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Recent Investment Arbitration Developments in Australia

Recent investment arbitration developments in Australia and the practical implications of the protections commonly afforded by investment treaties

What you need to know

Recent changes to Australian gas export and taxation policy serve as reminders that the protections afforded to investors under investment treaties are not only relevant to investors in emerging markets. Investment treaties are also relevant to investors in modern and developed jurisdictions with widely recognised adherence to the rule of law. Three developing investor-state arbitrations in Australia, each also concerning alleged expropriation and breaches of other common investment treaty protections, demonstrate the relevance of investment treaty protections in jurisdictions of that kind.

This article discusses recent investment treaty developments in Australia and considers the practical implications of protections commonly afforded by investment treaties.

Australia's investment treaties generally

To encourage investment between the contracting states, an investment treaty will commonly confer certain minimum levels of protection on investors from one state with respect to their investments in the other. The nationality of the investor is therefore important.

These protections are typically enforceable by the investor directly against the state party. This is called investor state dispute settlement, or ISDS. For the most part, investment treaties grant to an investor of one state the right to bring claims directly against the other before an independent tribunal. The resulting award can then be enforced globally, and so it is unusual for an award to go unpaid.

Australia has taken a cautious approach to its treaty arrangements (of which it has only 31 – including 21 bilateral investment treaties and 10 free trade agreements – a far smaller number than, for example, the UK with 106) and, in some of its treaties, confers no or only limited ISDS rights. For example, under the Australia-China bilateral investment treaty, disputes regarding compensation payable as a result of expropriation are referred to arbitration. Under the Japan-Australia Economic Partnership, and in Australia's free trade agreements with China, Malaysia, and New Zealand, the state parties are exempt from liability with respect to measures necessary for public order and the protection of life, the environment, and national treasures.

However, Australia has not taken such a limited approach to the availability of ISDS in its investment treaties with South Korea, Singapore, Thailand, and the United States.

It is also relevant that Australia has neither ratified, nor allowed provisional effect, in relation to the Energy Charter Treaty, which it signed on 17 December 1994. The Energy Charter Treaty is a multilateral treaty that grants investment protection rights in the energy sector akin to those found in bilateral investment protection treaties.

Despite Australia being a party to a relatively small number of investment treaties, it should be noted that the low thresholds that apply to the establishment of corporate "nationality" can result in significant exposure to investment treaty claims. This is because "brass plate" corporate subsidiaries established in a treaty country can be enough for a party to secure the protection of an investment treaty with that country.

A recent, high-profile example of an investor-state arbitration involving Australia is the arbitration commenced by Philip Morris arising from the enactment of what was commonly known as the "Tobacco Plain Packaging Legislation" (*Phillip Morris Asia Limited v Commonwealth of Australia*, UNCITRAL, PCA Case No 2012-12). Philip Morris Asia (a Hong Kong company) alleged, amongst other things, that its investments in Australia – being its shareholding in its Australian subsidiary Philip Morris (Australia) Limited and that company's intellectual property – were expropriated without compensation by the enactment of the Tobacco Plain Packaging Legislation. Philip Morris Asia commenced an arbitration against Australia for breach of Australia's bilateral investment treaty with Hong Kong (the 1993 Agreement between the Government of Australia and the Government of Hong Kong for the Promotion and Protection of Investments.)

Unique advantages of investment treaty protection

ISDS provisions enable an investor to claim directly against the respondent sovereign state. Without it, an investor is either left with domestic law remedies, or its own government which may or may not intervene on its behalf. The first alternative is vulnerable to unsympathetic, and sometimes biased, local courts (even contract-based commercial arbitration can, in some jurisdictions, be vulnerable to interference by domestic courts). The second alternative is usually only available to those investors that are big enough to warrant the assistance of their own government and defending commercial investors may not always be the priority of diplomats.

Another advantage is that a sovereign nation cannot disappear, and in most circumstances

it is unlikely to become insolvent. Without ISDS provisions, an investor may be left to claim against the government owned corporation or private entity it contracted with (the assets of which can be withdrawn) leaving the investor with no assets to claim against. In addition, because of the operation of customary public international law principles known as 'articles of state responsibility' the host respondent state takes responsibility for the actions of 'subsidiary' elements extending to state entities in a federal structure, courts, regulators, etc.

Awards made by investor state tribunals are widely enforceable: awards arising from International Centre for Settlement of Investment Disputes (ICSID) proceedings are enforceable pursuant to the Washington Convention in the 153 nations that have signed and ratified the convention; and non-ICSID awards are enforceable pursuant to the New York Convention in the 157 nations that have signed and ratified the convention. Outside of the European Union, international arrangements for the enforcement of foreign judgments are less common. For example, the Hague Convention on the Recognition and Enforcement of Foreign Judgments has only three state signatories. This creates practical difficulties for an investor seeking to enforce a foreign judgment.

As a dispute resolution mechanism that is independent of any domestic legal system, ISDS is not vulnerable to local court interference or to local court bias. This is less important in economies like Australia and the United Kingdom which embrace a strong separation of powers and an independent judiciary; it is more important in economies whose judiciaries do not inspire such confidence.

ISDS proceedings typically are not confidential to the same degree as is commonly the case with commercial arbitrations, and so may be publicised. For example, the World Bank maintains a database of all ICSID cases. The potential damage to a State's reputation as a secure environment for foreign investment makes even the threat of ISDS proceedings a powerful tool that an investor can use to encourage change in the State's behaviour.

What protections are commonly available

Investment treaties will, unsurprisingly, protect 'investments'. That term is broadly defined, by reference not to local law, but by reference to public international law principles developed in a myriad of awards from investment protection arbitration tribunals, and will include, amongst other things, a contractual right to arbitration; cash in the bank; licences to mine or extract; and pre-contractual investment expenditure (provided it is not merely preparatory).

Investors should be mindful of these protections when making foreign investment decisions because, if properly advised, investors may be able to structure their investments in a way that takes advantage of the protections. The need for investment treaty protection is commonly associated with activities in developing economies, however, as will be discussed below it is also appropriate to consider these protections when investing in stable and affluent democracies such as Australia. That point is applicable also to a number of other economies that investors would typically regard as stable and secure, for example: in Canada, changes in the government's attitude to nuclear energy led to claims by United States investors; in the United Kingdom, there has been some discussion about investment

treaty claims arising as a result of Brexit; and Canada has lost or settled six claims under the North America Free Trade Agreement. Likewise, Governments should be mindful of the nature of their obligations under investment treaties, and consider whether their domestic policies risk triggering claims under those agreements.

The precise nature of these protections will differ from treaty to treaty, based on the particular wording. Set out below is a summary of the common treaty protections.

PROTECTION	DESCRIPTION
National treatment	A requirement that the host State treat foreign investment no less favourably than domestic investment. This is a contingent protection, in the sense that the standard of protection afforded depends on the standard of treatment the State affords to its domestic investors engaged in the same industry.
Most favoured nation treatment	A requirement that the host State treat an investor and its investment as favourably as the investors and investments from other States. This is the second contingent protection, in the sense that the standard of protection afforded depends on the standard of treatment the State affords to other foreign investors engaged in the same industry. Because the protection is contingent, claimants have used it to 'import' protections from other treaties, even where the State parties did not initially envisage that such protection would be afforded.
Fair and equitable treatment	Tribunals have interpreted this protection to require that States act consistently, transparently, reasonably, without ambiguity, arbitrariness or discrimination, in an even-handed manner, to ensure due process in decision-making and respect investors' legitimate expectations. Of particular concern for States is how this protection can be balanced against competing policy objectives. As noted above, for a number of its free trade agreements, Australia has included carve-outs with respect to certain public policy measures that it and other State parties might take.
Minimum standards	A requirement that the host state afford a foreign investor minimum standards of treatment for investments in accordance with customary international law principles. There is a degree of tension as to how this protection interacts with that of fair and equitable treatment, and whether fair and equitable treatment requires something beyond the customary international law minimum standard.
Free transfer of funds	A requirement that the host State permit the repatriation of earnings from foreign investments.

PROTECTION	DESCRIPTION
Prohibited expropriation	Investment treaties enshrine the Hull rule, a rule of customary international law which prohibits expropriation unless it occurs for a public purpose, in accordance with law, in a non-discriminatory way and in exchange for fair compensation. With the advent of investor state dispute settlement provisions in these treaties, investors now have a mechanism to directly enforce the Hull rule against States. Importantly, expropriation can be other than direct, and can occur even where the State does not take the benefit of the investment, and where the title is unaffected. Expropriation can also occur in a creeping way, where individual steps are not expropriatory, but the cumulative effect is the substantial deprivation of the asset. In considering whether it has occurred, it is useful to consider: whether the investor has been substantially deprived of the economic use and enjoyment of the rights to the investment; whether the alleged expropriatory act is irreversible or permanent; and the extent of the loss of economic value experienced by the investor.

Recent Australian policy changes

Australia's domestic gas security mechanism

On 27 April 2017, the Australian Federal Government announced its proposal to introduce export restrictions on liquefied natural gas, in the form of an 'Australian Domestic Gas Security Mechanism'. The Mechanism entered into force on 1 July this year, and empowers the Minister for Resources to impose export controls.

The move is said to address a domestic gas shortage, which has allegedly led to higher prices in the domestic market than those paid in the export markets – for the benefit of both consumers and industries reliant on gas, like manufacturing.

Many organisations invested heavily in LNG plants and liquefaction facilities with government on an assumption that the regulatory environment would be stable, predictable, and supportive of the LNG sector. There is also concern in the industry that east coast exporters are being unfairly targeted, and so the possibility of investment treaty claims on the basis of this mechanism might properly be front of mind for both government and industry.

Reformulation of Australia's Petroleum Resource Rent Tax

Following an independent review into the Petroleum Resource Rent Tax, there is continuing speculation as to how the Australian government may seek to bolster weakening receipts from oil and gas production. Whilst the imposition of non-discriminatory taxation measures are not ordinarily considered to be expropriatory, governments and investors

should be aware that indirect expropriation can occur where an investor is substantially deprived of the benefit of their investment.

The industry has previously expressed its steadfast opposition to a Mining Resources Rent Tax, arguing at the time that it could amount to expropriation. The associated legislation was ultimately repealed.

Potential disputes against Australia, and by Australian investors

NuCoal v Australia

In November 2016, NuCoal Resources, an Australian mining company, announced that it was considering bringing an investment arbitration against Australia on behalf of its United States shareholders under the Australia-US Free Trade Agreement. NuCoal purchased Doyles Creek Mining which was the holder of a coal mining license in New South Wales. The mining license was cancelled by the New South Wales Government when it was sensationally revealed that the State's Minister for Mineral and Forest Resources had engaged in corrupt conduct by granting the license. Although there was no allegation of wrongdoing on the part of NuCoal, it was not paid any compensation when the license was cancelled.

APR Energy v Australia

In November 2016, it was reported that APR Energy, an American company, had demanded US$260m compensation from Australia and threatened it with an investment arbitration under the Australia-US Free Trade Agreement. APR alleges that its investments in Australia were treated unfairly and inequitably and that its investments were expropriated and nationalised. APR had leased two gas turbines to Forge Group, an Australian construction company, which then used them as security for a loan with ANZ. When ANZ appointed receivers to Forge, APR lost ownership over the turbines because it had failed to register its ownership of the turbines on the Personal Property Securities Register. The turbines are still being used to generate electricity for a State-owned utility. On 14 April 2017, APR filed a Notice of Arbitration to formally commence the UNCITRAL Arbitration.

Kingsgate v Thailand

On 3 April 2017, Kingsgate Consolidated Minerals, an Australian goldmining company, announced that it had initiated the dispute resolution procedure under ISDS provisions of the Thailand-Australia Free Trade Agreement (**TAFTA**). In May last year, the Thai Government announced the closure of all gold mines in Thailand due to environmental concerns. TAFTA includes the usual investment treaty protections, including the prohibition on expropriation without compensation. Kingsgate is currently in consultations with the Thai Government in respect of the forced closure of its mine north of Bangkok. The TAFTA ISDS provisions provide for a three month consultation period that would have expired on 2 July 2017. On July 3 July 2017, Kingsgate announced that it had agreed to extension of the consultation period until 27 July 2017 at the request of the Thai Government. Consultations between the parties are continuing.

Comment

The recent policy developments in Australia's energy and resources sectors demonstrate,

on the one hand, that investors are increasingly aware, and increasingly willing to take advantage, of investment treaty protections; and on the other it shows that such awareness, by investors and governments alike, is appropriate. The relevance of investment treaty protection is not restricted to investments in developing nations and should properly be front of mind when investors are contemplating how to structure their arrangements, and for governments, when contemplating how to implement their domestic policies.

Very real protection has been afforded to Australian investors who have successfully protected investments through international arbitration. Indeed, the dominance of Australian players in the global resource and energy sectors (where investment protection claims have been especially commonplace) means appreciation of investment protection opportunities may be of particular relevance to Australian investors. Ultimately, investment treaties are modern and complex instruments, and their protections should be considered at the time when an investment is made, and their ramifications for governments should be kept in mind when policy is drafted.

The Philip Morris proceedings (though unsuccessful), and the other disputes that have been foreshadowed, demonstrate the potential breadth of the expropriation protection, and the complications associated with applying its broad elements. The practical consideration for investors is that investment treaties can operate to protect against more than just the open, deliberate and acknowledged taking of something by the host State (see *Metalclad v United Mexican States* ICSID Case No ARB (AF)/97/1 (Award) (30 August 2000) at [103]). Expropriation can occur in a variety of ways.

Like expropriation, the application of other investment treaty protections can be complex, particularly their interaction with State policy, and their precise scope will vary between treaties. If in doubt, investors should seek advice before investing in a host State and they should also consider taking other steps (such as political risk insurance) to protect their investments.

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