

Experts ask where their first responsibility lies

by Fiona Buffini

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After the Jackson inquiry, there is a lot of soul-searching going on at eminent professional firms.

When James Hardie told the public its asbestos compensation trust had enough money for future victims, it did so on the basis of “expert advice”.

The experts signed off on asbestos estimates that were “far too low” and on a financial model that was “wildly optimistic”, an inquiry led by David Jackson, QC, found this week.

It found Hardie never asked the experts — PricewaterhouseCoopers, Trowbridge or Access Economics — the right questions to tell if the trust, underfunded by at least \$1.5 billion, had enough money.

Senior executives, including Hardie chief Peter Macdonald, now face investigation for misleading the market.

While Jackson found Hardie carefully controlled its professional advisers and, in some cases, misused their advice, none of them blew the whistle after learning what was going on.

“Our people found it extremely difficult to know where to go, to know what to do,” says Trowbridge Deloitte chief Colin Brigstock.

“The big issue is what do you do if you’re involved with a transaction that just looks to be ethically or legally wrong . . . at the moment you really have no recourse. We have no whistleblower protections as exist in the insurance industry. It goes back to the role of professionals in our business system and one role is to provide assurance that people don’t do the wrong thing.”

One month before Hardie set up the trust in 2001, management told their board there was “no reliable basis” for assessing asbestos liabilities; the Trowbridge actuarial report was too uncertain. A few weeks later, the board accepted a version of the same actuarial report, which it never read, to justify separating its liabilities, though Trowbridge had not been asked to address this.

Jackson found that Hardie, and senior executive Peter Shafron, failed to ask the “first logical question: What actuarial advice do we need for a separation exercise?” They failed to address the question despite investor relations officer Steve Ashe flagging it a few months before. They even failed to tell Trowbridge until after it wrote the report how it would be used.

These “serious errors” were compounded by instructing Trowbridge to use high discount rates to reduce the estimate, and not asking Trowbridge to allow for judicial inflation despite knowing this was a problem.

Hardie’s use of the Trowbridge report was “careless in the extreme”, and Jackson found it “difficult to believe that Shafron and Macdonald could have had any faith” in using it to set the critical funding of the trust.

Hardie engaged PwC and Access after former Labor senator Stephen Loosley advised that the trust would be easier to sell if someone else verified the figures.

Shafron outlined the role of PwC and Access to Hardie executive Philip Morley, who was modelling how long the trust would last. "A job for you on Monday, get these guys to bless your model," Shafron wrote in an email.

Access and PwC (which is also Hardie's auditor) did bless the model, although they were told not to check its key assumptions, just that it added up, an exercise Morley agreed in the witness box was "arid and pointless".

Both firms warned of the model's limitations but there was "much doubt" the warnings were conveyed to the board.

A few days later, Macdonald issued a media release saying the trust was "fully funded", citing Trowbridge, PwC and Access a release Jackson found was a "pure public relations construct, bereft of substance".

In truth, the trust was "massively underfunded", on its way to being a "financial basket case" and the use of PwC and Access in the release presented a "quite incorrect view" of their actual role. But none of the experts complained about the media release or raised an alarm.

Jackson found Trowbridge's failure to alert Hardie or the trust after the press release "impossible to justify".

It was also "disturbing" that not one of the many advisers Hardie used, most closely law firm Allens Arthur Robinson, ever warned that the trust would fail unless it actually was fully funded, and that that should be "rigorously checked". Professionals say their ability to speak out is too restricted by client confidentiality contracts and changes should be considered. Actuaries are considering "public interest" clauses to remind clients of their wider duties. Others suggest reforms protecting whistleblowers for breaking confidentiality, like changes to the insurance industry after HIH.

"It's a difficult issue," Brigstock says. "Our code of conduct starts with an obligation to the public interest. But you've also got obligations to clients and the problem is what you do when those two come into conflict; at the moment the client wins legally."

Hardie shows the dangers for boards and advisers in taking a narrow view of their obligations.

"HIH, Enron and James Hardie all demonstrate that companies and their advisers need to consider their reputations; they need to go beyond their strict legal obligations," ex-regulator and lawyer Kathleen Farrell says.

It's not a new issue. As judge Neville Owen said on corporate governance in HIH: "I found myself rhetorically asking: Did anyone stand back and ask themselves the simple question, is this right?"