**Judge ends board game at James Hardie and ASIC scores a win**

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*ASIC's battle against 10 former directors and executives of James Hardie was a fierce one, writes Elisabeth Sexton.*

The corporate regulator did not have an easy road to its Supreme Court victory over 10 former directors and executives of James Hardie.

Of the eight witnesses called who attended a fateful board meeting on February 15, 2001, not one gave evidence that the central document of the case — a media release about asbestos compensation — was tabled at the meeting.

Nor did it help the Australian Securities and Investments Commission when it produced transcripts of earlier sworn statements from two key players in the drama who have since died, the James Hardie chairman Alan McGregor and a partner of law firm Allens Arthur Robinson, Peter Cameron.

Neither of them mentioned the release being tabled either.

With some understatement, Justice Ian Gzell said in his Thursday judgment that this lack of "positive evidence" from 10 witnesses did "not augur well for ASIC".

And the fierce fight put up by the defendants was hardly auspicious for the plaintiff. All had big reputations to protect, were able to rely on corporate indemnities to fund their share of what the judge described as "the enormous cost of this venture" and are, as he put it, "intelligent people".

Five of the non-executive directors chose to enter the witness box in their own defence. Martin Koffel and Peter Willcox swore that they had not approved the release. Michael Brown, Michael Gillfillan and Meredith Hellicar did not agree that it was approved.

Lawyers for the other two — Dan O'Brien and Greg Terry — argued there was not enough evidence to get ASIC to first base.

But ASIC's barrister, Tony Bannon, SC, has a reputation for tenacity. Large parts of the hearings were taken up with his pursuit of enough material to convince Justice Gzell to infer that the release was approved.

In the end Bannon persuaded the judge that, contrary to their sworn evidence, the directors discussed and approved the media release.

The defendants' decisions to enter the witness box backfired. The judge did not believe their "chorus of non-recollection", a damaging finding for any director or senior executive.

In Hellicar's case, Bannon's search for additional proof about what happened at the February board meeting had the more serious consequence of Justice Gzell saying "there was a dogmatism in her testimony that I do not accept" and that "she was proved to be inaccurate on a number occasions".

For example, Bannon pursued email evidence that five days after the

meeting, the directors held a phone hook-up to discuss the reaction to the media release.

Hellicar told the court she did not recall the board agreeing to hold the teleconference and she had not participated because she was attending a seminar at Coolum on that day.

Confronted with telephone records, Hellicar abandoned her evidence. "This incident tells against Ms Hellicar's credit," the judge said. "It was not the only incident in her testimony that an adamant statement made by her turned out to be wrong."

In the case of Brown and to a lesser extent Koffel, concessions they made under cross-examination about discussion at the meeting helped convince the judge that the board did approve the release.

The decision by the five defendants to give evidence also made it easier for Bannon to make out the other elements of his case on the media release.

He succeeded in arguing that all the directors knew it was misleading when it said a new asbestos compensation trust was "fully funded" and "provided certainty" for asbestos disease claimants. Further, they appreciated that if the truth came out, James Hardie's reputation would be harmed.

All that added up to breaches of their duties to the company to act with care and diligence, Justice Gzell found. Also guilty of insufficient care and diligence are the three executive defendants, the former chief executive Peter Macdonald, the former general counsel Peter Shafron and the former chief financial officer Phillip Morley. Only Morley chose to give evidence.

All three were found to have provided inadequate advice to the board before it approved the misleading media release.

There were also other breaches of duty of care by Macdonald and Shafron over other disclosures about asbestos.

A more serious allegation levelled only at Macdonald, that he did not act with good faith and for a proper purpose, was dismissed.

So was the second major part of ASIC's case, that there were also misleading statements about asbestos compensation in an information memorandum sent to shareholders and the

court in August 2001. The memorandum was prepared to gain approval for the company's move to the Netherlands two months later.

The judgment contains pronouncements about the responsibilities of directors and senior managers which will be pored over by many, particularly in the present climate of economic hardship and investor distress.

However, its enduring impact will not be known until after another hearing, when the defendants will have the opportunity to argue they should be relieved of liability. Appeals are also being considered.

The Corporations Act gives the court the power to exonerate breaches of directors' or officers' duties if "the person has acted honestly; and having regard to all the circumstances of the case — the person ought fairly to be excused for the contravention".

That may be an uphill battle, at least in the case of Hellicar.

"I have grave doubts about her evidence and that may have some relevance to the exoneration provisions that are invoked on her behalf," the judge said.

When the case began on September 29, Bannon relied on the formal minutes of the February meeting from the company's files, which said the board approved the release.

BY the seventh hearing day, October 8, it was obvious the defendants were going to challenge the accuracy of those minutes.

"We didn't understand that the public company directors were going to assert that their own minutes, which they confirmed, are incorrect," Bannon said that day.

Spirits rose among the defence lawyers when it emerged that ASIC had decided not to call as witnesses three people who had also attended the February meeting. They were a second Allens partner, David Robb, and two financial advisers from investment bank UBS, Anthony Sweetman and Ian Wilson.

The decision indicated that their proposed evidence would not help ASIC's case, the defendants suggested. After all, the three were ASIC witnesses and not expected to be sympathetic to the defence.

This submission cut little ice with Justice Gzell.

"Notwithstanding the cooperation of the three gentlemen with ASIC in the production of proofs of evidence, they remained in the camp of the defendants," the judge said.

James Hardie was a client of UBS and Allens, and "there is no suggestion that the three gentlemen could not have been called in the case of any of the defendants and there is no

suggestion that they would not have co-operated to the same extent as they had been prepared to do with ASIC. They were the last surviving independent advisers."

Three pieces of evidence persuaded the judge that the release was discussed and approved at the meeting.

The first came from James Hardie's former head of public relations, Greg Baxter, from the witness box.

He recalled taking a draft release with him to the meeting, which was supported by an email he sent to an associate that morning saying "this is the version I will take to the Bd meeting".

The judge found Baxter's evidence about whether the draft was read aloud at the meeting "equivocal" but concluded that either he or Macdonald "spoke to" the draft and put to the meeting "statements as to the key message to be communicated to the market".

The second decisive evidence was that three identical copies of the draft Baxter said he took with him, which differed in several places from the final published version, were produced under compulsion to ASIC.

Two were found in the files of the Allens partners, Cameron and Robb, and a third in the files of Brierley Investments Ltd. Two of the defendants, O'Brien and Terry, were on the James Hardie board in 2001 because they were executives of Brierley, which at the time owned a 29 per cent stake in James Hardie.

"There is no reason why Mr O'Brien or Mr Terry would have received the document from Mr Baxter after the meeting," the judge said. "And if they received their copies at the meeting, the clear inference is that so did Mr Cameron and Mr Robb."

The judge accepted that those four "would not have been the only persons to whom the document was distributed" at the meeting.

The third significant evidence was extracted under cross-examination from Koffel and Brown.

Koffel accepted that someone "could have outlined" what was to be in the announcement and "might have outlined" what was to be said about the sufficiency of funding.

Brown went further. He recalled the board discussing the overall communications strategy and the key messages at the meeting.

He also said it was likely that the board's approval of those messages was "summarised by Mr McGregor in the usual fashion, saying 'is the board happy with that?', and everybody nodded or otherwise indicated their agreement".

The accumulation of these pieces of evidence outweighed the “mistaken” testimony of the five directors who had an interest in saying the release was not before the meeting, the judge found.

“If a person was minded to dissemble, it would be an easy task for that person to say that he or she could not recall the draft ASX announcement being discussed at the meeting,” he said.

The next step was for ASIC to prove that the release was misleading by being “too emphatic” about the adequacy of the new trust’s $293 million assets to meet future claims from people who fall ill from exposure to James Hardie asbestos products.

The judge made short work of submissions that the word “certainty” was ambiguous because it could mean either that all claims would be paid or that the new trust made it certain that the $293 million would be spent meeting claims and not on other corporate purposes.

The latter was “a tortuous reading of the document,” he said.

Even a sophisticated reader of the release would assume — incorrectly — that James Hardie had “adopted highly conservative assumptions in determining the funding” for the trust, he said.

The evidence of the five directors who chose to appear went against them here, too.

All said they knew they had not authorised the release because it contained such unequivocal statements about the sufficiency of the trust’s funding that they would not have approved it.

“The non-executive directors knew that the draft ASX announcement contained false or misleading, or deceptive statements,” Justice Gzell said. “That is why all of them who gave evidence said they would not have approved it.”

THE judgment lists material presented to the board in May, August, October and December 2000 and January 2001 indicating the unreliability of actuarial forecasts of likely future claims.

This was not a claim of directors being expected to second-guess management or to go out of their way to interfere in operational matters.

There was also a detailed presentation about the new trust at the critical February 2001 meeting. Justice Gzell found that during that presentation the three executive defendants failed in their duty to advise the board properly.

Notwithstanding their failure, “the non-executive directors must have realised that

unqualified statements that there were sufficient funds in the foundation to cover all legitimate asbestos claims could not be made," he said.

Testimony by directors that they had not received copies of the final announcement sent to the stock exchange was also counter-productive.

"It is extraordinary that none of the non-executive directors who gave evidence recalled seeing the document that announced a most significant event in the life of the James Hardie group, an event that they were at pains to ensure was well received by the market," Justice Gzell said.

"Had they received copies of the final ASX announcement, and had it been true that they would not have approved the draft ASX announcement, they would have expressed the concern that it made forward-looking statements with which they disagreed."

There was no evidence any director ever complained about the content of the published release, he said.

Then ASIC's task was to argue that approving the release was in breach of directors's duties.

Some defendants submitted that writing media releases was the job of management, not the board. The judge disagreed.

"Management had sought the board's approval and the task of approving the draft ASX announcement involved no more than an understanding of the English language used in the document," he said.

Setting up the trust went beyond operational responsibility and involved "potentially explosive steps".

"Market reaction to the announcement of them was critical," he said. "This was a matter within the purview of the board's responsibility: what should be stated publicly about the way in which asbestos claims would be handled by the James Hardie group for the future". It was part of the function of the directors in monitoring the management to settle the terms of the draft announcement to ensure that it did not assert the trust had sufficient funds to meet all legitimate compensation claims and did not state that the foundation was fully funded, he said.

It was also submitted — unsuccessfully — that a director with no particular expertise in public relations was entitled to leave the approval of public statements to better-equipped fellow directors.

"All of the non-executive directors — knew or should have known that if James Hardie made the statements as to the sufficiency of funding of the foundation in the draft ASX

announcement, there was the danger that James Hardie would face legal action for publishing false or misleading or deceptive statements, its reputation would suffer and there would be a market reaction to its listed securities," Justice Gzell said.

"This was not a matter in which a director was entitled to rely upon those of his co-directors more concerned with communications strategy to consider the draft ASX announcement. This was a key statement in relation to a highly significant restructure of the James Hardie group.

"Management having brought the matter to the board, none of them was entitled to abdicate responsibility by delegating his or her duty to a fellow director."

James Hardie and its shareholders benefited in the short term from public relations strategy developed by management and adopted by the board at the February meeting.

The establishment of the trust, and with it the illusion that James Hardie's involvement in asbestos compensation had ended, proceeded unimpeded.

The directors "may well have believed they were acting in the best interests of the James Hardie group in divorcing asbestos claims — from the group," the judge said.

That did not mean they were fulfilling their legal obligations to the company.