

## **Why the Hardie finding will be good for corporate governance**

Elisabeth Sexton

August 21, 2009

Since the former board of James Hardie was found guilty of corporate misconduct in April, a torrent of business commentary has suggested that the law expects too much, particularly of non-executive directors.

These are the part-time stewards of a company charged with setting strategy and supervising its management.

The gist has been that the NSW Supreme Court decision was just about a single media release.

OK, it was about the politically sensitive subject of compensation for asbestos diseases. And, yes, it turned out the rosy assertion in 2001 that a new \$293 million trust would be “fully funded” was, by 2004, about \$1.5 billion out.

Even so, the argument goes, the non-executive directors had paid too heavy a price in the damage to their reputations and careers for a one-off lapse about PR. And more broadly, Justice Ian Gzell’s ruling had set an unrealistic standard by expecting boards to check every media release and micro-manage executives.

This sentiment was summed up in a June headline in *The Australian Financial Review*: Is this the death of the non-executive director?

If it wasn’t clear enough from Justice Gzell’s decision in April, his reasons yesterday for banning the directors from boardrooms for five years spell out that their breach of duty was more than an inadvertent slip. The board’s approval of the media release in 2001, “while isolated, was highly significant,” the judge said yesterday.

The non-executive directors knew from their board papers that James Hardie had to convince the public there were sufficient funds in the new trust to meet all legitimate asbestos claims, he said. They were aware of the significance of what the release would say about the level of funding. The advice they had received did not support its emphatic wording.

Their approval of the release was a deliberate attempt to gain acceptance of the plan to remove asbestos claims from the James Hardie group into the new trust.

“This was a serious breach of duty and a flagrant one,” the judge said.

These views might be overturned on appeal in a higher court. But that possibility does not alter the gravity of what was at stake in this case.

It was about convincing the federal and state governments that, in undertaking a major corporate restructure, James Hardie could be trusted to look after people suffering from vicious diseases.

Thousands of Australians are expected to contract mesothelioma and asbestosis from exposure to James Hardie products for decades to come.

One testimonial filed in the case was from the investment banker Peter Hunt, who advised the then chairman Meredith Hellicar during the three-year negotiations for the new compensation scheme which replaced the underfunded trust in 2007.

Hunt, the executive chairman of Caliburn, described a task made difficult by uncertainties - in projecting future claims, economic growth rates, investment returns and James Hardie's performance and funding capacity for at least 40 years - and by the complexity of the legal issues involved and the public and media spotlight on the negotiations.

Hunt praised Hellicar for her hard work yet his account of how much was involved in achieving the new scheme underlined the directors' shabby job of addressing these same uncertainties and complexities in 2001.

Directors and advisers hyperventilating about the wider impact of the penalties handed down yesterday should consult a note sent by law firm Arnold Bloch Leibler to its clients about Justice Gzell's main decision in April. ABL was involved in the case, representing the former non-executive director Dan O'Brien.

It began by noting the judgment had caused "widespread alarm within the business community" and that "some in the media have gone so far as to label the decision "a blow against good corporate governance" which will distract directors from their primary function of guiding a company's strategy".

The law firm said rather than being such an attack on good governance, "the case simply reaffirms that directors must actively participate and scrutinise matters discussed at board meetings" and should satisfy themselves about the accuracy of "announcements of importance to the company and the public".

You don't need to be an expert in corporate law to work that out.

*Elisabeth Sexton is a Herald journalist.*