) V. THE COMMONWEALTH OF AUSTRALIA: PERMANENT COURT OF ARBITRATION TRIBUNAL PUBLISHES REDACTED VERSION OF AWARD ON JURISDICTION AND ADMISSIBILITY

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The Permanent Court of Arbitration (“PCA”) has just released the full award of the Tribunal in *Philip Morris Asia Limited (Hong Kong) v. The Commonwealth of Australia*, which was rendered in late 2015. We previously published here an eUpdate on the dispute and the outcome of the proceedings, in which Philip Morris had challenged Australian legislation that required tobacco companies marketing cigarettes in Australia to sell them only in logo-free, drab dark brown packaging (the “Plain Packaging Measures”). The full award now makes available to us the grounds on which the Tribunal declined to exercise jurisdiction in the matter.

The claim was brought by Philip Morris Asia Limited (Hong Kong) (“Philip Morris HK”) under the provisions of Australia’s 1993 Investment Promotion and Protection Agreement with Hong Kong (the “Treaty”), which is a bilateral investment treaty or “BIT”. Philip Morris HK asserted that the Plain Packaging Measures “bar the use of intellectual property on tobacco products and packaging, transforming [the Claimant’s subsidiary in Australia] from a manufacturer of branded products to a manufacturer of commoditized products with the consequential effect of substantially diminishing the value of [the Claimant’s] investments in Australia”, for which it sought

declaratory relief and compensation. Its commencement of arbitration under the Treaty followed on the heels of the 2012 dismissal by the Australian High Court of a challenge to the law by Philip Morris and other major tobacco companies, including British American Tobacco, Imperial Tobacco and Japan Tobacco.

In its award, the Tribunal held that Philip Morris’s attempt to challenge Australia’s plain packaging laws was an abuse of rights. It determined that Philip Morris’s claims were inadmissible and that it was thus precluded from exercising jurisdiction over the dispute.

## Background to the Dispute

On 29 April 2010, Australia’s Prime Minister Kevin Rudd and Health Minister Roxon unequivocally announced the Government’s intention to introduce the Plain Packaging Measures.

On 23 February 2011, Philip Morris HK formally acquired shares in Philip Morris (Australia) Limited (“PM Australia”) in an internal corporate reorganization. This restructuring gave Philip Morris HK prima facie standing to bring its claim under the investor-state dispute settlement provisions of the 1993 BIT between Hong Kong and Australia (the “Treaty”).

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On 21 November 2011, some nine months after Philip Morris HK had acquired the shares in PM Australia, the Plain Packaging Measures that had been announced the previous year were actually enacted. On the same day, Philip Morris HK served The Commonwealth of Australia with a Notice of Arbitration under the Treaty.

Australia objected to the Tribunal’s jurisdiction on the basis that it was barred from considering Philip Morris HK’s claim because the dispute was foreseeable when Philip Morris HK obtained the nominal protection of the Treaty through the restructuring in which it had acquired PM Australia and, therefore, that the resort to arbitration under the Treaty constituted an abuse of right. Under the extensive body of jurisprudence resulting from the lengthy history of arbitrations under BITs and similar intergovernmental agreements, the invocation of the protections under such agreements may be abusive if standing to do so is acquired through measures taken when a dispute has already arisen or is clearly foreseeable. That line of authority is grounded on the principle of good faith, and its application depends upon the subjective motivation for the measures in question, particularly whether the purpose was simply to obtain the benefits of the relevant treaty.

According to Philip Morris HK, the “*overall objectives of the restructuring were to minimise tax liability, align ownership with control, and optimize cash flows*”. There were also “*additional benefits*”, such as alignment of the ownership of the Australian subsidiaries with Philip Morris HK’s pre-existing management control of the subsidiaries, optimization of the Philip Morris HK’s cash flow, as well as “*additional BIT protection[s]*”. A further key motivation behind the restructuring was, according to Philip Morris HK, that restructuring aligned the ownership and management control of many Philip Morris affiliates. In the submission of Philip Morris

HK, the restructuring had entirely legitimate objectives independent of its desire to obtain the protections of the Treaty.

## Reasoning

In the view of the Tribunal, it would not normally be an abuse of right to bring a BIT claim in the wake of a corporate restructuring, if the restructuring was justified independently of the possibility of bringing such a claim. However, the Tribunal found that Philip Morris HK had not proved that tax or other business reasons were determinative of the restructuring. From all the evidence, the Tribunal was only able to conclude that “*the main and determinative, if not sole, reason for the restructuring was the intention to bring a claim under the Treaty, using an entity from Hong Kong*” after it received ample warnings that the Australian government was considering introducing the Plain Packaging Measures.

In the Tribunal’s view, there was no uncertainty about the Australian Government’s intention to introduce the Plain Packaging Measures after its announcement on 29 April 2010. The Tribunal held that, from that date, there was at least a reasonable prospect that legislation equivalent to the Plain Packaging Measures would eventually be enacted and that a dispute would arise. The Tribunal further held that the Australian Government’s adoption of the Plain Packaging Measures was not only foreseeable but actually foreseen by Philip Morris when it chose to change its corporate structure.

The Tribunal concluded, accordingly, that the initiation of the arbitration constituted an abuse of rights, as the corporate restructuring by which Philip Morris HK acquired the Australian subsidiaries occurred at a time when there was a reasonable prospect that the dispute would materialise and was carried out for the principal, if not sole, purpose of gaining Treaty protection. Accordingly, the Tribunal held that the claim was inadmissible and that it was precluded from exercising jurisdiction.

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## Significance of the Case

The case is less important for what it decided than for what it did not. It has in fact become a “poster child” for political objections to investment treaties and trade agreements that allow investors, in practice usually foreign corporations, to bring legal challenges against governments, which would otherwise enjoy sovereign immunity. It has become a cause célèbre for those who see it as an intolerable subjection of the right of sovereign, democratic governments to regulate business conduct in their territories to abusive claims of large, well-financed multinational corporations, forcing states to defend their laws before tribunals composed of private individuals. This has, in fact, become a major issue in the negotiation of the Transatlantic Trade and Investment Partnership (“TTIP”) Agreement currently under negotiation between the United States and the European Union, and it significantly influenced the disputes provisions of the recently-concluded

but as-yet-unratified Transpacific Partnership (“TPP”) Agreement.

This political backlash has obscured the fact that governments do occasionally take actions affecting foreign investors in violation of established principles of international law. The possibility of such actions reduces the security of investment, thus potentially depriving countries, particularly in the developing world, of much-needed capital investment, which is the purpose of BITs to encourage. The inability of the Tribunal to exercise jurisdiction in the Philip Morris case has deprived us of a possible opportunity for clarification of the line between legitimate regulation, which is recognized in nearly all BITs and in customary international law, and interference with rights protected by treaty and law. This is not a new conundrum in public international law, but it is one the balance of which is constantly shifting as economic and social conditions change. It is unfortunate that this case, having provoked so much angst and political hyperbole, could not have resulted in some much-needed clarification on the merits of that significant issue.

## Author Profile



Steven Nelson is a Partner with Dorsey & Whitney LLP. Beginning with his service in the Office of the Legal Adviser of the US State Department, Steve has focused throughout his career on the complex legal issues involved in international trade and investment.

Although concentrated primarily in cross-border, multi-country M&A transactions, his practice has included extensive work on joint ventures, notably in emerging countries, as well as both litigation and arbitration of disputes involving multiple jurisdictions.



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