

Undertaking to the Australian Competition and Consumer Commission

Given under section 87B of the *Competition and Consumer Act 2010* (Cth) by Philip Morris Ltd (ABN 65 004 694 428).

1 Person giving the Undertaking

1 This Undertaking is given to the Australian Competition and Consumer Commission (**ACCC**) by Philip Morris Ltd (ABN 65 004 694 428) (**PML**), for the purposes of section 87B of the *Competition and Consumer Act 2010* (**CCA**).

2 Background

2.1 Australian Consumer Law and mandatory safety standard

2 Section 18 of the Australian Consumer Law (**ACL**), contained in Schedule 2 to the CCA, provides that a person must not in trade or commerce, engage in conduct that is misleading or deceptive, or is likely to mislead or deceive.

3 Section 29 of the ACL sets out prohibitions against the making of certain false or misleading representations in trade or commerce, in connection with the supply or use of goods including:

(a) in s29(1)(a), a false or misleading representation that goods are of a particular standard; and

(b) in s29(1)(g), a false or misleading representation that goods have performance characteristics.

4 Section 33 of the ACL provides that a person must not, in trade or commerce, engage in conduct that is liable to mislead the public as to the nature, the manufacturing process, the characteristics, the suitability for their purpose or the quantity of any goods.

5 Section 106(1) of the ACL, provides that a person must not, in trade or commerce, supply consumer goods of a particular kind if:

(a) a safety standard for consumer goods of that kind is in force; and

(b) those goods do not comply with the standard.

6 As a result of the *Trade Practices (Consumer Product Safety Standard) (Reduced Fire Risk Cigarettes) Regulations 2008* (**Reduced Fire Risk Standard**), the supply of cigarettes in trade or commerce requires that cigarettes so supplied must comply with the Reduced Fire Risk Standard.

7 To comply with the Reduced Fire Risk Standard, cigarettes are manufactured in such a way that, when lit and left unattended, they have a propensity to go out by themselves. This is often done by using Low Ignition Propensity paper to manufacture them. Testing for compliance with the Reduced Fire Risk Standard is done by lighting sample cigarettes in laboratory conditions and observing whether they burn along their full length. The Reduced Fire Risk Standard states that such testing must be done in accordance with Australian Standard AS4830-2007 Determination of the extinction propensity of cigarettes (AS4830). Compliance with the standard requires that 75% go out before they burn along their full length. The risk of cigarettes starting fires is greatly reduced if those cigarettes comply with the Reduced Fire Risk Standard.

2.2 PML's actions

(a) Launch of new product

8 In September 2015, PML launched two new blended tobacco products into the Australian market, *choice Signature Classic* and *choice Signature Bold* each in packs of 20 cigarettes (the **Products**).

9 Approximately 1.8 million packs of the Products were produced in the facilities of a PML affiliate in South Korea (**PMK**) and transported to Australia in August 2015 for sale from 1 September 2015.

(b) Identification of potentially non-compliant products

10 On Monday 5 October 2015, PML identified that there may be an issue with the Products relating to the test results conducted on 2 October 2015 to determine compliance with the Reduced Fire Risk Standard. A decision was made to obtain further information from PMK and to conduct retesting of the Products immediately. PML collected samples from its national distribution centre in Victoria.

11 On Tuesday 6 October 2015, PML's accredited testers in Indonesia advised PML that samples of the Products tested did not comply with the Reduced Fire Risk Standard.

12 On Wednesday 7 October 2015, PML decided to immediately stop selling the Products pending results from the retesting, and the samples collected on Monday 5 October 2015 were immediately transferred to the testing site in Indonesia. At this time, 306,000 packets of 20 cigarettes had been supplied to retailers for sale. The remaining 1.5 million packets of the Products remained in PML controlled warehouses.

13 On Saturday 10 October 2015, PML received the results of additional testing that confirmed that tested samples of the Products were not compliant with the Reduced Fire Risk Standard.

(c) Voluntary recall

14 On Monday 12 October 2015, PML initiated a voluntary trade level recall of the Products from all retail outlets with the aim of having all Products removed from sale by retailers by Thursday 15 October 2015. PML considered that, given typical consumption patterns, all Products purchased by consumers were likely to have been consumed by the weekend after 15 October 2015.

15 On Wednesday 14 October 2015, PML informed the ACCC by telephone of PML's voluntary trade recall of the Products and filed a formal notification with the ACCC.

16 PML has fully cooperated with the ACCC both in relation to the voluntary recall and the ACCC's enquiries. This cooperation included advertising the voluntary recall to consumers as agreed with the ACCC.

17 On 5 February 2016, PML provided a final report to the ACCC on the voluntary recall, in which it reported that:

(a) 192,470 of the 306,000 packs of the Products supplied to retailers were recovered from retailers; and

(b) 113,530 packs of the Products had been sold to consumers and none of these packs were returned by consumers.

18 The lack of any returns by consumers is consistent with PML's expectation that all Product purchased by consumers before the voluntary recall would have been quickly consumed by them.

19 PML has not received any consumer complaints about the Products and it is not aware of any safety-related incidents arising from the consumption of the Products.

3 The ACCC's consideration of PML's conduct

20 The ACCC has formed the view that PML supplied 306,000 packets of the Products containing cigarettes that were likely to be non-compliant with the Reduced Fire Risk Standard, and in doing so is likely to have contravened sections 18, 29(1)(a), 29(1)(g), 33 and 106(1) of the ACL.

21 PML acknowledges that by offering the Products for retail sale, it is likely to have contravened sections 18, 29(1)(a), 29(1)(g), 33 and 106(1) of the ACL.

4 PML's investigations and changes to PML's systems

22 PML promptly investigated why it had not detected that the Products may not have complied with the Reduced Fire Risk Standard before they were sold. PML discovered that, due to the Products' relatively small batch size, they had been exported to Australia by air instead of by sea (which is the norm), which meant that they arrived in Australia before the Reduced Fire Risk Standard testing had been completed. PML's processes did not prevent the Products being supplied without having first passed that testing.

4.1 PML's immediate changes

23 Immediately after the investigation, PML implemented changes to its systems, effective November 2015, to prevent a recurrence. These changes were to:

- (a) ensure that the testing results are received before the release of the products to market by holding the products in PML's national distribution centre in Victoria until the testing results have been obtained; and
- (b) requiring the testing site to immediately notify by phone (on the same day of analysis) the Australia OPS Director or Manager Australia Product Services and the manufacturer where the testing identifies any failure to comply with the Reduced Fire Risk Standard.

24 In addition to the systems changes referred to in paragraph 23, following consultation within PML and its affiliates, further systems were implemented effective 1 January 2016. These further systems involved three main changes to PML's previous system.

- (a) In addition to having all manufactured products sent to Australia and stored in PML's national distribution centre, these products are automatically placed on 'hold' until such time that laboratory results show that products are compliant with the Reduced Fire Risk Standard. The 'hold' is recorded in the Inventory Management System used by PML and results in stock levels appearing as zero and no stock being able to be allocated to customers.
- (b) The 'hold' status is only released once laboratory results confirm that all products are compliant with the Reduced Fire Risk Standard and only on the authority of one of two PML employees, Manager Supply Chain and Logistics or Manager Product Services.
- (c) To facilitate testing, samples are sent by the manufacturer to the testing facility during the first week of any production batch.

4.2 Donation

25 In addition to its obligations outlined below, PML has advised the ACCC that it will make a donation of \$300,000 to the NSW Rural Fire Service.

5 Commencement of Undertaking

26 This Undertaking comes into effect when:

- (a) the Undertaking is executed by PML; and

(b) the ACCC accepts the Undertaking so executed.

6 Undertaking

27 Upon the commencement of this Undertaking PML undertakes to:

- (a) not, in trade or commerce supply, or offer for supply products that do not comply with the Reduced Fire Risk Standard; and
- (b) continue to have systems directed to the prevention of the supply of products that do not comply with the Reduced Fire Risk Standard as outlined in paragraph 24 above,

for the purposes of section 87B of the CCA for a period of 3 years.

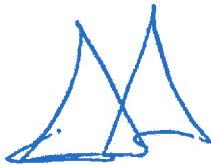
7 Acknowledgments

28 PML acknowledges that:

- (a) the ACCC will make this Undertaking publicly available including by publishing it on the ACCC's public register of section 87B undertakings on its website;
- (b) the ACCC will, from time to time, make public reference to this Undertaking including in news media statements and in ACCC publications; and
- (c) this Undertaking in no way derogates from the rights and remedies available to any other person arising from the alleged conduct.

Executed as an Undertaking

Executed in accordance with section 127 of the *Corporations Act 2001* by Philip Morris Ltd, (ABN 65 004 694 428):



Director Signature

N. Theofilopoulos

Print Name



Director/Secretary Signature

ROSAMUND GILLIAN FIELDEN

Print Name

Accepted by the Australian Competition and Consumer Commission pursuant to section 87B of the Competition and Consumer Act 2010 (Cth) on:

Date

23/11/16

and signed on behalf of the Commission:



Signature

Chairman

Rod Sims

Print Name

Date: