Australian High Court gives guidance on sovereign immunity for foreign State owned entities

Foreign States enjoy immunity in Australia from the civil jurisdiction of the Australian courts and from enforcement over their assets based in Australia. This immunity is also extended to "separate entities" of foreign States. [1]

However, the immunity from jurisdiction is subject to certain exceptions. In particular, foreign States and separate entities will not have immunity from jurisdiction if the proceeding "concerns a commercial transaction".

Key issues

- Foreign Governments and State owned enterprises have certain immunity
- Australian companies need to be aware of the scope of their rights when dealing with Foreign Governments and SOEs
- Similarly companies or entities which have full or partial Foreign Government ownership need to be aware of the scope of their immunity

Recent decisions of the Full Federal Court and Australian High Court provide welcome clarity to the question of when an entity of a foreign State will be protected by immunity from civil proceedings in Australian courts, and the scope of the "commercial transaction" exception to foreign State immunity.

Australia's legislative framework

The *Foreign States Immunities Act* 1985 (Cth) (the FSI Act) grants immunity to foreign States[2] from the civil jurisdiction of Australian courts in proceedings (which do not include prosecutions for offences or appeals from such prosecutions), subject to a number of exceptions.[3]

This immunity extends to a "separate entity" of a foreign State, which is defined to mean, relevantly, an individual (other than an Australian citizen) or a corporation (other than one established by or under Australian laws) that is an agency or instrumentality of a foreign State, and is not a department or organ of the executive government of the foreign State. [4]

The significant question of whether a corporation falls within the definition of "separate entity" and therefore is entitled to immunity from jurisdiction under the FSI Act is not always straightforward. [5] The Full Federal Court of Australia has recently[6] clarified that the test of when an individual or a corporation will be regarded as a separate entity of a foreign State, is whether the individual or the corporation is being used to achieve some purpose or end for the foreign State in the relevant circumstances.

The exceptions to the absolute grant of immunity from jurisdiction are set

out at Part II of the FSI Act. One exception is that a foreign State (and its separate entities) will not have immunity where the proceeding concerns a "commercial transaction".[7] There has been little judicial guidance on the meaning of this term and the scope and application of this exception until this recent High Court decision. The decision also provides useful insight into the Australian's approach to extending sovereign immunity to State owned entities.

The High Court has held that the "commercial transaction" exception to the immunity is not limited to proceedings instituted against the foreign State or separate entity in relation to contracts. Nor is it limited to proceedings commenced by a party to a commercial transaction.[8] Proceedings brought by regulators can fall within the exception.

Background facts

In 2009, the Australian Competition and Consumer Commission (ACCC) commenced proceedings against airlines including PT Garuda Indonesia Ltd (Garuda), alleging that they had entered into anti-competitive arrangements or understandings between themselves to impose surcharges on commercial freight services to Australia and that the anti-competitive conduct was implemented by way of prices charged in contracts entered into by Garuda with its customers.

The ACCC alleged that this conduct contravened s45 of the *Trade Practices Act* 2010 (Cth), and sought orders including the imposition of a pecuniary penalty of up to A$250,000 per airline. A civil proceeding for the imposition of a pecuniary penalty is a proceeding to which the FSI Act might apply.

All of the airlines including Garuda claimed that they fell within the definition of a separate entity under the FSI Act, and therefore had immunity from the jurisdiction of the Australian courts in the proceedings brought by the ACCC. Garuda sought an order that the proceedings be dismissed or stayed.

"Separate Entity" test

The primary judge in the Federal Court considered that the test of whether an individual or a company is a separate entity is whether the foreign State exerts day-to-day management control.[9] On appeal, the Full Federal Court held that this was not the correct test.[10]

The Full Federal Court considered that in determining whether an individual or a corporation is a separate entity of a foreign State, regard will be had to: ownership, control, the functions which the corporation performs, the foreign State's purposes in supporting the corporation, and the manner in which the corporation conducts itself or its business.[11]

The Full Federal Court determined that the correct approach is to consider, on the whole of the evidence, "*whether the corporation or individual is being used to achieve some purpose or end for that State in the relevant circumstances*"[12].

95.5% of the issued shares in Garuda are owned by the Republic of Indonesia and the minority shareholding is held by government-controlled corporations associated with Indonesian airports. At relevant times four of the five members of its Board of Commissioners were senior officials of the Indonesian Government.

Garuda was held by the Full Federal Court to be a separate entity. The Court considered that it was difficult to see what other purpose Indonesia could have had in incorporating, directly owning 95.5% of, and investing in Garuda, unless it wanted the airline to act in the state's interests.

The Court found it persuasive that all shareholders in Garuda (including the holders of the remaining 4.5%) were governed by Indonesian state-ownership laws that had the stated purpose of being to "*benefit the public by providing high-quality and satisfactory … services fulfilling the needs of the people*".

Interestingly, the Full Federal Court considered that another of the airlines, Malaysian Airline System Berhad (MAS) was not a "separate entity" and therefore was not immune from liability. This was despite a majority shareholding in MAS by the Malaysian Government, and the exercise of complete control by government officials over the airline.

The Full Federal Court considered MAS was in a different position to Garuda, first because it is a public listed company on Bursa Malaysia, and secondly because it has third-party shareholders and is not therefore solely accountable to Malaysia.

Loss of immunity by the "commercial transaction" exception

Section 11(1) of the FSI Act provides that a foreign State is not immune in a proceeding in so far as the proceeding concerns a "commercial transaction" which is defined as:

"a commercial, trading, business, professional or industrial or like

transaction into which the foreign State [separate entity] has entered or a like activity in which the State has engaged and, without limiting the generality of the foregoing, includes:

a) a contract for the supply of goods or services;

b) an agreement for a loan or some other transaction for or in respect of the provision of finance;

c) a guarantee or indemnity in respect of a financial obligation;

but does not include a contract of employment or a bill of exchange."

In relation to Garuda, the Full Federal Court gave quite a wide interpretation to the term "commercial transaction", which the Court considered extended to arrangements or understandings which would likely have the effect of substantially lessening competition.

It was on this basis that the Court found that if it were established that Garuda was party to various price fixing, market sharing and anti-competitive cartels with the other airlines, then such conduct would concern a commercial transaction. Therefore whilst Garuda was a "separate entity", it was not entitled to immunity from the jurisdiction of the Court in the proceedings brought by the ACCC as the proceedings were found to concern a "commercial transaction."

Garuda was granted special leave to appeal to the High Court of Australia on the question of whether the proceeding concerned a "commercial transaction". In particular Garuda argued that the words "commercial transaction" should be interpreted as only applying to a dispute between parties in contractual relations, or as to the existence of their contractual relations – that is, to litigation which is private in nature – neither of which were the case with the claims raised against it by the ACCC.

Decision of the High Court

On 7 September 2012, the High Court dismissed Garuda's appeal on the basis that the definition of "commercial transaction" was satisfied in respect of the arrangements and understandings which the ACCC alleged that Garuda had entered into with the other airlines.

As a matter of statutory interpretation, the High Court held that the "commercial transaction" exception to immunity does not require that the activity concerned be contractual in nature, nor does it require that proceedings be instituted against the foreign State by a party to the commercial transaction in question.

Significance of the decisions

This decision is particularly relevant for the many companies which will deal with Foreign Governments, companies and entities that are controlled by Foreign Governments as well as sovereign wealth funds that invest and/or conduct business in Australia (such as in its finance, energy and resources and agriculture sectors).

This is especially important for those Australian companies which engage in cross border trade, and those which are dealing with foreign entities investing into Australia. Foreign investment is welcome in Australia, and more and more of it is coming from Foreign Governments, companies and entities that are controlled by Foreign Governments and sovereign wealth funds.

The application of the FSI Act may impact on the ability of Australian companies to bring civil proceedings in Australian courts against certain state owned entities.

The decision of the Full Federal Court is significant as it emphasises that in determining whether a state owned entity will generally be protected by immunity from civil proceedings in Australia, a court will not treat ownership and control as determinative, but will also consider factors such as the foreign State's purposes in supporting the entity.

Further, the High Court's decision clarifies that the "commercial transaction" exception to Foreign State immunity will apply not only to proceedings that are private in nature, that is proceedings brought between parties to a commercial transaction, but will extend to civil proceedings brought by Australian regulators in which they seek pecuniary penalties, if the subject matter of the allegations concern commercial transactions or like activities.

Conclusion

Australian companies need to be aware of the scope of their rights when dealing with Foreign Governments and foreign entities in which Foreign Governments have an interest.

Likewise, foreign States conducting commercial activities in relation to Australia need to be aware that immunity from proceedings in Australian courts will not apply where the entity involved is not being used to achieve some purpose for the State and/or where the entity is engaging in commercial activities (whether or not the activities are contractual in nature).

This means that counterparties and regulators can pursue them in Australian courts in some instances.

They need to carefully understand their legal obligations and comply with them.

If you are dealing with Foreign Governments, companies and entities that are controlled by Foreign Governments or sovereign wealth funds, we would be happy to discuss with you the scope of your rights and the ways in which you can protect your rights.

If you are a Foreign Government, company or entity controlled by a Foreign Government or a sovereign wealth fund wanting to understand the law as it applies to you we would be happy to discuss this with you.

Footnotes

[1] As defined under the FSI as "*separate entities*", and subject to meeting the requirements of that definition.

[2] "*Foreign State*" is defined in section 3 of the FSI Act.

[3] The FSI Act also deals with service of initiating processes on a foreign State and enforcement of judgments, orders or arbitration awards against property of a foreign State. However, only the issue of immunity from jurisdiction is addressed in the *PT Garuda Indonesia Ltd v Australian Competition & Consumer Commission* (2011) 277 ALR 67 case, and consequently in this briefing.

[4] See the definition of "*separate entity*" in section 3 of the FSI Act. "*Separate entity*" is further defined in section 3(2) of the Act, which states that a natural person who is, or a body corporate or corporation sole that is, an agency of more than one foreign State shall be taken to be a separate entity of each of the foreign States.

[5] Note that the test for "separate entity" is narrower in relation to Part IV of the FSI with respect to immunity from execution.

[6] *PT Garuda Indonesia Ltd v Australian Competition and Consumer Commission* (2011) 277 ALR 67

[7] Section 11 of the FSI Act.

[8] *PT Garuda Indonesia Ltd v Australian Competition & Consumer Commission* [2012] HCA 33 (7 September 2012)

[9] *Australian Competition & Consumer Commission v PT Garuda Indonesia Ltd* (2010) 269 ALR 98

[10] *PT Garuda Indonesia Ltd v Australian Competition & Consumer Commission* (2011) 277 ALR 67 at [72] per Rares J

[11] Ibid 76 at [48] per Lander and Greenwood JJ

[12] Ibid 52 at [128] per Rares J

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