Allens Arthur Robinson

Special Commission of Inquiry into the Medical Research & Compensation Foundation

Submissions in Reply

of

James Hardie Industries NV

and

ABN 60 Pty Limited

on

Terms of Reference 1 to 3

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General Response to the Unions' Submissions

1. The Union submissions stand apart from those of the other parties and should be treated with care. They are written without regard to the convention and rule that serious allegations are not be made unless reasonably justified by the material available. They contain assertions of the most serious possible level of misconduct which, on no view, could be properly founded in the evidence.

2. For example, an allegation is made that Mr Robb and Mr Cameron were complicit in "perverting the course of justice" in Chapter 7 of the Union submissions. The evidence for this offence is described as the circumstances “previously referred to and [which] need not be repeated” (Unions 7.4).

3. Other examples of serious allegations made without any apparent evidentiary foundation are the allegations of conspiracy at Unions 9.1(c) and the allegations that judgment was obtained by fraud (at Unions 1.8, 4.30, 6.2, 6.3, 6.53). At paragraph 6.49(b), the Union submissions pass over the “fifth element” of fraud in *Wentworth v Rogers* (1986) 6 NSWLR 534, namely that “it must be shown *by admissible evidence* that the successful party was responsible for the fraud which taints the judgment under challenge” (emphasis added). The Unions have not addressed the requirement that the evidence be admissible, seeing fit to address this requirement in “summary form” by suggesting that “[n]o persons other than the JHIL interests ... could have been responsible for the fraud”.

4. The language of the Union submissions is also inflammatory: Mr Macdonald’s conduct is described as “deplorable” (4.17), Mr Shafron's conduct is described as "manipulative and scheming" (4.31), JHIL’s conduct is described as “heinous” (8.41), and the company’s conduct of past litigation is said to display “contumelious disregard for the rights of others” (8.43).

5. Further, at Unions 4.18, it is said that “Macdonald’s failure to inform his co-directors of the various matters set out in paragraph 4.16 should be seen as deliberate, misleading, disgraceful”. The second of those matters was "that Trowbridge did not have James Hardie data beyond March 2000”.

6. As to that, the evidence of Messrs Macdonald, McGregor and Peter Cameron is that the Board knew that Trowbridge did not have the most recent data. The references have been given at JH 12.2.6-12.2.7. The evidence of Mr Peter Cameron, in particular, was as follows (T3021.7-37):

> Q. You agree with me that your recollection of what happened at the Board was very vague?
>
> A. No.
>
> Q. You don’t remember who raised it?

A. I believe the issue of the claims data was raised by Mr McGregor.

Q. But was there raised at the board the question of whether or not the latest claims data had been given to Trowbridge and the question of whether Trowbridge might need that data or not?

A. I'm sorry, I understood that was the effect. The answer to that question, there was a debate at the Board because the claims data which was attached to the Board papers was a reference to the most recent claims and there was a question as to whether or not that had been taken into account by Trowbridge. That question, I understood, was raised, the extent of it by Mr McGregor. I'm reasonably comfortable with that recollection. There was a response, I'm not sure by whom, which substantially reflects the discussion to which you've just taken me.

Q. Did Mr McGregor – sorry, did Mr Macdonald or Mr Shafron say at the Board meeting that Trowbridge do not require the most recent data and it wouldn't make a difference to their conclusions because their reports were based on longer term trends?

A. I don't recall who said it. I believe it may have been Mr Macdonald but those words to that general effect were said at the Board meeting.

7. The contrary was never put to any of Messrs Macdonald, Peter Cameron or McGregor. Senior Counsel for the Unions chose not to cross-examine Mr Peter Cameron at all on the topic.

8. There was no failure by Mr Macdonald to inform the JHIL directors of those matters. The submission (Unions 4.18) that his alleged failure to do so was "deliberate, misleading and disgraceful" cannot properly be put.

9. Secondly, at Unions 9.39, it is said, in connection with Mr Robb's draft advice, that:

   (a) "Allens had purported to comply with numerous summonses to produce but had failed to provide this seminal document"; and

   (b) "Allens has provided no explanation for its failure to so comply".

10. These submissions are wrong. The Unions' submission is made by reference to questions asked of Mr Robb by Mr Slattery on the afternoon of 10 June 2004 in which Mr Robb *volunteered* that he had prepared the draft advice (T2873.55-2874.10), confirmed that it had been sent to the client (T2876.4-6) which led to a request for its production, made on the (false) premise that it had not already been produced. At the commencement of the following day, Counsel for James Hardie made it clear that "[c]opies of those documents were produced to the Commission on 21 May", but in any event distributed copies along the bar table (T2887.19-.40) and tendered those documents as Exhibits 191 and 192. Senior Counsel for the Unions then cross-examined Mr Robb on Exhibits 191 and 192, and confirmed that the documents which had by that time been provided *twice* to the Commission (initially on 21 May 2004, then again on 11 June 2004 in answer to the fresh

summons (T2889.12-14)) were the draft advice to which Mr Robb had referred on the previous day.

11. The submissions in Unions 9.39 should be withdrawn.

12. Thirdly, at Unions 9.40(b) it is said that:

> Robb and Cameron gave false evidence to the Commission as to the intention of JHIL to cancel the partly paid shares.

13. One would expect it to be stated what precisely was said by Mr Robb and Mr Peter Cameron, what in fact the position was, and on what basis it is said that they knew when they gave their evidence that it was false. One would also expect that submission to have been put to them squarely by the cross-examiner. Both are elementary aspects of natural justice and professional ethics. Neither has been done. The submission should be withdrawn.

14. This is not merely a case where submissions which in truth are not grounded in the evidence are put. This is a case where the submissions founded on false premises are of the most serious character conceivable. And, this has been done in circumstances where:

    (a) it is perfectly plain that the submissions will be given wide publicity;

    (b) it is perfectly plain that the reputation of the men involved will be tarnished; and

    (c) there is presently in place an active political process to consider amendments to the law.

15. The inference is available that the decision to make extremely serious submissions using highly inflammatory language against James Hardie and its lawyers has been influenced or motivated by a desire to create an impact on the political process. That, of course, would be a grave breach of the privilege enjoyed by the practitioners involved, and an abuse of process. That inference could be more confidently drawn if the many submissions which are not properly based are not withdrawn before the Unions' submissions become public.

A. The Current Financial Position of the MRCF

In response to the submissions of Counsel Assisting the Commission and the MRCF with respect to Term of Reference 1, the James Hardie parties rely on their submissions in chief and add the following.

A1 Current assets and liabilities of Amaca and Amaba

A1.1 There is little controversy as to the *current* liabilities and assets of Amaca and Amaba other than the extent of the insurance recovery rights. This matter is addressed below (see A2.1–A4.3).

Errata

A1.2 The MRCF misstated Amaba's income statements for the period June 2001 to May 2004, by putting all figures in units of $1 million rather than in units of $1,000.

A1.3 The James Hardie parties erred in stating Amaba's figure for Net Litigation Costs in the YTD May 2004 as $262,000: JH Term 1, Table 2. This figure should be $424,000, as recorded in the statutory declaration of Cooper (9 July 2004): Ex, 295 [9].

A2 Available insurance cover

A2.1 Counsel Assisting has not addressed the insurance cover issue pending "receipt of Mr Wilkinson's report on insurance matters and additional information anticipated from the MRCF". The James Hardie parties reserve their right to reply should Counsel Assisting make written submissions on this subject.

A2.2 The primary submissions on insurance cover are by the MRCF. The following paragraphs are a limited reply to the MRCF submissions, as the James Hardie parties' submissions in chief respond to almost all issues raised by the MRCF.

A3 General comments

A3.1 The MRCF submissions are made without reference to Mr Hutchinson's statement of 23 June 2004 (Ex 294). This statement qualifies the oral evidence given by Mr Hutchinson and the statement of 31 May 2004 (Ex 218) and substantially undermines the MRCF's submissions. As a minimum, the statement of Mr Hutchinson's "unchallenged evidence" at MRCF, 3.36–3.39 must be read in the light of Mr Hutchinson's later evidence.

A3.2 The MRCF concedes the uncertainty in the extent of its insurance cover, yet persists to offer a quantification of this cover. There is no basis for the MRCF's claim that "[w]hile it is impossible to quantify future recoveries it is likely that such recoveries will not exceed 12% of the claims paid and may well be less": MRCF, 3.5.

A3.3 There is also no basis for the claim that "[a]ny assistance provided by the HIH Claims Support Scheme should be regarded as speculative and a windfall": MRCF, 3.12, 3.61-3.73. Mr Hutchinson's evidence went much higher: see JH, Term 1, 20(a) – 20(d).

A3.4 The MRCF claims about the status of "late claims" for recovery under s54 of the *Insurance Contracts Act* have been made without the benefit of the legal advice which the MRCF claimed that it would obtain: MRCF, 3.46 and 3.52, cf JH, Term 1, 20(h) and 23(b).

A3.5 The MRCF does not address the question of the identity of the insurers of the London period policies and their solvency: cf MRCF, 3.29–3.34.

A4 Commutation value of various policies

A4.1 The MRCF has submitted that "time pressure" was a "considerable factor" for the James Hardie companies to enter into an allegedly reduced value commutation of the QBE policy in June 2000: MRCF, 3.98. Yet the MRCF acknowledges that it has insufficient information to be able to determine the precise justification for the amount of the QBE commutation in June 2000 "or to draw any conclusions as to [its] reasonableness": MRCF 3.97. In the absence of any evidence to the contrary, Mr Attrill's evidence on the reasonableness of the QBE commutation should be accepted, and allegations of improper motivations of "time pressure" should be rejected.

A4.2 Mr Hutchinson's opinion on the commutation value of the QBE policy should not be accepted. In evidence, Mr Hutchinson stated that he "*would have no way of knowing that [the commutation of the QBE policies at the time it was done] was either prudent or imprudent*": T2991.36. Mr Hutchinson stated that he had "*not analysed anything about the QBE commutation or the reasons for it or why the amount selected as agreed to by the parties*": T2991.42.

A4.3 In relation to the London policies of the 1981 to 1986 policies, the MRCF conceded that Mr Hutchinson "is not qualified in relation to commutation calculations and did not have available to him information to specifically calculate the commutation value of the 1981–1986 insurance policies": MRCF, 3.84. There is no reason, therefore, that Mr Hutchinson's views on the value of these policies should be accepted, as suggested in MRCF, 3.84.

A5 Suggested "future asbestos–related liability" figure

A5.1 Counsel Assisting stated that the "future asbestos–related liability" figure is "a sum not less than $2,240 million": CA, Section 1, [27]. In reaching this recommendation, Counsel Assisting proposed a number necessary to provide "reasonable confidence" that the asbestos liabilities of Amaca and Amaba will be met. There are two difficulties with that approach.

A5.2 First, it is more appropriate to attempt to determine, in the light of all the information presently known, the best estimate of those liabilities. Of course, there will be a measure of uncertainty, but that can be reflected in the finding by indicating a range. That is what Issue 1, in terms, is directed to.

A5.3 Secondly, there is *no* actuarial evidence to support the view that there is "reasonable confidence" that the asbestos liabilities will not exceed the amount selected. In respect of the possibilities of "third wave" claims, exemplary damages, etc, there is simply no basis on which it can be asserted that these claims, to the extent that they emerge, will make a difference to the central estimate. As the MRCF submission notes, "there is no evidence before the Commission which purports to estimate or quantify the impact of the future emergence of [third wave] claims": MRCF, 2.65. It is inappropriate to use the sensitivities in respect of other assumptions to provide a justification for such liabilities.

A5.4 Counsel Assisting derives the $2,240 million in the following way: start with Mr Wilkinson's figure of $1,573 million, then add, cumulatively, Mr Wilkinson's sensitivity figures for superimposed inflation ($384.6 million), claims size ($136.5 million) and claim numbers ($149.3 million): CA, Section 1, [25].

A5.5 However, sensitivity analysis is a tool for testing how a central estimate is affected by the various assumptions upon which it is based. The 10% increases in claim size and claim numbers are arbitrary: they show the impact of such an increase, but they do not, and are not intended to, provide a measure of reasonable confidence. Further, it does not follow that, by adding a buffer constituted by the sum of the sensitivity figures for superimposed inflation, average claim size and claim numbers, that a measure of "reasonable confidence" will be derived.

A5.6 Moreover, that addition is contrary to Mr Wilkinson's note: "If one were to wish to combine two or more scenarios together, adding the monetary changes indicated above would not necessarily reflect the true combined effect of the revised scenarios but would provide a broad indication of the financial impact": Ex 252, p 109.

A5.7 It is respectfully submitted that the Commission should:

(a) find that the central estimate should be **$1,573.4 million** (which is Counsel Assisting's starting point); and

(b) make it clear that the actual liabilities may be considerably more, *or less*, than that amount.

A6 Rate of superimposed inflation

A6.1 Counsel Assisting and the MRCF correctly identified the rate of superimposed inflation ***(SI)*** as the most significant difference in the actuarial evidence. The appropriate SI rate should be found to be 2%.

A7 No support for SI rates higher than 4%

A7.1 Counsel Assisting submitted that Mr Wilkinson had suggested that a more appropriate SI rate was a rate running at 6% for 5 years decreasing linearly to 2 % over 5 years, then remaining at 2% in the long term: CA, Section 1, [8]. Mr Wilkinson did not, in fact, suggest

this. Mr Wilkinson said that the 6% per annum figure for five years trending down to 2% per annum figure "remains an illustrative sensitivity test and not an alternative central estimate of mine": Ex 312, [19].

A7.2 The MRCF stated that "[i]t is possible that claims costs will increase above inflation and the adoption of a superimposed inflation rate of 4% (which means assuming future inflation at a rate of 8%) is ... possibly even conservative": MRCF, 2.10. It also stated that "[t]he evidence as to whether it is necessary to make allowance for superimposed inflation and if so, at what rate was inconclusive": MRCF [2.22]. The MRCF adduced no evidence on this issue, and did not participate in this stage of the hearing. Argument for a rate of superimposed inflation higher than 4% is entirely speculative and should be dismissed.

A7.3 The only serious question to be determined is whether the appropriate SI rate assumption is 2% (as suggested by James Hardie) or 4% (as suggested by Counsel Assisting).

A8 Choice between 2% and 4% SI rate

A8.1 Notwithstanding the assent by Messrs Whitehead, Minty and Marshall to a 4% SI figure, the most carefully reasoned and persuasive estimate of superimposed inflation for this particular class of claims is that of Mr Wilkinson: Ex 312. The submission of Counsel Assisting that "Mr Wilkinson's 2% SI figure was not one he defended with conviction" predated Mr Wilkinson's supplementary statement: Paragraphs 4 to 20 of that statement cogently defend his choice of a 2% SI rate, the rationale for which is also contained in Ex 252, pp 21-22.

A8.2 Counsel Assisting's submissions for a 4% SI figure were based on the fact that the class of claimants is closed and ageing, leading to a consequent countervailing tendency towards smaller claims. Mr Wilkinson made explicit allowance for the ageing effect and found it to be minimal. He supported this by specific reference to an analysis of the James Hardie population of claimants. Mr Wilkinson in fact found a negative SI effect which over a period of two decades averaged out to a 2% SI rate: Ex 312, [5]–[9].

A8.3 Both the MRCF and Counsel Assisting made reference to claim numbers and costs in support of a higher SI figure. Mr Wilkinson noted that although claims costs have risen, the trend will slow down, because these costs are a function of MRCF being joined as a co–defendant: Ex 312, [12]–[15]. This will slow down as the MRCF share of claims trends to 100%: Ex 312, [15]–[16]. Mr Wilkinson also assumed rising claim costs and claim numbers ("notifications") and this assumption was made explicit in his report: Ex 252, 9.2.1–9.2.3.

A8.4 In its submissions, Trowbridge stated that it regarded a low estimate of SI to be 0%, a high estimate of SI to be 4% and a "mid" estimate to be 2%. A rate of 4% is at the "top end" of the range of assumptions: Trowbridge, [106] and [98] (in reliance on Marshall, T3437.44-3438.4).

B. The February 2001 Report

B1 Overview

B1.1 Part B of Section 1 of Counsel Assisting's submissions addresses issues arising in relation to the preparation and use of the February 2001 Trowbridge report.

B1.2 The substantial question which arises upon those submissions is whether Shafron acted dishonestly in permitting the February 2001 Trowbridge report to be used by the incoming directors, the outgoing Coy and Jsekarb directors and the JHIL directors because he either knew that it was likely to be unreliable or was recklessly indifferent as to its accuracy and suitability. Counsel Assisting argues that Shafron was recklessly indifferent: CA, Section 1, [190]. The MRCF argues that he either knew that the Trowbridge estimates were likely not to be accurate or lacked concern about that: MRCF, 30.30, 30.35 and 38.10. The Unions assert that Shafron was fraudulent in knowingly permitting Trowbridge to rely on data which "he knew to be false" or which was "stale and false claims data": Unions 4.4, 4.29 to 4.30. (The submission that the claims data used by Trowbridge was stale is understood but should be rejected. The submission that it was false is unsustainable.)

B1.3 No submissions of fraud or dishonesty are made by Counsel Assisting or the MRCF against Macdonald, Morley or Attrill in relation to the use of the Trowbridge report: see, eg, CA, Section 1, [134], [135], [140], [191].

B1.4 The Unions assert deception on the part of Harman (para 4.28), deceit and the promotion of deceit on the part of Attrill (paras 4.40 and 4.42) and deliberately misleading conduct by Macdonald in his dealings with the JHIL Board: para 4.18. In relation to the briefing of Trowbridge, Morley is said to have engaged in conduct which demonstrated "a deliberate attempt to mislead": para 4.4. However, that submission is not elaborated upon at all and there is no attempt to substantiate or justify it either by argument or reference to evidence.

B2 The significant findings argued for by Counsel Assisting

B2.1 As the MRCF notes, several differing accounts were given of the circumstances in which Trowbridge was commissioned to prepare its revised report: MRCF, 30.12. Similarly, the positions taken by the parties before the Commission in relation to those matters are different.

B2.2 Counsel Assisting argues for the following findings in seeking to justify the conclusion that Shafron was reckless:

(a) that Minty was told by Shafron on 19 January that he did not think that there was anything in the current data that would affect the Trowbridge analysis because nothing significantly different from what had been projected had occurred in the relevant nine month period: CA, Section 1, [45] to [70], especially [57];

(b) that Shafron and Morley were not told by Minty or Marshall on 19 January that Trowbridge did not need the recent claims data because it was unlikely to make much difference: CA [49] to [69], [190];

(c) that as a result of his being present at the meeting on 19 January where Attrill records Minty as having said words to the effect that James Hardie's mesothelioma numbers had "levelled off recently", Shafron was either conscious of an inconsistency between James Hardie's current experience and the basis on which Trowbridge was proceeding or was indifferent to that difference and the accuracy of Trowbridge's report: CA [100] to [135], especially [133];

(d) that Shafron deliberately withheld the 2000 Trowbridge report from the incoming directors because he was concerned about the impact its contents might have upon them: CA [159] to [174], especially [173].

B2.3 The MRCF says that the finding in (a) should not be made because Minty's recollection is "unsupportable": MRCF, 30.25(e) and (f). It submits that the finding in (b) should be made: MRCF, 30.25. It would support the finding in (c): MRCF, 30.33 to 30.35. The MRCF only makes a general submission to the effect of (d) above: MRCF, 25.10, 38.30(b), 39.1, 44.5.

B2.4 Trowbridge argues for findings in terms of (a) and (b): Trowbridge paras 45(c) and (e); submits in relation to (c) that Shafron, Attrill and Morley knew the statement not to be accurate: Trowbridge paras 163 to 173; and makes no substantial submission upon (d): Trowbridge para 36.

B2.5 Each of the findings argued for is responded to below. In summary, James Hardie submits that findings should be made as follows:

(a) it was Shafron's preference for Trowbridge to proceed based on the March 2000 data. That much is common ground: CA [72]. However, he raised the question with Trowbridge as to whether more recent data was needed;

(b) Trowbridge's communicated position was that the updated data was not required because a couple of quarter's data was unlikely to make any difference. It was not required for a further reason, namely that the exercise which Trowbridge proposed to undertake involved a comparison of James Hardie *annual* data with the *annual* data derived from the Australian Mesothelioma Register;

(c) there was no attempt to withhold the relevant information from Trowbridge. It was aware that it did not have data after March 2000 and was aware of the nature of the deterioration in the December quarter which was communicated to Marshall and, as a strong likelihood, to Minty;

(d) Shafron, Attrill and Minty expected the results of the revised report to show an increase in the projected liability forecasts and believed that any recent

deterioration in the James Hardie experience was consistent with what would flow from a revision which took account of Watson and Hurst;

(e) it was Shafron's view that the more recent data (and specifically the December quarter claims figures) did not mean that the James Hardie exposure over time was going to be different.

B3 Minty was not told by Shafron that he did not think there was anything in the current data which was significantly different (Issue 5)

B3.1 A finding to this effect should be made for the following reasons.

B3.2 First, it is not Minty's best recollection that Shafron said anything to him to that effect. Minty's best recollection is that something to that effect was said to him by Attrill either on 16 January when Attrill made the note "can run with the data we have" (Minty T764.8) or at the meeting on 19 January: Minty T680.11, T681.32, T789.35, T810.15, T814.26.

B3.3 Secondly, Attrill's evidence is consistent with the issue as to the data to be used having been raised and dealt with on 16 January, as Attrill's note records. Attrill's note of 19 January does not record that Shafron made any statement to the effect suggested by Minty. See also MRCF, 30.25(b).

B3.4 Thirdly, the subsequent conduct of Minty and Marshall is not consistent with such a statement having been made and they having relied upon it. The suggestion in Minty's evidence is that he needed the up-to-date claims information because it may have been relevant to the exercise of revising the June 2000 report. However, Marshall, and most likely Minty, were advised of the effect of that information and did nothing in the way of pressing James Hardie for further details or in qualifying subsequent written or oral statements made to the incoming directors. Furthermore, Minty's statement on 13 February that the actuarial report was based on the "best information available" is consistent with a belief that post-March 2000 data was not statistically relevant to the exercise he had undertaken: Ex 189, vol 1, p 328; Robb T2854.46ff.

B3.5 Marshall was told about the recent deterioration in James Hardie's experience in a conversation with Attrill at some time between the middle of January and 8 February either in person or at a meeting: Marshall T852.25, T910.50. He agreed that it was highly likely that he would have communicated what he was told to Minty: T911.31ff. Attrill agreed that he had conversations to this effect with Marshall: Attrill T977.30, T1009.28, T1147.9ff. Specifically, Marshall was told that the December quarter was worse than previous quarters in terms of numbers of claims and payment amounts. Based on what he was told, he understood that the recent experience numbers were "higher" than the numbers calibrated in the revised model: Marshall T866.50-T867.14. James Hardie's actual experience of $16.3 million for the six months ended 31 October accorded with what he was told and understood was the recent experience: Marshall T890.52-T891.14. (The

Trowbridge submission that the information provided was not inconsistent with the experience having "levelled off" recently should be rejected: Trowbridge paras 169, 170.) Neither Minty nor Marshall said anything about that knowledge either during the presentation on 13 February or in the Trowbridge letter of that date.

B4 Shafron and Morley were told by Minty or Marshall that they did not need the current data because it would not make any difference (Issue 5)

B4.1 Shafron and Morley gave evidence of a conversation to this effect: see JH 7.3.6, 7.3.9.

B4.2 The conduct of Trowbridge described above is consistent with Minty and Marshall having had and expressed a view that the recent experience was not likely to have any impact or effect on its analysis and that any increase in claims cost would be accounted for in the revised model. There are four other respects in which the evidence indicates that this is likely to be what occurred.

B4.3 The first is that a statement by Minty to the effect that two or three quarters' data would not make much difference was in accord with his view at that time. And Minty agreed that it was a view he expressed at the meeting on 19 January: Minty T806.40.

B4.4 The second is the terms of Trowbridge's second letter to the MRCF on 29 August 2001: Ex 3, vol 3, tab 5. In that letter Trowbridge was asked to estimate what the results of its analysis would have been if it had been provided with the nine months' additional data in January 2001. Trowbridge concluded that the June quarter and September quarter information would probably not have caused it to make any significant change to its analysis because of its earlier experiences of "surges and falls in reporting". As to the December quarter information, it said that the information "may have caused us to question" whether the annual numbers had peaked. That is certainly not an unequivocal conclusion. At the time of that analysis Trowbridge also had the March and June 2001 quarter reports which were described by it as "confirming again what appeared to be emerging by December".

B4.5 The third is Shafron's contemporaneous state of mind as recorded in Robb's note of his conversation with Shafron and Macdonald on 15 February: Ex 187, para 56, tab 17, p 65. That note records:

> Most recent numbers not given.
>
> Karl said recent numbers not needed.

Statements to the same effect were made by Shafron at the JHIL Board meeting on 15 February: JH paras 12.2.6 and 12.2.7; cf. Trowbridge paras 47 to 56.

B4.6 The fourth is that Trowbridge did not in fact require the data (or use it) in updating its June 2000 report. The methodology adopted by Trowbridge was as follows:

(a) Trowbridge formed the view that it was appropriate to assume that James Hardie's mesothelioma event projections would be based on Berry Medium (as the best estimate) and Berry High (as the high estimate);

(b) Trowbridge also formed the view that James Hardie's projections should reflect national incidence;

(c) the most reliable source of national mesothelioma numbers was the Australian Mesothelioma Register, which provided annual numbers, but accurate numbers were only available after around three years;

(d) it was not possible, therefore, for Trowbridge simply to take the most recent twelve months' data from James Hardie and find what proportion of the national incidence it represented;

(e) instead, since the most recent reliable national data was 431 incidents in 1996, Trowbridge projected that number forward to 1999 for each of Berry Medium and Berry High (obtaining 454.3 and 473.28 respectively);

(f) Trowbridge then found what proportion the 89 events in the March 2000 data bore to each of 454.3 and 473.28 (obtaining 19.6% and 18.8% respectively);

(g) Trowbridge then projected James Hardie mesothelioma event numbers on the assumptions that they would be a steady 19.6% of the Berry Medium national projections, and a steady 18.8% of the Berry High national projections.

B4.7 The James Hardie submissions (JH 13.1.7 to 13.1.56) identify a number of serious flaws in the assumptions involved in the methodology set out above. But for present purposes, they may be put to one side.

B4.8 There were two critical consequences of the methodology adopted by Trowbridge:

(a) it could be done relatively quickly (and in fact it was done by the morning of 2 February 2001); and

(b) the starting point was the annual data from the Australian Mesothelioma Register, which had to be projected forwards in time and then compared with annual James Hardie data to derive a percentage (19.6% and 18.8%).

B4.9 Trowbridge already had (from the work done by Messrs Watson and Hurst) the annual Berry Medium and Berry High national projections, based on the 1996 figure of 431. (These are the rightmost two columns on Schedule B.) See footnotes 20, 21, 24 and 25 of Ex 257 (Minty 4 June 2004) and see T3276.3-10:

> Q. And if we focus, just by the way, at 1996, you'll see that the number that both of those curves is 431.00. That's not a coincidence, that's because each curve has been calibrated to 431, that being the number of mesothelioma events for that year that was available from the Australian mesothelioma register?

A. I think it was some – estimated by Watson and Hurst on the basis of the meso register, that's correct.

B4.10 In order to compare like with like, on the approach taken by Trowbridge it was necessary to obtain comparable James Hardie annual data. Critically, because the comparison was with an *annual* projected national number, additional months' data from James Hardie short of a year would not be applicable. For that reason, it is inherently plausible that Trowbridge indicated that only annual data, not monthly data, was required.

B5 Significance of no response to Minty statement "meso numbers have levelled off recently" on 19 January 2001 (Issues 5 & 8)

B5.1 It is suggested by Counsel Assisting that the absence of any response to a statement apparently made by Minty in the meeting on 19 January when such a response was called for is evidence of dishonesty or recklessness on the part of Shafron: CA, Section 1, [133].

B5.2 Attrill's note of the meeting records "JH meso numbers have levelled off recently". Attrill agreed that the note reflected something said by Minty: Attrill T1024.15, T1136.12. He understood the statement as a reference to the James Hardie experience in the period up to March 2000: Attrill T1136.40. And that was the sense in which Minty believes he made the statement. Recently meant "recent years" being the three years up to March 2000: Minty T773.35ff, esp T774.1. Accordingly, the maker of the statement and the person who took the note understood the statement to be a statement of James Hardie's claims experience in the period to March 2000. As a statement of Minty's opinion based upon data he had received and analysed it was from the perspective of those present an accurate statement of the position.

B5.3 The statement was not made or understood as a statement describing James Hardie's experience in the three quarters since March 2000: cf. the formulation of the question in Issue 8(a) and Trowbridge para 173. It did not call for comment on the basis that it was not a correct statement.

B5.4 If any question arose as a result of the making of that statement, it was whether the recent experiences reflected in information available to James Hardie were relevant to the task Trowbridge was undertaking in the sense that they were likely to have an impact on it: see also Attrill, Ex 56, [18]. If, as it is submitted was the position, Trowbridge had indicated that it could do the exercise on the existing data and that six to nine months' data was unlikely to make any difference, the comment attributed to Minty did not require any response. This was more so if Shafron and Attrill, rightly or wrongly, did not believe there had been such a deterioration in the James Hardie experience as would affect the long-term trends.

B5.5 When considering what inferences should be drawn, Counsel Assisting's submissions draw a distinction between the positions of each of Shafron, Attrill and Morley in not responding

to the statement and only identify Shafron as the person who should have responded notwithstanding that the person with the greatest knowledge of the subject was Attrill.

B5.6 Attrill did not think to raise the question of the recent data with Minty at that time because the methodology being used to produce the revised report had been agreed upon at the earlier meeting on 16 January: Attrill T1024.51.

B5.7 The suggestion that Attrill did not turn his mind to the significance of the data or speak out because he "deferred to Shafron" should be rejected: cf. CA, Section 1, [135]. Attrill was not told by Shafron that he could not talk about that subject and never had the impression that Shafron was seeking to keep information from Trowbridge which was material: Attrill T1147.30ff. Secondly, if Attrill had thought that Trowbridge or the incoming directors were being duped it is likely that he would have raised it with Shafron: Attrill T1150.41. The evidence does not suggest that he did so. There was no reason for him to withhold information in circumstances where his future was likely to be with the incoming directors and the MRCF. His interest was in seeing that the actuarial exercise being undertaken was meaningful: Attrill T1150.25. Thirdly, he did raise the subject of the deterioration in experience with Marshall at some stage between 19 January and 8 February: Marshall T910.50. He also knew that the same information had been provided to Cooper in the form of the Operating Plan Review and to the incoming directors during the presentation on 15 January. The fact of James Hardie's most recent experience was certainly not a secret and there was no reason for Attrill not to raise it if he thought it was an appropriate response to what had been said.

B5.8 Whilst Attrill agreed "with the benefit of hindsight" that he should have said something at this meeting (Attrill T1222.40), he maintained that at the time of the meeting what was said by Minty as recorded in the note did not "trigger" in him an understanding that Minty was speaking about contemporary claims figures as distinct from the period before March.

B5.9 Shafron had no recollection of what his reaction was to the Minty statement as recorded in Attrill's notes. His explanation for not referring to the more recent experience was that it was "not in his mind at the time": Shafron T1747.55. At the time Shafron did not believe there was any serious deterioration in the claims experience happening: Shafron T1745.25. Shafron's understanding of the position in relation to the third quarter results is reflected in the draft Board paper reporting those results which he received from Attrill on 1 February 2001: Ex 56, vol 4, p 976.

B5.10 That Board paper records that December was a bad month although the number of new product and public liability claims received was in line with the previous twelve months quarterly average. The analysis of that report by Counsel Assisting (CA, Section 1, [129]) does not take account of Trowbridge's subsequent detailed analysis of the information for the first three quarters of 2000 which was undertaken in August 2001: Ex 3, vol 3, tab 9. That analysis concluded that the experience for the first two quarters would not have and

the experience for the December quarter "may have" caused Trowbridge to "question" whether the annual numbers had peaked.

B5.11 It should be concluded that the February Board paper reflected the understanding of Shafron and Attrill in February 2001 which was that there was not a serious deterioration in the claims experience happening and that this was a reasonable view for them to hold. That understanding is consistent with their evidence. It was not "obvious", even to Trowbridge, that the nine months' data indicated or suggested that James Hardie's experience had not yet peaked: cf. CA, Section 1, [103] and [104].

B5.12 The same point may be made with greater emphasis by reference to the Operating Plan Review (OPR) and discussion on 13 December 2000. Counsel Assisting submit that the document and discussion suggest that Shafron, Morley and Attrill knew or ought to have known that the Trowbridge exercise ran the risk of being seriously flawed because it did not have data after March 2000: CA, Section 1, [106] to [113]. The OPR contained figures for a period of six months. Trowbridge's 2001 analysis of that data, presumably put into a form which was satisfactory to Trowbridge, was that it probably would not have caused it to make any significant change to the model or projections because the numbers reflected the expected "surges and falls in reporting": Ex 3, vol 3, tab 5.

B5.13 There is no doubt that in varying degrees Attrill and Shafron were aware that there had been a deterioration in the experience after March 2000. The fact of such a deterioration was advised to Marshall of Trowbridge (in a way which suggested a $16.3 million half-year result and claim numbers above those calibrated in the revised model). As has been submitted above, the real question is whether Attrill and Shafron understood the fact of that deterioration to be statistically relevant or to be likely to have an impact upon the Trowbridge analysis. In the light of what Minty had said and in the light of their views (which coincided with those of Minty) they were entitled to proceed on the basis that it was not relevant or likely to have an impact on forecasts for periods up to fifty years.

B6 The 2000 Trowbridge report was not withheld because of a concern about the impact its contents might have (Issue 10)

B6.1 Counsel Assisting submits that it should be found that Shafron deliberately withheld this report from the incoming directors because he was concerned about the impact its contents might have on them and that the suggestion that he was concerned to keep the report privileged was "merely a pretext" and an afterthought: see esp CA, Section 1, [162], [164], [166], [173].

B6.2 Shafron's decision not to provide the incoming directors with a copy of the draft 2000 Trowbridge report was made for two reasons. The first was that he was concerned not to lose any claim to privilege in respect of the document and to maintain its confidentiality. The second was that it did not represent Trowbridge's most recent thinking because it did

not take account of Watson and Hurst and was to be superseded by the February 2001 report: Shafron T1595.55; T1600.44.

B6.3 The relevant sequence of events was as follows:

(a) at the time of the meeting with the incoming directors on 15 January Gill asked that the current draft of the Trowbridge report be circulated "tomorrow". Those directors also asked to meet Trowbridge and wanted an update of the Trowbridge projections: Shafron T1593.23. In response, tentative arrangements were made for the incoming directors to attend a meeting on the following Tuesday, 23 January. Robb's note records that Edwards asked for the 2000 Trowbridge report and a meeting with Trowbridge: Ex 187, para 44, tab 15, p 59;

(b) on 16 January Attrill telephoned Minty and discussed the Watson and Hurst analysis. In that discussion, Minty said that the impact of the revised model "may be another ten claims" per year and for a longer period so that it could add several hundred more claims. He said the likely revision would be in the order of 20%. There was also discussion about a meeting on 23 January. During that discussion Attrill made his note "can run with the data we have";

(c) as at 16 January Trowbridge were to undertake the revised exercise in relation to the June 2000 report using the data they had. It was proposed that there be a meeting with the incoming directors and Trowbridge at which Trowbridge would discuss the effect of Watson and Hurst upon the June 2000 report: Ex 56, vol 4, p 956. Attrill confirmed this in an email to Shafron on 16 January: Ex 56, vol 4, p 957;

(d) at midday on 17 January Shafron telephoned Attrill saying that the JHIL Board intended to proceed with the restructuring but wanted to slow the pace. He said that there was no need for Minty to carry out a further review "now" and that Tuesday's briefing by Trowbridge would likely be cancelled: Ex 56, vol 4, p 958. Attrill said that "now" meant "at the moment": Attrill T1149.12. Later on the same day Attrill telephoned Minty and advised him to the same effect: Ex 56, vol 4, p 959;

(e) at this time Shafron prepared a note as to how to "go forward". In its typewritten form it said:

> Minty to review with independent directors current Trowbridge report of future costs.

Following a discussion with Shafron, probably on 18 January, Attrill amended the note to read:

> Minty to review with independent directors current Trowbridge *thinking on* future costs.

(Ex 56, vol 4, p 961);

(f) at some stage on 17 or 18 January Shafron decided to refine the request to Trowbridge so as to provide for the preparation of a report addressing scenarios "for 10-15 years" to be presented at a meeting with the incoming directors on 13 February. Shafron's expectation at the time was that the likely outcome of the Trowbridge revision could be a net present value of claims "as high as $350 million": Ex 56, vol 4, p 960. That represented a significant increase over what he understood the March 2000 projection to be after taking the QBE receivable into account: Shafron T1599.13;

(g) on 18 January Shafron asked Attrill to arrange a meeting (that afternoon): Ex 56, vol 4, p 960. That meeting occurred on the following morning, 19 January. Attrill's note records that the revised assessment was to be in the form of a report which, whilst updating the current report, was to be more focused on the concerns of the incoming directors.

B6.4 The 2000 report was treated as confidential and privileged within James Hardie to the extent that neither Morley nor Macdonald or any other member of the JHIL Board had seen the report: Macdonald T2584.5ff; Morley T2159.23ff. Its circulation was restricted to those within the legal department (including Attrill) and Shafron. Until about 17 January 2001 the position was that Trowbridge was to make a presentation to the incoming directors of its revised report or numbers on 23 January. The evidence does not indicate whether the 2000 report would have been provided or made available during that presentation.

B6.5 It is <u>not</u> correct to say that the issue of privilege was not raised on 16 or 17 January as a reason for not providing the 2000 report or that it was not raised until after the MRCF had been established: cf. CA, Section 1, [64] to [167]. An Allens file note (Quinlan) of 17 January indicates that on that date an inquiry was made of Robb as to whether the report would remain privileged in the hands of the incoming directors: Ex 189, vol 1, p 142. That note records:

> Trowbridge report
>
> – potential directors of trustee coy want to see Trowbridge report.
>
> - JHIL Board never properly considered or received it.
>
> - Could such a report be prepared under privilege so JH and prospective directors could review it?

The existence of that file note makes it most unlikely that Shafron's 18 January note (Ex 57, vol 4, p 961) did not reflect his thinking at the time: cf. CA, [162].

B6.6 The slowing of the pace on 17 January enabled Trowbridge to prepare a separate report for the incoming directors which addressed the position in the light of Watson and Hurst. That was probably the reason for the amendment which Attrill made to Shafron's "go

forward" note. At the meeting on 19 January there was reference to a separate retainer letter from Allens: Ex 56, vol 4, p 971. The evidence does not suggest that at any time after 15 January there was any complaint by any of the incoming directors that they were not provided with the 2000 report. That is because at some stage on or after 18 January Edwards and the other incoming directors were told that Trowbridge was preparing a revised report for a presentation to them on 13 February. That report was referred to in the fax from Macdonald to Edwards of 27 January 2001: Ex 150, p 97; and on 5 February Gill contacted Attrill and discussed what the "directors and trustees" expected to see in it: Ex 150, p 112.

B6.7 The suggestion that privilege and incompleteness of the Trowbridge report were "merely pretexts" for not providing the report to the incoming directors and that the real reason it was withheld was that it would disclose uncertainty, sensitivity analyses and the extent of liabilities beyond twenty years also does not sit comfortably with what was proposed and what occurred in relation to Trowbridge.

B6.8 Looking forward from mid-January 2001 Shafron did not know what any report which Trowbridge produced might contain (other than it was to be kept brief). The report which eventually emerged made it clear that mesothelioma claims would extend until 2040 and that non-mesothelioma claims would continue until at least 2034, that there was an "inherent uncertainty" in the projections, that one possible outcome was the "high basis" projections, that the projections were heavily influenced by legal decisions that were impossible to predict and that the estimates were based on a continuation of the current environment regarding legal principles and settlement practices: Ex 3, vol 3, tab 3.

B6.9 Furthermore, it was proposed that the incoming directors receive a presentation from Minty and Marshall and that they be able to ask whatever questions they chose concerning James Hardie's asbestos liabilities and the Trowbridge report. That occurred. During the discussion Gill asked questions about the scope of the exclusions from the report and Minty spoke about the projections. Attrill's note refers to him saying there were "big questions about the underlying number of claims": Ex 56 at p 1058. Robb's notes record Minty saying that "cashflows over the next ten and fifteen years are reasonably predictable". There is no suggestion that any of Minty or the incoming directors were constrained from asking questions which addressed matters of qualification contained in the 2000 Trowbridge report. The likelihood is that the incoming directors appreciated that the projections involved uncertainty and that they were not interested in further detail. That is almost conceded in the submission that it cannot be said with any confidence what impact the 2000 report would have had on the incoming directors had they seen it: CA, [174].

B6.10 By way of summary, it should be found that Shafron did not provide the draft 2000 Trowbridge report to the incoming directors because he took the view it was unnecessary

to do so after the decision had been made to have Trowbridge prepare a revised report which it would present to those incoming directors. It should not be found that Shafron did not provide the report because of a concern about the impact its contents might have.

B7 Shafron's preference for Trowbridge to proceed based on the March 2000 data was explained by concerns about delay (Issue 5)

B7.1 Counsel Assisting argues:

(a) that Shafron's evidence that it was his preference for Trowbridge to proceed based on the March 2000 data because of concerns about delay may not be plausible;

(b) that if that evidence is not accepted, the available inferences are that the data was not provided because Shafron perceived that it might be unhelpful (by producing a higher assessment) or, because, although he was concerned about delay, he was indifferent as to the accuracy of the report: CA, Section 1, [72] to [80], esp [80].

B7.2 The current data was not "withheld" from Trowbridge: cf CA para 72. Minty agreed that Shafron asked him whether data after March 2000 was required: Minty T806.6; and the fact that there had been a deterioration in claims numbers and amounts particularly in the December quarter was communicated by Attrill to Marshall in the period from mid-January to early February 2001.

B7.3 Shafron's evidence was that his preference was that the data not have to be provided because of time constraints: Shafron T1419.37, T1710.10. That evidence accords with Attrill's recollection of Shafron's position at the time: Ex 57, [105] and Attrill T1133.53ff. The sequence of events described above demonstrates that there were time constraints put upon the Trowbridge exercise. When the first approach was made to Trowbridge it was expected that the revised analysis would be presented to the incoming directors within a week.

B7.4 The evidence relied upon by Counsel Assisting as casting doubt upon the veracity of Shafron's evidence that he was motivated by concerns of delay is the terms of Shafron's memorandum to Macdonald of 9 November 2001: Ex 85, p 3. It is said that this letter does not expressly state a concern about delay: CA, [78]. That may be so. However, it is implicit in the statement that the data used represented the most up-to-date "claim" numbers, that to use numbers after March 2000 would have involved delay in order to put them into a form in which they could be reliably used and verified by the actuary: see JH paras 7.3.22, 7.3.23. That is what happened in March and April 2000: Ex 57, vol 1, pp 101-2.

B7.5 It is also suggested by Counsel Assisting ([79]) that the absence of any inquiry by Shafron as to whether Trowbridge could make use of the data in the time available is consistent with his not having a genuine interest in obtaining the best estimate from Trowbridge. In the circumstances, such an inquiry was not called for. Trowbridge and James Hardie had

a relationship which commenced in mid-1996. It was obvious that James Hardie had further information available even it was not in a form which could be used immediately. A report by Attrill to Shafron that Minty was happy to undertake the task without that data made it unnecessary for Shafron to ask whether Trowbridge could use it.

B8 Shafron was not indifferent to the accuracy of the Trowbridge report

B8.1 Shafron was entitled in these circumstances to allow Trowbridge to prepare the revised report on the March 2000 data. He believed based upon what had been said that two or three quarters' data was not going to make any difference and that any deterioration in claims experience in the most recent data would be accounted for in the Watson and Hurst revision. That those were reasonable views to hold in the circumstances is supported by the fact that they were views held by Minty and Attrill.

B8.2 It was Minty's view in January 2001 that six to nine months' data was unlikely to make any difference (Minty T806.40) and that any adjustments made to take account of the Watson and Hurst study would reflect any deterioration in the James Hardie experience after March 2000: Minty T799.56. The conduct of Marshall in the face of the knowledge acquired as to the December quarter experience is only explicable upon the basis that the same views were held by him. Attrill's view was that the updated 2001 Trowbridge report would be accurate despite the lack of more recent data because the Watson and Hurst study involved significant increases: Attrill T1064.13.

B8.3 If Shafron was indifferent to the accuracy of the Trowbridge report (cf. CA, Section 1, [80]) it is most unlikely that he would have permitted a sequence of events which involved Trowbridge preparing a report and making a presentation to the incoming directors during which those incoming directors could ask whatever questions they wanted of Trowbridge concerning the report and the information upon which it was based. The likelihood was that if there was any question about the accuracy of the report it would become apparent during that presentation with the consequence that the incoming directors would withdraw and the transaction would not proceed. No sensible reason is given for why Shafron would have been indifferent to that outcome.

B8.4 Shafron was also aware that the incoming directors had been provided (via Cooper) with the OPR and a presentation on 15 January which referred to the most recent data. It is possible that he was also aware that Trowbridge via Marshall had been told of the December quarter results. Each of these matters would have made it more likely that any question about the suitability or reliability of the Trowbridge report for the purposes of the incoming directors would have become apparent in the Trowbridge presentation on 13 February.

B9 Trowbridge was not "positively misled"

B9.1 The submission (CA [139], [140]) that Trowbridge was "positively misled" by James Hardie as to the quality of its current experience should be rejected. It appears to be common ground that Marshall was told that there had been a deterioration in James Hardie's claims experience since March 2000: CA [137], [138]. As is pointed out above, Marshall understood from what he was told that the actual experience was "higher" than the numbers calibrated in the revised model and what he was told accorded with an actual experience of $16.3 million for the six months ended 31 October. That evidence cannot be put to one side: cf. CA [139]. Marshall's evidence was that this information was provided before 8 February and that it was highly likely that he communicated it to Minty.

B10 No inference adverse to Shafron should be drawn from the selection of a period of twenty years for projections for the incoming directors

B10.1 Shafron was asked why he requested Trowbridge to do a report limited to twenty years. His answer was because that was what the incoming directors had sought: JH, 9.6; CA, [144]. What Shafron wanted was something which answered the description of what the incoming directors had sought. It is not an accurate summary of the position to say that Shafron wanted evidence that they were not concerned about the period after twenty years: cf. CA [145].

B10.2 Two further things should be kept in mind. First, there is no suggestion in any of the contemporaneous evidence of a complaint by the incoming directors that they had not received information which they had sought. Second, the Trowbridge report did indicate what the position was in relation to mesothelioma and non-mesothelioma claims after the twenty years and there were no restrictions upon questions which could be addressed to Minty concerning the period beyond twenty years. The fact that no questions appear to have been addressed to that subject confirms the interest of the incoming directors in the shorter period.

B11 The February report and the Trowbridge work were believed by Shafron and Macdonald to be suitable for the purpose(s) proposed (Issues 12 and 13)

B11.1 It is accepted, looking at the matter with the benefit of hindsight, that the Trowbridge February report was not suitable for the purpose of estimating the amount of money which would have to be set aside to cover with a high degree of confidence the liabilities of Amaca and Amaba. However, that was not the purpose for which the incoming directors or the JHIL directors required or used that report.

B11.2 The incoming directors sought to be satisfied as to whether the Foundation could meet the "most likely" Trowbridge forecast of asbestos claims for the next fifteen to twenty years. Each of them approached that subject upon the basis that there was a prospect that it would be unable to do so: see JH, 9.6. Their position is reflected in the briefing note

prepared by Mallesons following a meeting on 6 August 2001 and the statement made by Cooper at his meeting with Ashe on 7 August 2001: see JH, 9.6.8(d) and (e). It was their collective view that the funding would last fifteen to twenty years and that, for the purpose of doing that exercise, an earnings rate of 8.7% was more realistic than a rate of 11.7%. (Jollie had also been given an analysis using an earnings rate of 7%: JH, 8.1.8.)

B11.3 The JHIL directors were provided with a cashflow analysis using the Trowbridge "most likely" projections for the purpose of assessing whether the Foundation would have sufficient funds to allow it to meet those projections: JH, 5.3.48.

B11.4 There are six respects in which it is submitted by Counsel Assisting that the February report was not suitable to be used for the purpose of assessing the "likely longevity of the MRCF" and whether the companies "would have adequate funds to pay all legitimate claims": see CA, Section 1, [180].

B11.5 Looking at the matter from the perspective of the incoming directors, three of those matters were known to or appreciated by them. They knew the February report excluded from consideration significant areas of risk, that it assumed static medical and legal environments and that it omitted data after twenty years. The fact that the "most likely estimate" was only a statistical median outcome was not appreciated by the incoming directors or Macdonald, Morley, Cameron or Shafron: CA, Section 1, [176]. The fact that it was subject to assumptions, limitations and sensitivities was obvious when one has regard to Minty's presentation on 13 February and to the terms of the draft Trowbridge letter of 13 February. The sixth matter is that the report was prepared by reference to "out of date data which was not reflective of recent experience". The fact that the nine months' data was (or was likely to be) statistically relevant was not appreciated by the incoming directors or by Macdonald, Morley, Shafron or Attrill. Indeed, it does not appear to have been appreciated by Minty and Marshall.

B11.6 It is not submitted by Counsel Assisting that Macdonald acted dishonestly in relation to the use of the Trowbridge figures: CA, Section 1, [191].

B11.7 The submission that Shafron acted dishonestly does not draw any distinction between the different uses to which the report or Trowbridge information was to be put. The substance of the submission is that Shafron was indifferent to whether it was suitable for use because he knew it was prepared by reference to out of date data which did not reflect James Hardie's recent experience.

B11.8 For the reasons stated above it should be found that Shafron was not indifferent to the accuracy of the Trowbridge report, that he did not believe it had been prepared by reference to out of date data and that he did not believe that James Hardie's recent experience was statistically relevant to the exercise Trowbridge had undertaken.

B11.9 Shafron's conduct in arranging for the February report and for the opportunity for the incoming directors freely to ask questions of Minty is not the conduct of someone who was indifferent as to whether it was suitable to be relied upon. Most of the respects in which it is said that the report was unsuitable were known to the incoming directors and Minty and Marshall and not the subject of any qualification or adverse remark.

B11.10 There are two additional considerations which make it unlikely that Shafron was recklessly indifferent to the suitability of the report. The first is that the Trowbridge projections were to be relied upon by the JHIL Board. No reason is given for why Shafron would consciously or recklessly permit the JHIL Board to proceed on material which was or could be unreliable and which was likely to be shown to be such at some time in the future.

B11.11 The second is that Marshall, and more likely than not Minty, appreciated the matters which it is said justify a conclusion that Shafron was recklessly indifferent. They knew that their report was based upon James Hardie data up to 31 March 2000. Marshall knew and it is highly likely that Minty knew that the more recent experience indicated claims higher than the numbers calibrated in the revised model and consistent with a figure of $16.3 million for the first six months to 31 October 2000. Each appreciated something which Shafron did not appreciate (CA para 176(iv)), namely that the "best estimate" represented a median outcome as distinct from Trowbridge's view as to the most likely result. Neither made any comment to the effect that the report was not suitable to be relied upon.

B11.12 Minty and Marshall knew that their report was being used as the basis for calculating or justifying the funding of the MRCF: Minty T754.55. Robb's note of the meeting records the way in which the actuarial assessment was being put and relied upon. They record (Ex 187, tab 16, p 62):

> D Minty – background – started review '96
>
> - Last review as at March 2000
>
> - Future is not clear
>
> - Dependent on medical/nature of claims/Court decisions
>
> - That said, there is a claims history
>
> - Future cashflows analysis
>
> - Cashflows over the next 10 + 15 years are reasonably predictable
>
> - Based on experience + evidence, ie. based on best info available, this is Trowbridge view.
>
> …
>
> Are we getting better at working at the peak and knowing when?
>
> D Minty + better info on latency periods

+ Not clear who + how many Aust were exposed.

The reliability of the actuarial material was then explored further in the exchanges between Minty and Gill: see JH para 9.5.5 which records Attrill's notes (Ex 56, vol 4, p 1058). Those notes conclude with comments by Jollie and Gill as noted:

PJ: We intend to rely on this.

MG: DM to send a copy to the incoming directors thru' Tony Bancroft

B12 Allegations of fraudulent and negligent misrepresentation and misleading conduct on the part of JHIL by Shafron (Issues 14 and 15)

B12.1 The MRCF contends that there was misleading and deceptive conduct on the part of Shafron (and JHIL) in relation to the February report and the meeting on 13 February: MRCF, 38.7, 38.8, 38.28 to 38.31. Counsel Assisting argues that there was a representation by Shafron (and JHIL) to the incoming directors and the outgoing Coy and Jsekarb directors that the February report and data contained in it were "suitable for the purpose of assessing the appropriateness of the consideration offered to Coy and Jsekarb in the DOCI and the likely period of solvency of those companies if separation occurred": CA, Section 1, [213]. It is said that the representation was fraudulent because of Shafron's reckless indifference and alternatively that it was negligent and constituted misleading conduct: CA, [216], [234], [246].

B12.2 The representations alleged are not expressed in terms of opinion or belief but rather as a warranty as to the position. It is submitted that no express or implied representations were made in the terms suggested. If there was any misrepresentation or misleading conduct in relation to the Trowbridge report, it is likely to have been with respect to a need to state clearly that the Trowbridge exercise had been conducted on information which did not extend beyond March 2000. If there was any misrepresentation or misleading conduct with respect to that subject, it was not dishonest or reckless on the part of Shafron.

B13 Possible remedies (Issues 14 and 15)

B13.1 Counsel Assisting argues that there was misrepresentation and misleading conduct in relation to the incoming directors of the MRCF and the outgoing directors of Coy and Jsekarb. The MRCF submits that there was misleading conduct in relation to the incoming directors.

B13.2 As to the incoming directors: Counsel Assisting does not suggest that there might be any significant remedy available to the incoming directors upon the basis that they were misled: CA, [225]. The MRCF does not in its analysis identify any significant remedy available to those directors or the MRCF. It is argued that if the asserted misleading conduct had not occurred, the incoming directors would not have agreed that the transaction go ahead in the form in which it did: MRCF, 39.43 to 39.45. In that event, the submissions do not go on to consider the likelihood of the transaction not going ahead at all or going ahead in some

different form and they do not attempt any damages analysis on either of those hypotheses.

B13.3 Assuming that the February report was "unsuitable" for the purposes of the incoming directors and that they appreciated that, the likelihood is that the separation transaction would not have proceeded because they would have asked for something which answered the description of a "suitable" report and either that would not have been given in the time available or, if given, would have contained an estimate of the net present value of the future liabilities well in excess of $293 million. The latter does not appear to be controversial: CA, Section 1, [219].

B13.4 In either of those eventualities the likelihood is that the transaction involving the transfer of Amaca and Amaba to the MRCF would not have proceeded because JHNV and JHIL either could not have funded, or would not have been prepared to fund, the shortfall and the JHIL Board would not have proceeded in the absence of that funding: JH, 12.6. The opportunity of Coy and Jsekarb to negotiate for an amount above that to be provided under the DOCI was not of significant value because of the inability or low likelihood of JHIL/JHNV raising or putting up sufficient funds.

B13.5 In the event that the transaction did not proceed, Coy and Jsekarb would have remained subsidiaries of JHIL and the DOCI would not have been executed. Subject to any defences available to JHIL, those companies could have pursued any causes of action which they had against JHIL or any of its directors in respect of management fees and dividends. The existence of those causes of action is contested: see JH, 3.2 and 3.3.

B13.6 As to the outgoing directors of Coy and Jsekarb: Counsel Assisting argues that they would have had the opportunity to seek to negotiate for a much higher level of funding from JHIL in return for a release in relation to claims concerning management fees and dividends, the provision of funds to take account of JHIL's potential asbestos liabilities and the value of the separation to JHIL: CA, [220] to [222].

B13.7 Any assessment of the value of that opportunity also would have to take into account the ability and preparedness of JHNV and JHIL to fund Coy and Jsekarb. The probability is that they would not have provided or been able to provide significant funds. McGregor suggested that it was unlikely an amount in excess of $60 million could or would have been agreed to: JH, 12.6.6.

B14 Issues 16 and 17 - Counsel Assisting

B14.1 In relation to Issue 16, James Hardie is in agreement with the submissions of Counsel Assisting at CA, Section 1, [251] - [255] as to the deficiencies in Trowbridge's determination of Berry medium as an appropriate curve and 25% as the percentage of nil claims.

B14.2 The inappropriate selection of 25% for nil claims led to a small, but still significant, understatement of the value of asbestos liabilities (responsible for $35.3 million of the $371.6 million difference, or slightly under 10%: Wilkinson, Ex 252, Table E.4). Moreover, this error (like the $67 million error in the undiscounted liabilities (Wilkinson, Ex 252 pp 67-68)) is confirmatory of the less than professional approach that was adopted by Trowbridge.

B14.3 James Hardie says further that the choice of zero superimposed inflation was inappropriate: this is not an actuarial issue but a question of fact as to the instructions that were given. It is common ground that, subject to Trowbridge receiving instructions to the contrary, *some* allowance for superimposed inflation was necessary. For the reasons given by Mr Wilkinson, including in Ex 312, that rate should have been 2%: see paragraph A8.1 above.

B14.4 In relation to Issue 17, JHINV and ABN 60 are also in agreement with CA, Section 1, [256] – [259] that the February 2001 report should have stated expressly that the data had not been updated, rather than stating that it was "based on all the information available".

B15 Issue 16 - Trowbridge

B15.1 Trowbridge [189]-[264] attempts to defend the February 2001 report, and in particular the assumptions made by Trowbridge as to:

(a) the peak and duration of mesothelioma claims;

(b) the rate of superimposed inflation; and

(c) the rate of future "nil" settlements.

The first of these is addressed below. The second is not an actuarial question (see above), and the third has been addressed in chief at JH 13.1.51-56 and above.

B15.2 Understandably, Trowbridge seeks to highlight the uncertainties inherent in predicting the future, and the range of views which different actuaries can reasonably hold. Much of this may be acknowledged.

B15.3 However, on any view, the most relevant information for determining the peak and duration of James Hardies' future mesothelioma experience must be James Hardies' past mesothelioma experience. That past experience demonstrated:

(a) a steady increase in mesothelioma *events* in the last decade;

(b) a possible plateauing in mesothelioma *claims* in the previous three years.

B15.4 The primary data was the number of events, not the number of claims. That is clear because:

(a) claim numbers could include multiple *Compensation to Relatives Act* claims arising from a single mesothelioma event;

(b) Trowbridge itself merely assumed in its projections that the number of claims would be the number of events multiplied by 1.15: T3280.4-15; and

(c) the actual recalibration undertaken by Trowbridge was based on *events*, not claims. This was necessary, because the national data from which the James Hardie projection was derived (see submissions in chief 13.1.34) was of course based on events.

B15.5 It follows that the reliance on any apparent plateau in claims was misplaced. What had to be addressed was the steady increase in mesothelioma events which had been observed in James Hardie, throughout Australia, and in Europe. That was a major challenge in the cross-examination of Messrs Minty and Marshall to which no answer has been identified in the submissions.

B15.6 True it is that each of the "best estimate" and "high" bases in the February 2001 report projected higher claim numbers for the next few years: cf Trowbridge [198], but those increases were extremely modest. In the case of the "best estimate", the increase in events was from 89 in 1999, to 89.86 in 2000, 90.39 in 2001 and a peak of 90.59 in 2002. That is to say, an increase of no more than 2 events over a three year period, when the number of events had risen by 11 in the previous year, 5 in the year before that, and 10 in the year before that. See Schedule B, column 8 to Mr Minty's statement Ex 257.

B15.7 An attack is made upon Mr Wilkinson's reasoning to the extent it was based on the Watson and Hurst paper: Trowbridge [201], [237]-[240]. It is true that he was unaware that the Berry Medium and Berry High curves on p 22 of that presentation were different from the Berry Medium and Berry High projections on pp 11, 12 and 13 of the same presentation. No criticism could be made of Mr Wilkinson in that respect, because there is no explanation in the presentation that the two curves, identically described in the presentation, were in fact different. An explanation was not provided until Mr Minty's statement of 18 June 2004 (Ex 258) and in his evidence in chief: T3265.23 - 3267.48.

B15.8 But in any event, Mr Wilkinson's basic criticism remains unanswered. Watson and Hurst showed convincingly that Berry Medium and Berry High were poor predictors of mesothelioma incidence. Why should those curves, even recalibrated, be better predictors in the future? In particular, why should Berry Medium be the best estimate, when all the available data demonstrated that Berry High was too low?

B15.9 An attack is made on the comparison performed by Mr Wilkinson in his figure 3.1 (Ex 252 p 18), based principally upon the failure to make allowance for various categories of exposure to asbestos: Trowbridge [213]-[223]. It was readily acknowledged by Mr Wilkinson that the model was "crude"; its purpose was to identify the peak and shape of Australian asbestos exposure with that in the United Kingdom (T3416.16-44), not for any more precise task.

B15.10 Notwithstanding those criticisms, the model showed a peak shortly after 1970. That is entirely corroborated by the modelling performed by Mr Whitehead (Ex 251, figure 3.1 on p 3-15 and figures 3.4 and 3.5 on p 3-21), which also showed a peak in 1974 or 1975. Nor, despite the cross-examination of Mr Wilkinson, does Trowbridge seriously dispute that result. The basic proposition, derived from the analyses of both Mr Whitehead or Mr Wilkinson, is that Australian exposure to asbestos peaks some years after that in the United Kingdom.

B16 Issue 17 - Trowbridge

B16.1 Trowbridge's invitation to the Commission to find that Messrs Minty and Marshall were *not* aware that the incoming directors proposed to use the February report in forming a view as to the likely longevity of the fund (Trowbridge [265]ff) should be rejected. If that was not obvious from the instruction to provide the report for 10, 15 and 20 years, it was made perfectly clear by Mr Gill's question to Mr Minty: "How long would $280 million last?" (cf Trowbridge [282]).

B16.2 Trowbridge submits that it owed no duty of care to and there was no reliance by Coy and Jsekarb: Trowbridge [293] – [305]. Trowbridge further submits that it owed only a qualified duty to the incoming directors: Trowbridge [324] – [325].

B16.3 As for the duty of care owed to Coy and Jsekarb, Trowbridge was told that its report was being prepared for new management. Trowbridge ought to have known that business decisions were likely taking place in connection with that management change, and that any such decisions would be made in reliance on that report.

B16.4 As for the submission that Messrs Morley and Cameron did not in fact rely on the Trowbridge report (Trowbridge [301] – [304]), it should be rejected. Both of Messrs Morley and Cameron entered into the DOCI in the belief that Coy and Jsekarb would be in a position to meet all present and future liabilities: T538.23; T2158.1. That they did not read the actual February 2001 report does not stand in the way of their relying on its bottom line.

B16.5 As for the duty owed to the incoming directors, that duty is informed by the Actuaries' Code of Conduct 15:

> If there is reason to believe that an actuary's advice will be transmitted in whole or in part to a third party, the actuary must take all reasonable steps to ensure that authorship and responsibility are acknowledged to the third party, that any significant implications of the advice are stated, that the advice is not presented in a way likely to give a misleading impression, and that any constraints on the actuary's independence are disclosed.

B16.6 Trowbridge knew that the February 2001 report was being relied on by the incoming directors: Mr Jollie told them so expressly, and his statement was rhetorical, not informing Trowbridge of something hitherto unknown. The obligation was upon Trowbridge to take all reasonable steps to ensure that:

(a) all significant implications of the advice were stated; and

(b) the advice was not presented in a way likely to give a misleading impression.

B16.7 The only way in which the February 2001 report could conceivably comply with actuarial standards was if it were read in conjunction with the draft June 2000 report. It must have been obvious to Trowbridge that the incoming directors did not have that report. In any event, the onus was on Trowbridge to ensure that they did. At the very least, the February 2001 report should have stated:

> This report is a supplement to, and must be read in conjunction with, our report of June 2000.

B16.8 The deficiencies identified above and in chief give rise to the possibility of claims for damages against Trowbridge.

C. The Cashflow Model and Earnings Rate Assumption

C1 Overview

C1.1 Ultimately two submissions are put by Counsel Assisting. They are:

(a) that JHIL by Messrs Macdonald, Morley and Harman was negligent in permitting the cashflow model to be used by the JHIL Board and the incoming directors of the MRCF because they ought to have realised it was not suitable to assess the likely longevity of the MRCF or what level of funding would be appropriate to found a reasonable likelihood that all claims against Coy and Jsekarb could be met: CA, Section 2, [49], [51];

(b) that the evidence supports a finding that Mr Macdonald was recklessly indifferent to the utility and suitability of the cashflow model: CA, Section 2, [66].

C1.2 Each of these submissions should not be accepted.

C2 No negligence on the part of Harman, Morley or Macdonald (Issue 27)

C2.1 As to the alleged breach of any duty owed to the incoming directors of the MRCF:

(a) none of Messrs Macdonald, Morley or Harman undertook to the incoming directors to formulate a model which was suitable to assure the likely longevity of the MRCF;

(b) those directors wanted to be satisfied that the fund would be sufficient to last for fifteen to twenty years;

(c) they did so by receiving the Trowbridge "best estimate" forecasts for ten, fifteen and twenty years with projections of returns based on different assumed earnings rates: JH, 9.6;

(d) they did not rely upon a forecast gross earnings rate of 11.7%. For example, Jollie requested calculations based on earning rates down to 7%: JH, 9.6.16, 9.6.17. In August 2001, Mr Cooper told Mr Ashe that the incoming directors had regarded 11.7% as unrealistic and that it was their view that 8.7% was more realistic: JH, 9.6.8(e).

C2.2 As to the alleged breach of any duty owed to the directors of JHIL:

(a) Mr Harman prepared the cashflow model at the request of Mr Shafron and Mr Morley;

(b) the assumptions underlying the model he prepared were laid out for all to see: cf CA, Section 2, [26];

(c) Mr Harman liaised with PwC and Access Economics in relation to their reports;

(d) the limitations upon the reports of PwC and Access Economics were made known to the Board of JHIL;

(e) the fact that PwC and Access Economics had expressed concerns about the assumptions underlying the model was raised with the Board of JHIL: JH, 8.8.2;

(f) Mr Morley formed his opinion about the gross earnings rate of 11.7% pa after a detailed analysis of historical rates of return achieved by equities, pooled funds and superannuation funds: JH, 8.3;

(g) the JHIL Board was advised that PwC or Access Economics had suggested that independent advice be obtained upon the earnings rate. It was also advised that UBS Warburg had declined to advise on that question: CA, Section 2, [6], [29];

(h) the JHIL Board was also advised that earnings rates could be volatile: JH, 12.3.7, 12.3.8; and was supplied with sensitivity analyses on different assumptions as to the Trowbridge projections and earnings rates: see Ex 150, pp 135, 142, 145, 146 and JH, 12.3.1 and 12.3.2;

(i) the possibility of using a risk-free rate of return as distinct from an earnings rate based on returns on equity investments was debated before the JHIL Board on 15 February: JH, 12.3.4.

C2.3 At the end of this process, each of Mr Harman and Mr Morley believed, it is submitted honestly, that the earnings rate of 11.7% pa was within a reasonable range or conservative: JH, 8.3.2.

C2.4 It is not suggested by Counsel Assisting that any finding of dishonesty should be made concerning Mr Morley or Mr Harman: CA, Section 2, [57].

C2.5 The evidence indicates that Mr Macdonald had a very limited role in relation to the formulation and development of the cashflow model and the dealings with PwC, Access Economics and UBS Warburg. The submissions of Counsel Assisting do not suggest otherwise. See also JH 8.1, 8.2, 8.3, 8.4, 8.5. Mr Harman and Mr Morley were responsible for the preparation of the cashflow model and its presentation to the JHIL Board on 15 February. Mr Macdonald listened to the discussion concerning the model and earnings rates and ultimately accepted the logic of the model and the reasonableness of the earnings rates: Ex 308, [43] to [49]. In doing so, and in reaching that conclusion, it is submitted that he was not negligent.

C3 The use of an earnings rate of 11.7% (Issue 18)

C3.1 This issue is dealt with in JH 8.1, 8.2 and 8.3. The suggestion that the task Mr Harman undertook simply involved calculating an earnings rate which would produce a positive outcome after fifty years does not reflect the evidence: cf. CA, Section 2, [3] – [4]. An early model produced on 4 January 2001 used an earnings rate equivalent to the overdraft rate of 8.1%: JH, 8.1.3. The first model using the Trowbridge data was prepared on 7 February 2001. It used gross (pre-tax) earnings rates of 10%, 12.5% (which was described as

equivalent to an after-tax rate of 8.1%) and 15%. The models produced on 8 February 2001 continued to use gross earning rates of 12.5% and 15%: JH, 8.1.4. Subsequently, Mr Harman was asked to identify the earnings rate which would ensure that the Fund would survive the entire fifty years. It was at that stage that the number 11.7% was produced. By that time, gross earnings rates in excess of that number had been used in the models: JH, 8.3.3.

C3.2 It should also be noted that the model tabled at the JHIL Board meeting of 15 February 2001 contained sensitivity analyses for earnings rates varying between 9.70% per annum and 13.70% per annum: Ex 75, tab 121, p 2824.

C4 The retainer and use of PwC and Access Economics (Issues 20 and 21)

C4.1 It is probably not the case that the idea of having the model independently verified was first suggested by Mr Loosely: see JH, 8.5.2 and 8.5.3 and cf. CA, Section 2, [8], [12]. The evidence does not suggest that it was ever contemplated that either expert would review the earnings rate assumption. It would seem that at some point it was proposed that that task be undertaken by UBS Warburg. That is what Mr Harman believed: JH, 8.5.11; and at some time before 15 February, Mr Sweetman of UBS Warburg was asked by Mr Morley to provide views about those rates: JH, 8.4.1. He declined to do so and that fact was ultimately communicated to the JHIL Board: CA, Section 2, [29].

C4.2 In these circumstances, the suggestion that the decision to retain PwC and Access Economics was not implemented with the "seriousness it deserved" should be rejected: cf. CA, Section 2, [12]. Initially, it was proposed that UBS Warburg examine the earnings rates. That made it unnecessary to have those experts look at that question. When UBS Warburg declined to do so, Mr Morley formed the view that his analysis of the historical rates was sufficient. Mr Harman did not disagree.

C4.3 Not much should be made of Mr Morley's agreement that the exercise which had been undertaken by PwC and Access Economics was "arid and pointless": cf. CA, Section 2, [11]. The concession was understandable from his perspective. He was entitled to believe that the model was sound. Moreover, the Commission should be cautious in judging these events with hindsight; no one other than Mr Harman had reviewed the detail of the model (Harman T1263.48) and it is inherently likely that Mr Harman would have seen some benefit in having PwC and Access Economic Reports confirm that the model was logically sound and technically correct (T1263.2).

C5 Use of Minty advice (Issue 22)

C5.1 The comments made by Mr Minty on 19 January 2001 were made in Mr Morley's presence. They were not matters about which Mr Minty was asked to or did express a professional opinion. Mr Morley was the officer who had charge of the earnings rate analysis. There was no reason for Mr Shafron to point out to Mr Morley what Mr Minty had said. It was not

suggested to Mr Morley that he did not have any regard to Mr Minty's remarks or that he should have communicated those remarks to the JHIL Board. In the circumstances, nothing should be drawn from this: see also JH, 8.6.1.

C6 The Access Economics and PwC reports (Issues 23, 24, 25 and 26)

C6.1 Suggestions that the JHIL Board seek an independent review of the underlying assumptions used in the model and of the need to test the model to accommodate volatility in earnings rates and cash outflows were communicated to and discussed by the JHIL Board on 15 February 2001: see paragraph C2.2 above. The only "warning" contained in any draft report which was not in terms advised to the JHIL Board was the Access Economics statement that an earnings rate of 11.6% was "a relatively high return on assets" which would need to be tested. However, the evidence as to discussion at the JHIL Board meeting is that there was debate about the earnings rate, as to whether a risk-free rate should be adopted and as to how Mr Morley justified an earnings rate of 11.7%: see paragraph C2.2 above. That discussion took place in a context where it was appreciated that there was no independent advice from UBS Warburg or any other entity on the earnings rate. It also took place in the presence of various advisers including Mr Wilson and Mr Sweetman of UBS Warburg: JH, 12.1.2.

C6.2 There is nothing sinister in the drafting suggestions made by Mr Harman to PwC and Access Economics. He was aware of the limitations on their retainers. However, it would seem that he believed at the time that UBS Warburg was to provide advice on future earnings rates: JH, 8.5.11. That belief would explain both of the drafting suggestions which he made:

(a) that made to Mr Brett of PwC which resulted in the deletion of the words "to seek an independent view": JH, 8.5.11; and

(b) that made to Mr Waterman of Access Economics which resulted in an observation as to a gross earnings rate of 11.6% being "a relatively high return on assets" being deleted: JH, 8.5.11.

C6.3 No attempt was made to suppress the limitations upon the retainers of PwC and Access Economics or their recommendations as to the obtaining of independent advice and the reviewing of assumptions. Each of these matters was referred to at the JHIL Board meeting: JH, 8.8.2, 8.8.3 and 12.3.1ff. Mr Harman's denial that he was seeking to keep anything from the Board in making those changes should be accepted: JH, 8.5.9.

C6.4 There is no basis in the evidence for a finding that any of those drafting suggestions followed directions from or were known to any of Messrs Morley, Shafron or Macdonald.

C6.5 Nor is there a basis in the evidence to justify a finding that the suggested changes made to the PwC and Access Economics reports were part of a strategy of the "management team" or some "managed" process: cf. CA, Section 2, [18] to [23]. For the reasons given above,

the suggested changes were made at the instigation of Mr Harman. There is no evidence of input from Messrs Morley, Macdonald or Shafron. The substance of the cautions about checking the assumptions and obtaining independent advice was communicated to the Board. The JHIL Board was even told that UBS Warburg had been asked and declined to give advice about future earning rates: CA, Section 2, [29].

C6.6 There is a specific suggestion in the submissions of Counsel Assisting that the management of JHIL together resolved to keep material information from the Board. It should be rejected. The evidence does not indicate that there was any discussion between the "management team" as to the three options identified in CA, Section 2, [18]. Mr Harman's requests to Mr Brett and Mr Waterman to make drafting changes were not the result of any strategy by management to pursue an option which involved suppressing information from the Board.

C7 Appropriateness of earnings rate adopted

C7.1 The gross earnings rate of 11.7% was equivalent to an after-tax rate of 7.6% which is not very different from the rate identified by Dr Kingston (6.4%): see JH, 8.7.1 to 8.7.10. The following other matters are relevant to a consideration of the reasonableness of the rate adopted by Morley.

C7.2 First, the draft Access Economics comment was that a gross rate of 11.6% was "a relatively high return on assets". That description is to be contrasted with Dr Kingston's description of that rate as "substantially too high". The latter opinion is given with the benefit of hindsight.

C7.3 Secondly, the incoming directors (including Mr Jollie) were satisfied that a rate of 8.7% was reasonable: see JH, 9.6.8.

C7.4 Thirdly, in mid-2001 Towers Perrin suggested to the MRCF a "most likely investment return" of 7.5%: JH, 8.7.11.

C7.5 Finally, the analysis undertaken by Mr Morley which is now criticised was a logical and rational analysis to undertake.

C8 Macdonald was not recklessly indifferent to the utility or suitability of the cashflow model (Issues 28 and 29)

C8.1 CA, Section 2, [58] – [66] address the "honesty" of Mr Macdonald.

C8.2 The first thing to note is that there is a deal of sliding between submissions that Mr Macdonald's conduct was dishonest and submissions that his conduct displayed reckless indifference. Although either state of mind is sufficient for there to be criminality, there is a very real difference in the quality of the underlying conduct.

C8.3 The second thing to note is that, at CA, [62] – [64], the submissions seek to rely as "surrounding events and circumstances" upon events which occurred years after the cash

flow model was put in place. That mode of reasoning would only be valid if the later conduct ("fobbing off" the MRCF, the transactions of 2003 and the rectification) was part of the one grand scheme or was strikingly similar to the February 2001 conduct. Neither is correct. In addition, the conduct referred to is “corporate” conduct as distinct from conduct for which Mr Macdonald was solely responsible and was conduct where he was constrained by obligations and perceived obligations to JHIL and JHINV.

C8.4 The third thing to note is the lack of precision in the after-occurring conduct:

(a) there was no "fobbing off" (cf. CA para 63(a)) of the MRCF. The MRCF for a very long period of time did not make any claim against JHIL or JHINV and, when it did, it did so with diffidence: see JH, 14.6, 14.7 and 15; see also Ex 189, p 408 which indicates a concern of Mr Macdonald in April 2001 that there were no "errors" on the part of JHIL;

(b) it is true that JHINV (not JHIL) sought to negotiate a transfer of shares in ABN 60 to the MRCF (cf. CA [63(b)]) but the indemnity was in exchange for an additional amount of some $18 million - $20 million;

(c) the cancellation of the partly paid shares (cf. CA [63(c)]) only occurred after the directors of JHIL were satisfied that there were sufficient funds to meet claims against it;

(d)&(e) the indemnity as drafted and as rectified did extend to claims by the MRCF against ABN 60 (cf. CA paras 63(c) and (d)). At the time it was given, Allens’ advice was that the MRCF and Amaca and Amaba had no compensable claims against ABN 60 and the distinction between an indemnity in respect of “asbestos” (Amaca and Amaba) and “non-asbestos” related claims was justified by reference to the original separation in February 2001. The indemnity was also given as part of the transaction by which ABN 60 was provided with significant additional funds to meet possible asbestos related liabilities.

C8.5 The fourth thing to note is that the reasoning from things that JHINV did *not* do years later ignores:

(a) the fact that the claims against Amaca and Amaba were no longer its concern; and

(b) the advice given to Macdonald that separation had to be real and that he should no longer have a role in those companies and the MRCF’s internal affairs.

C8.6 The fifth thing to note is that the final step in the reasoning is the assertion that "to say that JHINV treated the plight of victims of James Hardie asbestos with disdain would be an understatement". There is no basis for that suggestion.

C8.7 An example of conduct which could be so characterised would have been the stripping of assets from Amaca and Amaba for less than market value. That did not occur.

C8.8 A further example of conduct which arguably could be so characterised would have been putting Amaca and Amaba into liquidation, or leaving those companies only with the assets they possessed. This too did not occur. That was the proposal rejected by the JHIL Board in January 2001.

C8.9 What did occur was that Mr Macdonald urged upon the JHIL Board a proposal to infuse very substantial additional funds into the MRCF, with the consequences that the amount at hand would meet its asbestos liabilities for many years, according to the Trowbridge report and the cash flow analysis. Having persuaded the Board to part with in excess of $100 million, Mr Macdonald was concerned to ensure that the operating companies would not be subject to further claims to the extent that that could be avoided.

C8.10 Counsel Assisting submits that the quality of Mr Macdonald's conduct should be understood in the light of a course of:

> … doing all it could to ensure that even legitimate claims made in the interests of asbestos victims by MRCF, Amaba or Amaca would go unsatisfied.

C8.11 That reasoning should be rejected. The only appropriate way to assess the quality of Mr Macdonald's conduct in February 2001 is by reference to what he was doing (and understood he was doing) in February 2001 - propounding a proposal by which, to the extent of in excess of $100 million asbestos victims would be *better off* than they would have been had they been left to their rights against the manufacturers.

C8.12 That leaves the matters set out in CA, Section 2, [60], which are said to be "arguably" sufficient to permit an inference that Mr Macdonald was recklessly indifferent to the suitability of the cashflow model.

C8.13 As to the first, Counsel Assisting includes Mr Macdonald's knowledge of the limitations of the Trowbridge reports even upon the assumption (which JHINV says is well founded) that Mr Minty said the recent data was not required. The fact that a person relies upon actuarial advice detracts, from rather than supports, a finding that the person was recklessly indifferent. In Mr Macdonald's case, he was aware of the limitations on the reports as actuarial reports but was not aware of any limitations which meant that they could not be relied upon as such: Ex 308, [29] to [32]. He was aware that the recent data had not been used but had been told (with the other members of the JHIL Board) that Mr Minty had said that it would not affect the trend established: Ex 308, [33]. He also understood that Mr Minty had met with the incoming directors and made a presentation about the same Trowbridge estimates as were to be relied upon by him and the JHIL Board: Ex 308, [37].

C8.14 As to the second, Mr Macdonald, and all others concerned, well knew that the cash flow model was based on the Trowbridge projections and the earnings rate assumption. That does not support a finding of reckless indifference.

C8.15 As to the third, while Mr Macdonald knew that the earnings rate assumption was based on the assessment of Mr Morley and Mr Harman, their assessment is labelled "amateur" by Counsel Assisting. Even accepting that they were not specialists in the field, both had a great deal of financial, accounting, and taxation experience, and could scarcely be called amateurs. This is not a sound basis from which to conclude that Mr Macdonald knew or should have known that the earnings rate assumption was unrealistic.

C8.16 Furthermore, Mr Macdonald did not regard Mr Morley's assessment as "amateur": Ex 308, [45]. He participated in a lengthy Board meeting in which the appropriateness of the earnings rate was considered by directors who, at the end of that discussion, were, like him, satisfied with the rate used in the model: Ex 308, [46] to [47]; see also JH, 8.8.1 to 8.8.6 and 12.3.1 to 12.3.8. Those directors included persons with significant accounting and financial qualifications and experience: see Ex 78, tab 3, p 21.

C8.17 As to the fourth, it does not follow from the fact that he was aware that neither PwC nor Access Economics had reviewed the earnings rate assumptions that he was recklessly indifferent to the reliability of the cashflow model. He understood that Mr Morley had undertaken an analysis by reference to historical material and he had participated in the discussion at Board level which addressed and concluded upon the reasonableness of the earnings rate assumption in a context where it was known that no independent advice had been obtained and that the model was sensitive to volatilities in earnings rates: Ex 308, [43] to [53].

D. Independence and Time Pressure

D1.1 Counsel Assisting addresses Issues 30 and 31 at CA, Section 2, [67] – [87].

D1.2 The stated relevance of these issues is to explain how it came to be that separation occurred without adequate funding: CA, Section 2, [69]. That may be acknowledged, but it is submitted that a full explanation should, for the reasons given in JH section 9 (especially 9.2.8-9.2.9 and 9.6), also have regard to the willingness of the incoming directors to accept their positions irrespective of a full analysis of the life of the MRCF: this is most pronounced in the case of Mr Cooper.

D1.3 Each of the directors was willing to be persuaded (each to varying degrees). Of course, that was not unexpected, because each of the incoming directors was initially sounded out, and expressed enthusiasm. Responsibility is not to be attributed to JHIL insofar as the incoming directors disregarded the advice of Mr Bancroft that they needed to "undertake a due diligence akin to purchasing a business".

D1.4 The incoming directors were chosen because they were senior and experienced lawyers, accountants or company directors: Ex 150, p 33. It was Mr Shafron's expectation at the outset that the incoming directors would undertake something equivalent to a due diligence inquiry: Ex 150, p 41. When he wrote to Mr Jollie on 4 January, Mr Shafron said, "We are expecting to be guided by the prospective directors in relation to additional documents and information requests": Ex 17, tab 85.

D1.5 Responsibility is not to be attributed to JHIL insofar as the incoming directors did not follow up requests for the draft 2000 Trowbridge report or an early meeting with Mr Minty (referred to in CA, [77]). As at 7 February, Mr Shafron's expectation was that Minty would discuss the assumptions underlying his projections with the incoming directors at the presentation on 13 February: Ex 150, p 112. JHIL provided free access to Mr Attrill in the meantime (T108.6), and did not prevent them from asking questions of Mr Minty at his presentation. There is a suggestion in the evidence that the delay in circulating the February 2001 report occurred by an oversight on the part of Trowbridge: see Mr Minty's email to Mr Shafron on the morning of 13 February "Apologies for the delay - I thought we had sent this to you" (Marshall, Ex 54, tab 10, p 77).

D1.6 Counsel Assisting suggests (CA, [72]) that the incoming directors did not follow up on the request for a cashflow model at a 7% earning rate. The Commission should find that JHIL produced the model using 7% and that Mr Jollie received it: see JH, 8.1.8. Again, no responsibility can be attributed to JHIL in this regard.

D1.7 Counsel Assisting suggests that the incoming directors were put under great (and unnecessary) time pressure (CA, [81], and [82] – [87]). This should be seen in its context:

(a) on 15 January 2001, the directors were told that the JHIL Board was meeting on 15 February 2001 and if they decided in favour of the Foundation, "we're in operation next day": Ex 75, tab 92, p 2499 (Mr Attrill's note);

(b) the incoming directors were content to proceed on that basis;

(c) such time pressure as there was arose through the late provision of the Trowbridge report and the cash flow model which was based on it - the other materials were circulated in advance;

(d) that delay is not attributable to JHIL;

(e) even so, the incoming directors were content to proceed on the basis of the presentation by Trowbridge on 13 February 2001 and the draft report circulated at that presentation - even Mr Jollie, although his evidence is that he returned the draft report, nevertheless was prepared to become a director two days after.

D1.8 All of this suggests that the time pressure was not of great significance in analysing the way in which the incoming directors made their decision.

D1.9 As Counsel Assisting submits at CA [82] – [87], JHIL did consider itself to be under significant time pressure, by reason of the introduction of ED 88. There is no reason to criticise JHIL for forming that view; in particular, there is no dispute that JHIL management believed that its principal Australian competitor CSR would shortly adopt ED 88, and no valid criticism is available that was not something to which the JHIL Board was legitimately entitled to have regard.

D1.10 It is also said in Counsel Assisting's submissions (CA, [81]) without particularisation that the incoming directors were misled by James Hardie in material respects, and that significant information was withheld from them. JHINV relies on its earlier submissions in response.

E. Deed of Covenant and Indemnity of February 2001 (Issues 32 to 38)

This subject is specifically addressed in chief by parties as follows:

(a) sections 11.2 and 12.7 of the JHINV/ABN 60 submissions;

(b) section 2, [88]-[157] of Counsel Assisting's submissions; and

(c) Chapter V, [32.1]-[35.74] of the MRCF's submissions.

E1 Calculation of the consideration for the DOCI (Issue 32)

E1.1 The MRCF submits that the amount of the indemnity was intended to reverse the October 1996 dividend: MRCF, [34.11]. That is incorrect. The amount to be paid was the amount calculated by Mr Harman's cashflow model to be the additional funds that Coy and Jsekarb required to meet all of their liabilities, particularly their asbestos liabilities: see JHINV/ABN 60, [11.2.13]. Counsel Assisting do not appear to take a different view: CA, Section 2, [90], [91]. Mr McGregor's and Mr Cameron's evidence that it was the additional amount needed to fund the Trowbridge estimates was an imprecise way of saying the same thing, CA, Section 2 [91], and see Mr Cameron's evidence at T527.9 and T661.5 – which demonstrates that Mr Cameron understood how Trowbridge's calculations were used. The rough similarity between the amount required to reverse the dividend (with compound interest) and the additional sum that came from the Harman model was a coincidence.

E1.2 The observation that the $80 million (NPV) was not the product of negotiation by parties at arm's length is not to the point. A transaction is not tainted just because it was not conducted at arm's length. If it were otherwise, a group of companies could never properly function. This was a case of a parent company wanting to provide assistance to its subsidiaries in circumstances where the parent believed, on legal advice, that it had no obligation to do so. The DOCI provided a commercial justification for the perceived generosity.

E1.3 Both Counsel Assisting and the MRCF contend that Mr Morley and Mr Cameron as directors of Coy, should have given consideration to how much the separation was worth to JHIL and used that intelligence to bargain for a bigger payment: CA, Section 2, [100], [103]; MRCF, [35.10]-[35.11], [35.43]. There are several problems with this submission.

E1.4 First, it assumes that the DOCI was an essential part of the separation. It was not. It has not been established that JHIL would have paid more if Mr Morley and Mr Cameron had asked for more – given that JHIL already thought that it was being generous the likelihood is that no extra money would have been provided.

E1.5 Secondly, and perhaps more fundamentally, the proposition that the directors of Coy and Jsekarb were duty bound to seek to negotiate to extract as high a price as possible, in a transaction between those companies and their sole shareholder is unsound.

E1.6 The MRCF identify section 187 of the Corporations Act as a "failsafe" method of removing the conflict of interest that was said to exist in the transaction between Coy and Jsekarb and their parent company: MRCF, [35.32]. That is a fair submission, and it is one that ABN 60 relies on in relation to the ABN 60 Foundation. The failure to include express provisions in the constitutions of both Coy and Jsekarb to invoke section 187, as Mr Koeck had advised, was almost certainly an oversight: T2154.54-2155.28.

E1.7 However, section 187 does not add a great deal to the common law position. A director is not in breach of duty to a company if:

(a) the director acted having regard to the interests of the shareholders of the company;

(b) the company was solvent at the time; and

(c) the director acted in good faith.

See *Pascoe Ltd (in liq) v Lucas* (1998) 27 ACSR 737, affirmed at (1999) 75 SASR 246 and discussed by Baxt in "Directors' Duties and Corporate Governance" (2000) 18(3) CSLJ 223. Provided there is no prejudice to creditors and there is good faith, there is no impediment for a wholly owned subsidiary to take into account the interests of its parent company. Payment of dividends, for example, involves decreasing the assets of a company in favour of the owners of the company. Considering the interests of the group does not result in a breach of duty: *Maronis Holdings Ltd v Nippon Credit Australia Pty Limited* (2001) 38 ACSR 404. Thus, Mr Morley and Mr Cameron would not need to rely on section 187 in order to justify acting in the interests of JHIL, or at least taking into account the interests of JHIL – provided they were satisfied that creditors were not prejudiced. This submission is not intended to undermine or contradict the submission put in chief that Mr Morley and Mr Cameron were properly satisfied that the execution of the DOCI was in the best interests of Coy and Jsekarb.

E1.8 Thirdly, it would appear that the MRCF and Counsel Assisting would have had Mr Morley and Mr Cameron use information acquired by them as officers of JHIL to seek to obtain extra advantage for Coy and Jsekarb. This follows from the submissions suggesting that Mr Morley and Mr Cameron knew what separation was worth to JHIL and should have exploited that knowledge. But on the kind of analysis now being employed by Counsel Assisting and the MRCF, that conduct would have resulted in breach of duties owed to JHIL. This serves to demonstrate that dealings between companies in a group are not by their very nature dealings as between completely independent entities. They should not be judged by reference to dealings between independent entities.

E2 Advice on intercompany payments (Issue 33)

E2.1 Nor can Mr Morley or Mr Cameron properly be criticised because they did not obtain a final legal opinion on the question of whether Coy could recover the 1996 dividend: CA, Section 2, [101], [103], [113]-[120]; MRCF, [34.3]. That is a counsel of perfection. Directors are entitled to form business judgments without concluded legal opinions. In the present case, at the very least Mr Morley and Mr Cameron were entitled to conclude based on the information that had been received that the prospect of recovering the 1996 dividend was low and that it was worth giving up the opportunity to seek to recover the dividend in order to secure the DOCI payment. Indeed, given the terms of the DOCI, entering into the DOCI could almost certainly be justified even if Mr Morley and Mr Cameron had received advice that the prospects of recovery were high.

E3 Independent advice (Issue 34)

E3.1 Having regard to all the circumstances, described above and more fully in the JHINV/ABN 60 submissions in chief, the criticism that Mr Morley and Mr Cameron failed to ensure that Coy and Jsekarb were independently advised is also unfair. That is essentially because it was not necessary for Coy and Jsekarb to seek to extract every possible advantage out of the transaction in order for the transaction to be unimpeachable at law. It is also significant in this context that Mr Koeck, who thought that Allens were acting on both sides of the transaction and was unconcerned by that fact (T1882.25), did not advise Mr Morley and Mr Cameron that they should instruct separate solicitors to protect the interests of Coy and Jsekarb.

E3.2 The position of Mr Shafron is even stronger: see CA, Section 2, [133] – it may be that the reference to Mr Shafron in this context is a typographical error. It was not his responsibility to make sure that Coy and Jsekarb obtained independent advice and he acted very properly by insisting that Mr Morley and Mr Cameron were independently advised. He was entitled to believe that if the directors were independently advised, then the decision of the directors on behalf of the companies would be made properly.

E4 The views of Mr Morley and Mr Cameron (Issue 35)

E4.1 Counsel Assisting submit that Mr Morley was prepared to enter into the DOCI "provided he was satisfied that the Foundation would have enough funds to meet the liabilities of Coy and Jsekarb: CA, Section 2, [100]. Counsel Assisting accept that Mr Morley and Mr Cameron held views that the amount of money paid to secure the indemnity (coupled no doubt with the assets of Coy and Jsekarb) would be sufficient to meet all liabilities: CA, Section 2, [135]. In this context, the word "liabilities" is used in a relatively loose way to include all prospective creditors; such as person who contract an asbestos disease in the future. There is a real doubt about whether those persons are relevantly "creditors" for the purposes of the Mr Morley's and Mr Cameron's decision on 15 February 2001: see the

section below on cancellation of the partly paid shares where this topic is considered in more detail. On this basis, Mr Morley's and Mr Cameron's goal to gather sufficient funds to meet all future asbestos liabilities went much further than they were obliged to go.

E4.2 If Mr Morley and Mr Cameron did not have to consider the interests of all future liabilities, it is unfair to submit that the consideration that was given was inadequate or unreasonable: CA, Section 2, [135]-[146].

E4.3 Furthermore, Counsel Assisting's criticism of Mr Morley's understanding is not fair. Counsel Assisting submit that he did not appreciate that the Trowbridge best estimate represented a 50/50 chance of being realised: CA, Section 2, [139(c)]. However, Mr Morley's answer to the relevant question shows that he may not have understood the question put to him: T2245.51. It is also incorrect to suggest that he did not appreciate that the net present value of $284 million related to a period of only 20 years: T2246.46; CA, Section 2, [139(d)]. With the benefit of hindsight, it is possible to point to some additional things that Mr Morley and Mr Cameron might have done to satisfy themselves that all future liabilities would be funded. But that does not mean that at the time the views that were honestly formed were not formed reasonably.

E5 Liability of JHIL (Issue 36)

E5.1 Having regard to the constraints on what was able to be considered in the evidence, the Commission is not in a position to assess the actual or potential liability of JHIL for asbestos related claims as at the date of separation. It is not possible to conclude that the assessment in February 2001 that the liability was limited was wrong.

E6 The put option (Issue 37)

E6.1 It is not clear whether Counsel Assisting mean to convey a criticism in relation to the inclusion of the put option in the DOCI: CA, Section 2, [149]-[153]. It is submitted that inclusion of a put option in order to provide a mechanism by which total separation from an asbestos association might be achieved is not improper or wrongful.

E6.2 The Commission should not draw any adverse conclusions based on the inclusion of the put option.

E7 Shadow directors (Issue 38)

E7.1 The relevant question is whether the decision made on behalf Coy and Jsekarb to enter into the DOCI was made by JHIL, or by Mr Macdonald or by Mr Shafron. In other words, did Mr Morley and Mr Cameron merely do what they were told to do?

E7.2 The evidence put against JHIL, Mr Macdonald and Mr Shafron on this subject is unconvincing. Thus the mere fact that Mr Shafron "gave them the number" does not mean that Mr Shafron was giving an instruction: CA, Section 2, [157]. Nor do JHIL, Mr Macdonald or Mr Shafron become shadow directors merely because they requested Mr

Morley or Mr Cameron to do something or even by letting them know that JHIL, as the sole shareholder, would like something done. Mr Shafron does not become a shadow director because Mr Morley is "close to Mr Shafron": MRCF, [35.64]. Nor can any inferences be drawn because Mr Cameron sought the advice of Allen's in response to correspondence from Clayton Utz in 2003: MRCF, [35.66], [35.67]. Allens responded to correspondence for both JHINV and ABN 60: Ex 3, vol 1, tab 28.

E7.3 Mr Morley and Mr Cameron received independent legal advice from Mr Koeck and turned their minds to the question of whether Coy should enter into the DOCI. The decision to do so was theirs and theirs alone.

E7.4 None of JHIL, Mr Macdonald or Mr Shafron was a shadow director of Coy or Jsekarb.

E8 JHINV

E8.1 The MRCF also seek to sheet home liability to JHINV: MRCF, [35.68]-[35.74]. As at February 2001, which was prior to the scheme of arrangement, the company that later became known as JHINV was a subsidiary of JHIL: ABN 60/JHINV [1.1.8]. Its name then was RCI Netherlands Holdings BV.

E8.2 The MRCF submits that JHINV was knowingly concerned in the alleged contraventions of the Corporations Act by Mr Cameron. The fact that Mr Cameron was a director of RCI Netherlands Holdings BV does not make it an accessory. Nor can it sensibly be suggested that in February 2001 he was engaged in conduct for the benefit of JHINV (to say nothing of the fact that that was not suggested to him in cross-examination). MRCF also submits that JHIL acted on behalf of JHINV. It cannot be inferred that as at February 2001, JHIL was relevantly acting as agent for an undisclosed principal, namely RCI Netherlands Holdings BV. JHIL was plainly involved as a principal. There is no reason to suppose that references in February 2001 to "JHINV" were intended to be references specifically to RCI Netherlands Holdings BV.

F. Separation and public relations (Issues 39-42)

The submissions of Counsel Assisting are found at CA, Section 2, [158] – [203]. There are in substance three matters addressed:

(a) the alleged secrecy in relation to the decision to establish the MRCF and whether this affected government reaction;

(b) whether there were contraventions of *Corporations Law* s995; and

(c) whether there were contraventions of *Corporations Law* s999 or s1309.

Each matter is addressed in turn.

F1 Alleged "secrecy" of the decision

F1.1 CA, Section 2, [178] states: "It seems likely that the trust structure was chosen for the separation primarily to permit the transaction to occur secretly".

F1.2 CA, Section 2, [184] states" "All efforts were made to ensure the Foundation proposal remained secret until its announcement".

F1.3 Neither submission should be accepted.

F1.4 As to the first, the process by which JHIL made decisions about restructuring was influenced by an assessment of what, overall, was the most desirable result for the company. The February Board presentation, under the heading "Objectives", stated (Ex 75, tab 123, p 2845):

> The primary objectives of the recommended solution include:
>
> - minimising execution risk and costs
> - minimising change from a shareholder perspective
> - extracting maximum benefits
>   - improving financial efficiency and increased after tax returns to shareholders
>   - minimising/removing asbestos effects
>   - earnings distortion / investor appeal
>   - management distraction
>   - poison pill
>   - positioning JHIL for continuing international growth
>   - Targeting JHIL's limited capital at its highest growth/return prospects (fibre cement)

F1.5 There is no reason to think that secrecy was the *primary* motivation on the part of the JHIL Board for the trust structure. Admittedly, one aspect of the perceived reduction in

execution risk was the absence of a ready forum (in contrast with the applications for convening a scheme meeting) in which opponents of the separation might be heard. But that was merely one facet of the preferred option.

F1.6 That secrecy was not the primary motivation is also confirmed by the 7 February 2001 advice from Allens, which was included in the JHIL Board papers: Ex 75, tab 119. Allens queried "whether there will be market/claimant/government pressure to disclose". The key advantage Allens acknowledged of management's preferred option was that it could be achieved in a short timeframe, in contrast with the option favoured by Allens.

F1.7 As to the second, JHIL took the unusual step of consulting very senior levels of Government not merely prior to the announcement but also prior to the decision itself. The Board presentation states (Ex 75, tab 123, p 2867):

- On Tuesday we briefed the chiefs of staff of the NSW Premier and Industrial Relations Minister
- The briefing was confidential and simply sought a likely read on government reaction as a precursor to subsequent formal meetings between JH and the government before the announcement.

F1.8 It follows that the premise for the submissions made at CA, Section 2, [184] is not made out. In any event, there is insufficient evidence before the Commission to make findings as to the reasons for the government reaction and what would have been the reaction on other hypotheses (Issue 41).

F1.9 Further, there are some factual matters which require correction.

F1.10 Contrary to CA, Section 2, [166], there is no basis to find that Mr Shafron's plan to engage Towers Perrin was "presumably" to "handle Minty" by providing arguments to encourage Mr Minty to adopt a more confident, less uncertain approach to estimating liabilities. The understanding of Mr Baker at the time was that he would:

(a) assist you with your internal review of Deloitte's report on asbestos liability; and

(b) assist in your discussions with David in relation to such matters as underlying assumptions regarding uncertainty of estimates, etc: (Ex 61, vol 4, p 149).

That is corroborated by Mr Attrill's contemporaneous statement to Mr Ashe:

> Peter said that he only wants us to obtain Verne's initial impressions of the Trowbridge draft. I think he wants us to find out from Verne what his likely attitude would be before we commit to formally briefing him: Ex 61, vol 4, p 250.

F1.11 Contrary to the impression created by CA, Section 2, [167] – [170], the fact that JHIL management and advisers were simultaneously working on different proposals, some of which involved separation, some of which did not, is not "strange" but instead is reflective of the manner in which JHIL made decisions. The fluidity and flexibility in which new ideas

were investigated and analysed is also not without importance having regard to the issue of whether and when JH's directors formed an intention to cancel the partly paid shares.

F1.12 What is left unstated in CA, Section 2, [173] is that Mr Baxter's proposal that the briefing would not be web-cast did *not* occur.

F1.13 CA, Section 2, [176] states that the decision to increase the medical research funding was "moulded" by public relations concerns. It is true that this aspect of the proposal, like all others, was reviewed by JHIL's communications department. But before Mr Ashe made his comments, the incoming directors had expressed a preference for additional funding: for example, Mr Attrill's note records Sir Llew Edwards being concerned to fund recent research but being told that "Claimsure will have ltd funds" and Mr Jollie saying on 15 January 2001, "We should be allowed to put $10m into research to reduce the possibility of future claims".

F1.14 CA, Section 2, [179] asserts that there was much activity to get Trowbridge to remove the Watson & Hurst report from its website. Mr Shafron's evidence was that he wanted some time to consider the impact to the company: Ex 17, [134]. Mr Macdonald was concerned that the company have the opportunity to consider the report before it was required to respond publicly: see JH. 7.2.3.

F2 Alleged contravention of Corporations Law s995

F2.1 It is important to bear in mind the following matters in analysing whether the matters published by JHIL following the establishment of the MRCF contravened any legal norm of conduct.

F2.2 First, the quality of the representation conveyed by the media release must be considered in light of the media release as a whole.

F2.3 Secondly, the key difference between the proposal rejected by the JHIL Board in January 2001 and that approved by the JHIL Board in February 2001 was that the former was based on funding equal to the net assets of Amaca and Amaba whereas the latter contained very significant additional funding.

F2.4 It was an important element of the decision to establish the MRCF that it was not mere separation, but separation *funded* by a significant contribution from JHIL.

F2.5 Thirdly, the media release made it clear that the description "fully-funded Foundation" was to be understood as a statement that the MRCF would have "sufficient funds to meet all legitimate compensation claims anticipated from people injured by asbestos products that were manufactured in the past by two former asbestos subsidiaries of JHIL". The third paragraph of the press release must be read as explaining the short-hand reference to "fully-funded" in the fourth.

F2.6 Fourthly, "fully-funded" does not mean "over funded" so there is a high degree of assurance for claimants decades in the future. Nor does it mean "under funded" so that there is a low degree of assurance for such claimants. Fully-funded conveys that there is a reasonable basis for the belief that the funds would be sufficient.

F2.7 Fifthly, the press release makes it clear that the amount of funding was determined by the JHIL Board, with advice from PricewaterhouseCoopers, Access Economics and Trowbridge.

F2.8 The statement as to funding was not a warranty or assurance. (In the press release it is said that "James Hardie is satisfied".) Therefore, the question whether it was misleading or deceptive falls to be tested at two levels. The first is whether it reflected the belief or state of mind of Mr Macdonald and the JHIL Board. The second is whether there were reasonable grounds for the belief.

F2.9 For the reasons set out in JH 8.8, 12.1, 12.2 and 12.3, Mr Macdonald and the JHIL Board believed and had a reasonable basis for believing that the MRCF was "fully funded".

F2.10 Sixthly, as to Issue 40(c), the media release accurately stated that "James Hardie sought expert advice from a number of firms, including PricewaterhouseCoopers, Access Economics and the actuarial firm Trowbridge".

F2.11 Seventhly, as to Issue 40(d), the establishment of the MRCF did provide additional certainty for claimants, because the funds to meet claims were no longer held by subsidiaries of an operating company which had, among other options, been considering putting the subsidiaries into liquidation. The assets were dedicated to meeting those claims.

F2.12 The fact that asbestos liabilities, like any other forward looking projection, were uncertain was implicit in what was said, and explicit in the statement that any surplus funds would be used to support further scientific and medical research.

F2.13 Finally, in response to Issue 40(e), as to the "best available information", JHIL had the assurance from Trowbridge orally and in writing that its report was based on "all the information available" notwithstanding that JHIL and Trowbridge knew that the most recent data had not been provided. As to a "reasonable rate of return", that view was held, and open to be held, for the reasons set out at JH 8.3 and 8.8. As to "detailed, expert and independent advice", the advice from all external advisers was expert and independent, and certainly the Trowbridge June 2000 report updated by the February 2001 report was detailed.

F3 Alleged contravention of Corporations Law s999 and s1309 by Mr Macdonald

F3.1 For the reasons submitted below, a submission that there is evidence warranting the prosecution of Mr Macdonald for any of the offences identified should be rejected.

F3.2 No submission is made by Counsel Assisting that any of Messrs Shafron, Morley, Harman or Baxter contravened or were involved in contraventions of the Law with respect to the publication of any media release or information to the ASX: CA, Section 2, [56], [57], [202].

F3.3 In this context, the question for the Commission is not whether any person committed an offence (cf. CA, Section 2, [190], [198], [201]) but whether there is "evidence or sufficient evidence warranting the prosecution of a specified person for a specified offence": s10(2) of the *Special Commissions of Inquiry Act* 1983.

F3.4 When addressing that question the Commission is required to disregard evidence that in its opinion "would not be likely to be admissible in relevant criminal proceedings": s9(4). Evidence answering that description (ie. evidence which would not be admissible) includes privileged material (see s23(2)) as well as hearsay and non-expert material which is not within any relevant exception to the hearsay and opinion rules.

F3.5 The submissions of Counsel Assisting do not identify the evidentiary material (ie. material which is admissible or likely to be admissible) by reference to which it is submitted that the Commission should conclude that there is any or any sufficient evidence to warrant a prosecution. In the absence of the identification of that material it is very difficult for the Commission to address properly the question which may arise under s10(1). In addition and more significantly from the perspective of Mr Macdonald, that absence means he does not have a fair opportunity to respond to the possible adverse finding or recommendation.

F3.6 The difficulty with addressing these questions in the absence of an identification of the relevant evidence is not theoretical because of the large body of evidence which consists of communications between James Hardie and its lawyers or between the lawyers themselves which is likely to be privileged and inadmissible in any criminal proceeding. Those communications and matters springing from them have been examined with the persons directly involved as well as others who have, on occasions, been asked to speculate more generally. To that extent, a difficult question may arise as to the admissibility of that additional material.

F4 Possible contravention of s999 of the Law

F4.1 To establish a contravention it must be established that a statement was made that is "false in a material particular or materially misleading" and that when it was made the person did not care whether it was true or false or knew or ought reasonably to have known that it was false.

F4.2 The phrase "ought reasonably to have known" requires that regard be had to the knowledge, intelligence and, where relevant, expertise of the person concerned. The question is not whether some hypothetical reasonable person in the position of that person would have known of the relevant falsity. It is what the particular person with his or her actual knowledge and capacity ought to have known: *Boughey v The Queen* (1986) 161 CLR 10 at 28-29.

F4.3 Thus, it must be shown that the media release was false or misleading in a material way and that Mr Macdonald knew that or was reckless as to whether that was the case or that an honest and reasonable man in Mr Macdonald's circumstances would have known that it was false or misleading. This last element does not lay down a test equivalent to that of negligence. It accepts Mr Macdonald's circumstances even if they include knowledge or belief which was mistaken and carelessly so.

F4.4 Counsel Assisting asserts (CA, section 2, [190]) that the statement that the MRCF was "fully funded" was false and that Mr Macdonald knew or ought reasonably to have known that because the cashflow model:

(a) did not provide any such "assurance";

(b) was based on non-expert opinion as to future earnings rates; and

(c) was based on actuarial reports of dubious reliability and utility.

F4.5 The following responses are made to this submission.

F4.6 First, it treats the "fully funded" statement as a warranty or assurance rather than as a statement of belief or opinion. It then asks the wrong question, namely whether Mr Macdonald knew or ought reasonably to have known that the model did not give such an "assurance".

F4.7 Secondly, for the reasons outlined above in relation to s995, Mr Macdonald and the other Board members of JHIL believed and had reasonable grounds for believing that the funding would suffice. Even if Mr Macdonald did not have reasonable grounds for that belief, there is no contravention of s999 unless he knew that or unless an honest and reasonable man in his circumstances ought to have known that. If the position was otherwise, this element of s999 could be satisfied merely by establishing negligence.

F4.8 As to paragraph F4.4(a) above, Mr Macdonald did not know that Mr Harman's cashflow model was such that it was "not capable" of providing a basis for such belief. It was plausible on its face. PwC and Access Economics did not advise otherwise. Indeed, Mr Brett of PwC advised that subject to the limitations identified, the model was appropriate for use to demonstrate that there was a surplus of funds: Ex 67, tab 17, p 2; Brett T1234.15. The other directors and Mr Morley and Mr Harman believed and acted on the basis that the model could be used for that purpose.

F4.9 As to paragraph F4.4(b) above, it did not follow from the fact that the future earning rates were not based on the opinions of independent experts that the MRCF was not fully funded or that there were not reasonable grounds for such a belief. The absence of any independent opinion was made clear to the JHIL Board, as was the fact that PwC and Access Economics had suggested that independent advice be obtained. Mr Morley explained how he derived the earnings rate and there was discussion with the other Board members. Those Board members included persons with significant accounting and financial qualifications and experience: see Ex 78, tab 3, p 21; Morley T2003.24. They concluded that they could proceed on the basis that the MRCF was fully funded.

F4.10 As to paragraph F4.4(c) above, although the Trowbridge report was deficient for the reasons set out elsewhere, Mr Macdonald did not in February 2001 appreciate this. On the question of the most recent claims data, he understood that Trowbridge did not consider this necessary: see Ex 308, [29] to [42].

F4.11 Generally: The terms of the media release (described in the minutes as the ASX Announcement) were considered and the subject of a resolution at the JHIL Board meeting on 15 February: Ex 75, Vol 8, tab 118, p 7. The minutes indicate that the Board was satisfied after discussion that there was likely to be a surplus of funds in the Foundation taking into account available assets, likely earnings rates and likely future claims and costs: Ex 75, Vol 8, tab 118. The discussion in relation to the available assets and likely earnings rates was extensive: see C2.2 above. There was also detailed discussion about the Trowbridge report and the fact that it had not been prepared using data beyond 31 March 2000: see JH 12.2.1 to 12.2.7. In addition, at the commencement of the meeting Sir Llew Edwards informed those present that the incoming directors had 'completed their due diligence' and believed that the 'asbestos liabilities should be adequately funded in the future'. He also said that the incoming directors were happy to have that fact known: Ex 75, Vol 8, tab 118, p 1.

F4.12 Mr Robb was present at the Board meeting. He had been sent a draft of the media release and made amendments to it: further supplementary statement of David Robb dated 28 July 2004, [12] and tab 4. The media release was also sent to and subject to comment by Mr Brett of PwC: Ex 67, paras 34 to 37.

F4.13 None of the matters referred to above is consistent with Mr Macdonald knowing or not caring whether the statements in the press release were not true or misleading.

F5 Possible contravention of s1309(1) of the Law

F5.1 To establish a contravention it is necessary to identify information made available to a securities exchange that "to the knowledge" of the relevant officer is –

(a) "false or misleading in a material particular"; or

(b) which, because something has been omitted from it, is "misleading in a material respect".

F5.2 Subsection 1309(1) requires "guilty knowledge that [the information] is misleading or contains relevant omissions": *Roget v Flavel & Sanders* (1989) 51 SASR 313 at 315. Thus, even if the information provided in relation to the affairs of the company is false or misleading in a material respect, it has to be shown on a subjective standard that the relevant officer had knowledge of that fact.

F5.3 The basis upon which it is submitted by Counsel Assisting that Mr Macdonald may have contravened this subsection is not spelt out in much detail.

F5.4 It would seem to be that the statement that the MRCF was fully funded and was able to pay all legitimate claims was false or misleading either because it was not the fact (CA, Section 2, [192], [193]) or because it was not accompanied by a statement of limitations concerning the Trowbridge report and the cashflow model: CA, Section 2, [193]. In either way it is put, it would have to be shown that Mr Macdonald knew that the statement was false or misleading.

F5.5 The first way of putting this asserted contravention treats the relevant information as a statement of the underlying fact (ie. that objectively speaking the MRCF was fully funded) rather than as a statement as to the belief of James Hardie (and Mr Macdonald) about that matter which was the information relating to the affairs of James Hardie which was furnished. As a description of the belief, the information provided was accurate. The belief was not qualified and accordingly the description of it in the media release was accurate.

F5.6 The second way of putting the asserted contravention suffers from the same problem. In addition, neither Mr Macdonald nor James Hardie understood that the cashflow model and the Trowbridge report suffered from deficiencies which qualified the belief which he (it) had formed and which was the subject of the relevant part of the media release: see Ex 308, [29] to [49].

F6 Possible contravention of s1309(2) of the Law

F6.1 To establish a contravention, it is again necessary to establish that the relevant information was false or misleading. It must also be shown that Mr Macdonald did not take reasonable steps to ensure that the information provided was not false or misleading (ie. did not reflect his belief and the belief of James Hardie).

F6.2 For the same reasons as are stated above, Mr Macdonald did not understand that the cashflow model and the Trowbridge report suffered from deficiencies and for that reason the belief which he and the other directors held was not a qualified belief. The information provided reflected what had happened and the company's views. James Hardie had in place a standard procedure which was followed in relation to the preparation of press releases: Ex 308, [12]. He believed that that procedure had been followed in relation to the release to the ASX on 16 February: Ex 308, [55], [56]. That procedure included having the release reviewed by lawyers.

H. The 2001 Restructure – Issues 44 and 45

H1 Overview

H1.1 There is substantial common ground between the submissions of Counsel Assisting and JH on these issues. In particular, in relation to Issue 45, there is agreement that most of the matters raised in these issues "do not raise significant concerns": CA, Section 3, [16]. Such matters are:

(a) the failure to disclose the existence of the put option;

(b) the matters raised in Sir Llew Edwards' letter dated 24 September 2001; and

(c) the matters raised by Mr Cooper on 19 April, 26 June and 7 August 2001,

identified in Issue 45(c)(ii), (iii) and (iv). That is in accord with 14.5, 14.6 and 14.7 of the James Hardie submissions in chief.

H1.2 There is no significant dispute in relation to Issue 44(a), which is addressed in CA, Section 3, [17] - [25]. It is, however, incorrect to submit, as is said in CA, Section 3, [25], that Mr Shafron at Ex 17, [225] was wrong to say that "it was not until December 2002 that JHINV management began to give specific consideration to whether it was a desirable time to transfer ABN60 outside the Group". Mr Shafron said that at the time the MRCF was established "it was contemplated at that time that JHIL might, in the future cease to be the parent of the group and cease to hold operating assets": Ex 17, [224].

H1.3 There is no dispute in relation to Issues 44(b) and 44(c). As to Issue 44(b), CA, Section 3, [26]-[35] is consistent with JH 14.4. As to Issue 44(c), CA, Section 3, [36]-[41] is not disputed, and is in accord with JH 14.5.4 - 14.5.7.

H1.4 The sole matter in contention in this section of Counsel Assisting's submissions is whether there was a material non-disclosure of JHIL's plans and intentions as submitted at CA, Section 3, [1]-[15]. This is addressed in Section H2 below. The points of difference between the submissions from the Unions and the MRCF are addressed in Section H3 and Section H4 below.

H2 Material non-disclosure of theoretical destruction of value of partly paid shares

H2.1 Counsel Assisting's submissions at CA, Section 3, [1]-[15] are in essence as follows:

(a) the disclosures by JHIL led to the Court perceiving that "there should be no risk of a call on the partly-paid shares being ineffective for any reason": [2];

(b) it was possible pursuant to s256B to reduce capital: [3];

(c) a reduction must not materially prejudice the company's ability to pay its creditors: [4];

(d) the sanctions for non-compliance with s256B might leave creditors at best with a remedy against directors, and possibly (if they were negligent but honest) with no remedy under s256B but only at general law or under s180 or s181: [4]-[5];

(e) in those circumstances, it was material to disclose the five matters referred to at [7].

H2.2 There are flaws in the above reasoning.

H2.3 As to (a) and (b), they are themselves inconsistent. The Court must be taken to have been aware of s256B, just as the Court would have been aware of earlier court-approved reductions of capital. It was perfectly plain to Hutley SC who advised on 17 May 2001 that "partly paid can also be extinguished": Ex 187, p 207. The evidence of Mr Cameron reproduced at JH 14.3.2 and 14.3.3 that Santow J was well aware that all forms of capital were capable of cancellation is undisputed and not properly capable of dispute.

H2.4 As to (d), this requires the assumption to be made that JHIL would in the future contravene the law. It is not in dispute that the directors of JHIL well knew the law in this respect: see JH 14.4.3.

H2.5 If (d) were right, it would follow that it would be necessary, on any *ex parte* injunction not merely to proffer the usual undertaking, but also to address the Court on the consequences if the applicant breached that undertaking. It would also be necessary on any application for *Anton Piller* relief to address what would happen if the applicant breached the terms of orders which were designed to protect the respondent. Examples might be multiplied (judicial advice to trustees, liquidators applying for confirmation of transactions). That this never happens in practice is a strong indication that the premise is flawed. (Often the question is asked "what is an undertaking worth" but not (at least not without good reason) is it assumed that an *ex parte* applicant will deliberately or negligently act unlawfully in the future so as to reduce the worth of an undertaking.)

H2.6 If an applicant in any of the above circumstances were to raise the risk of future breach, the response might be for the judge to ask "is there anything about your client that should cause me to think that it does not understand its obligations under law?" In the present case, no different from most other cases, the answer to that question would be that the law was well understood. That answer would have been accurate and that would have been an end to the matter.

H2.7 As to (e), the third of the five matters which it is said should have been disclosed (at [7]) turns upon the hypothesis that the partly paid shares were not cancelled before the transfer or put of the JHIL shares. This is contrary to the evidence and assumes that the put option properly construed applied at all to the partly paid shares: see JH 14.5.9. Moreover, as disclosed in the Information Memorandum, the terms on which the partly paid shares were issued provided:

Transfer: Notwithstanding anything contrary in the constitution of JHIL, the directors of JHIL may refuse to register any purported transfer of the partly paid shares without giving any reason. (Ex 121, tab 132, p 3110)

H2.8 That provision protected JHIL against the possibility of JHINV transferring the partly paid shares to a third party which would not be able to meet a call on the shares. That would have been understood by the Court. Counsel Assisting's submission, that the possibility of the value of the partly paid shares being destroyed by their transfer to a third party should have been disclosed to the Court, requires the assumption to be made that the directors of JHIL would, in the future, breach their directors' duties by agreeing to register a transfer of the partly paid shares which was contrary to the interests of JHIL. For the reasons in paragraphs H2.4 to H2.6 above, that submission should be rejected.

H2.9 The fourth and fifth matters which it is said should have been disclosed (at [7]) require an assumption that the JHIL directors subsequently failed to comply with s256B(1)(b). Again, for the reasons set out at H2.4 to H2.6 above (no need to disclose the possibility of future unlawful conduct), that submission should be rejected.

H2.10 For those reasons, the Commissioner should reject the submissions made by Counsel Assisting that there was any failure to comply with its duty of disclosure.

H3 Unions and Asbestos Support Groups

H3.1 The disclosure to the Court by James Hardie in connection with the members' scheme is addressed in Unions Chapters 5, 6 and 7 (pp 45-89), and again in Chapter 9 (pp 112-119). No topic is given lengthier treatment in those submissions.

H3.2 The principal vitiating conduct alleged in the submissions is that JHIL represented to the Court that:

(a) JHIL had made a firm decision to avoid any action in the future that would prevent a call on the partly paid shares from being met: Unions 5.2;

(b) JHIL had made a firm decision (or, alternatively phrased, entertained a firm intention) to avoid any future action that might stand in the way of preventing a call on the partly paid shares from being met: Unions 5.8,

but that, to the contrary, JHIL had made no firm decision not to cancel the partly paid shares.

H3.3 First, the alleged representation is phrased as a double negative. Such a formulation is in stark contrast with the plain, direct and robust language of the Union submissions as a whole.

H3.4 Secondly, phrased as a double negative, it is apt to confuse. Even the author of the submissions was, presumably, confused - the triply negative formulation of the representation at Unions 5.8 is assumed to be an error.

H3.5 Thirdly, representations that are made implicitly, or by silence, are invariably simpler than that formulated by the Unions. The mind does not infer a double negative.

H3.6 Cast in plainer language, the alleged representation amounts to this:

> JHIL had made a firm decision that a call on the partly paid shares would always in the future be able to be met, at least so far as action on its part was concerned.

or

> JHIL had made a firm decision that, among other things, it would never cancel the partly paid shares.

H3.7 This amounts to no more than the first of the five elements in the submissions of Counsel Assisting: cf CA, Section 3, [2]. But it is basic that capital can be cancelled, and it is uncontradicted that JHIL, its solicitors and senior counsel and the judge well knew that fact. See JH 14.3.2 and 14.3.3.

H3.8 It would take very clear language to convey to the Court that the partly paid shares which were to be issued were different from every other form of capital, in that the issuer had firmly decided never to exercise its rights under s256B and never otherwise to bring about a reduction in capital.

H3.9 Contrary to the Unions' basic submission, such a representation could not on any view, be made implicitly or by silence. That is the short answer to the lengthy submission.

H3.10 The only response to the unchallenged evidence of Mr Cameron put in the Union submissions is the very serious assertions, that his evidence in this respect was "a prime example" of his "tendency to obfuscate", his "sophistry", and that he was "thoroughly tutored" (Unions 6.37 - 6.39). It is conventional to put such matters squarely to a witness before making such submissions. It is also conventional, if such serious allegations are to be made in address, to articulate the basis upon which it is said that those conclusions are to be drawn. Those conventions have not been observed in the Unions' submissions.

H3.11 The reality is that Mr Cameron's evidence was truthful, candid, and indubitably correct.

H3.12 The vast majority of members' schemes of arrangement involve the issuing of shares. It cannot be the case that the issuer must either "firmly decide" to preclude any future exercise of the right given by s256B, or else disclose to the Court that a future reduction of capital is possible in order to avoid a misrepresentation. If the Unions' submissions are correct, the Court has been misled on countless times in the past - all of which have hitherto passed without remark.

H3.13 It is asserted that if Santow J had been told that JHIL had not precluded the possibility of the future cancellation of the partly paid shares, "it is clear that conditions would have been imposed to safeguard the position of creditors": Unions, 5.21. This misconceives what was happening at court. Santow J was, rightly, concerned to ensure that the fact that JHINV

was a Dutch company did not prevent the partly paid shares being of any different quality from partly paid shares issued to an Australian parent. He was not concerned to alter the basic notion that capital was capable of being reduced. It was not the Court's role to do so; Parliament has legislated to provide that capital is susceptible to being reduced.

H3.14 Reliance is placed on the decision of *Re City Bank of Melbourne Ltd* (1897) 3 ALR 220 at 227-228: Unions 5.24. The Court there was speaking, in familiar terms, about the need to ensure that there is no class oppression at the scheme meetings. The passage relied on as being the very sort of non-disclosure as is said to have occurred before Santow J (Unions 5.25) is entirely inapt:

(a) first, the Full Court was dealing with the conduct of the scheme meetings, not disclosure to the court on the first application; and

(b) secondly, the Full Court was dealing with a *creditors'* scheme, not a *members'* scheme as here.

H3.15 The Unions' submissions also address, more briefly, three other "material matters" which were not disclosed:

(a) the put option (Unions 5.27-5.33);

(b) the covenant not to sue and the indemnity in the February 2001 Deed (Unions 5.34-5.38); and

(c) the communications in the letter from Sir Llew Edwards dated 24 September 2001 and related communications (Unions 5.38).

H3.16 The first was not material to the approval of the members' scheme for the reasons given at JH 14.5.

H3.17 The second is a novel proposition, not suggested by any other party. The rights of shareholders of the listed holding company before and after the scheme were essentially the same. Elaborate efforts were put in place to achieve this, notwithstanding that JHINV was a Dutch company. The rights and obligations of JHIL pursuant to the February 2001 Deed were unaltered by the scheme. The covenant not to sue and the indemnity in the Deed could not be material to any consideration whether to approve the scheme.

H3.18 The third is refuted at JH 14.6. No attempt is made in the Unions' submissions to address the time at which Sir Llew's letter was received by Mr Macdonald.

H3.19 The lengthy submissions which follow, at Unions 5.40-5.65, presuppose that a misrepresentation had been made. For the reasons set out above, the basic submission should be rejected. It is not necessary to deal with the other misconceptions in those submissions

H3.20 Likewise, it is not necessary to address the elaborate submissions in Chapter 6 on the jurisdiction to set aside the orders for fraud, nor the submission on perverting the course of

justice in Chapter 7. These submissions are based on a false premise. However, James Hardie makes submissions about the manner in which the Unions' submissions have been put at pp 1 to 3 above.

H4 MRCF

H4.1 Chapter VIII of the MRCF submissions (Vol 2, pp 372 - 440) addresses the implementation of the scheme.

H4.2 The principal themes in that Chapter are:

(a) the contention that the emerging MRCF funding issues should have been disclosed to the Court;

(b) the proposed finding that throughout 2001 up to and during the hearings before Santow J, the Board and Management of JHIL either intended, or were seriously contemplating, the option of cancelling the partly paid shares in conjunction with putting JHIL to the MRCF (MRCF, 49.4, 49.5, 49.25) and that *in either case* disclosure to the Court was required;

(c) the submission that a representation was made in the Information Memorandum and to the Court that the partly paid shares were "perpetual not terminable" (this is repeated, eg at MRCF, 50.44 and 50.45, but especially at MRCF, 50.61-50.72); and

(d) the non-disclosure of the put option in the February 2001 Deed.

H4.3 Each of these matters is addressed in turn below.

Alleged non-disclosure of the MRCF funding problems

H4.4 Section 48 of the MRCF submissions ("The MRCF discovers the funding shortfall") addresses the facts, which are largely uncontested, relating to the way in which the MRCF directors investigated the funding of the MRCF and communicated their concerns to James Hardie.

H4.5 This issue was addressed in chief relatively concisely at JH 14.6 and 14.7, and it is not without significance that the submissions made by Counsel Assisting, which might be expected to be more objective that those of the MRCF, state that it does not raise any significant concerns. However, in light of the claims that are made, culminating in a submission that Mr Macdonald's evidence should not be believed, it is appropriate to make the following further response.

H4.6 Taking the MRCF's case at its highest, the obligation to disclose is said to arise from the following communications:

(a) first, the meeting between Mr Cooper and Mr Macdonald on 19 April 2001 - this meeting lasted 20 minutes, according to the contemporaneous email (Ex 150,

p 156), the funding question was the 6th of 6 items raised, and Mr Cooper said James Hardie had "probably done a good job on claims numbers";

(b) secondly, the 10-15 minute meeting between Sir Llew Edwards, Mr Cooper and Mr Macdonald on 15 May 2001. The MRCF submissions (MRCF, 48.15 - 48.19) focus on Mr Macdonald's refusal to accept the document which had been prepared by Mr Cooper. But the signficance given to that in the MRCF submissions is at odds with the contemporaneous file note of Mr Cooper (MRCF.002.0002A, Ex 7, not referred to in the MRCF submissions), which *makes no mention of the refusal* and, to the contrary, states that Mr Macdonald was pleased to receive the information and would want to be kept informed if, following more extensive experience, the MRCF's concerns remained. The most likely explanations for Mr Macdonald's refusal are:

(i) the document prepared by Mr Cooper (Ex 7, tab 33) is, self-evidently, relatively crude (it is a single page, there is no analysis or justification for the new assumptions, which were merely to decrease the rate of return by 3% and to increase the cost of claims by $10 million per annum) and obviously required more detailed analysis; and

(ii) the February 2001 separation was in fact, and was to operate, as a real separation, and it was important that JHIL no longer have any control or influence in the internal affairs of its former subsidiaries;

(c) thirdly, the meeting between Mr Cooper and Mr Ashe on 26 June 2001, the contemporaneous note of which (Ex 150, p 163) shows that the MRCF were at that time undertaking (and had not completed) a solvency analysis;

(d) fourthly, a short telephone conversation between Sir Llew Edwards and Mr Macdonald in which no claim was made and the highest Sir Llew put the position, on his own evidence, was that the Foundation *could* be insolvent in less than ten years; and

(e) fifthly, the letter dated 24 September 2001.

H4.7 On any view, there is nothing in the matters (a), (b), (c) and (d) above which articulated or even foreshadowed a claim against JHIL.

H4.8 The letter dated 24 September 2001 has been addressed in chief at JH 14.7. It may further be noted that Mr Cooper wrote contemporaneously to his solicitor stating that:

> Of consideration is the fact that we did not believe that our letter could have been considered as a "claim", rather a provision of information and request for a meeting. We had received your earlier preliminary advice that we had very weak legal grounds upon which to build a case for more funding or related action against JHIL: Ex 327, tab 29, p2.

H4.9 The MRCF submissions contain an elaborate argument to the effect that Mr Macdonald must have received it prior to 5 October 2001: MRCF, 48.36 – 48.45. That argument requires the rejection of Mr Macdonald's direct evidence that Mr Macdonald did not see the letter before he returned to Mission Viejo on 24 October 2001.

H4.10 The MRCF submissions ignore:

(a) the advice sought by the MRCF directors from Mr Bancroft on the afternoon of Wednesday, 26 September 2001 that their interests would not be prejudiced by the sending of the letter: Ex 97;

(b) a response to that email by Ms Hunter of Mallesons appears not to have been made until 5.40pm on Tuesday, 2 October 2001: Ex 97; there is no other documentary evidence before the Commission suggesting an earlier response;

(c) no one on the part of the MRCF has adduced evidence that there was any earlier oral or documentary response from Mallesons;

(d) save for the bare statement by Sir Llew that the letter was sent on 24 September 2001 or a few days later (Ex 13, [147]), there has been a failure on the part of the MRCF and its then solicitors to provide any direct evidence as to when the letter was sent. Sir Llew's unassisted memory is not a reliable basis for making a finding, especially where Mr Macdonald has given direct evidence on the point;

(e) it is inherently plausible that Mr Macdonald would recall when in fact he received the letter, having regard to its nature.

H4.11 Having regard to the importance placed by the MRCF on the letter, the failure to adduce any additional evidence is telling.

H4.12 On that evidence, the Commission can be comfortably satisfied that:

(a) the letter could not have been sent before 27 September 2001; and

(b) the letter did not reach Mr Macdonald until mid or late October, and in any event, it did not reach Mission Viejo on or before Friday, 5 October 2001 (which is the critical date).

Intention or serious contemplation of cancelling the partly paid shares

H4.13 This proposition has already addressed in chief addressed at JH 14.4 and in H2 above in response to the submissions of Counsel Assisting. However, further response to the MRCF submissions on this point is set out below.

H4.14 First, the MRCF has sought to conflate "intention" with "serious contemplation", by inviting the Commission to reject the distinction drawn by Mr Cameron: MRCF, 50.88-89. The MRCF's reason for doing so is said to be that Allens correctly advised on 7 February 2001

that it would be necessary to disclose "potential future course of action". But Allens' advice stated that:

> It is likely that the scheme documents will need to disclose the directors' intentions with respect to JHIL post the reconstruction.

H4.15 What the JHIL Board intended to do was material. What they might have been contemplating, without having yet undertaken the analysis necessary to reach any decision, was not.

H4.16 It may be observed that similar questions arise very regularly in the case of all companies subject to continuous disclosure, and the same result obtains (otherwise, the result would be an inability to conduct any meaningful planning and analysis, and confusion to the market).

H4.17 Secondly, the MRCF conflates the intention of the Board and management of JHIL, as though they are indistinguishable. They are not. Allens' advice of 7 February 2001 focusses on the intentions of the directors.

H4.18 There were differences in view on the Board (as is true of most boards), and differences amongst management and advisers. Very significantly, the JHIL Board would and did reject proposals propounded by management. See JH 14.4.12 in chief.

H4.19 The relevant intention, for the purposes of non-disclosure to the Court, is that of the JHIL Board. The evidence assembled and relied on by the MRCF in support of its contention is, with three exceptions, evidence of JHIL management.

H4.20 The three exceptions are:

(a) a statement by Mr Dan O'Brien in January 2001 (MRCF, 49.4) that he would sooner leave cash, stock or some other sum rather than partly paid shares. This is in the context of the debate as to the mechanism to preserve the rights of creditors of JHIL and does not give rise to an inference that there was an intention to cancel the shares. What is more, Mr O'Brien (and the other BIL nominees) ceased to be a Board member from May 2001, after BIL had sold its shareholding in JHIL;

(b) the advice from Allens dated 7 February 2001 (MRCF, 50.14-18) which referred to the need to disclose the directors' future intentions. This advice is inconsistent with the finding sought by the MRCF;

(c) the Information Memorandum, which was approved by the Board on 23 July 2001: Ex 187, tab 34, p 2-3.

H4.21 Those documents all suggest that the JHIL Board did *not* have an intention to cancel the partly-paid shares at the time of the scheme.

H4.22 As for the intention of JHIL management, see JH 14.4 in chief.

H4.23 Alternatively, the MRCF submits that there was a "serious contemplation" to cancel the partly paid shares.

H4.24 If that were so, then it would be expected that that contemplation would have been revealed in the months leading up to the implementation of the scheme. The difficulty confronting the MRCF here is that there is a lack of any such evidence, and there is the positive evidence of, for example, Mr Cameron that he believed it was not the case: see JH 14.4.5.

H4.25 The MRCF does not make the serious allegation that there was deliberate concealment by JHIL management from their external advisers of an intention: cf JH 14.4.9-10.

H4.26 The difference between the MRCF and James Hardie parties is, at this point, perhaps more apparent than real. It is plain that the cancellation of the partly paid shares was seen, or would have been seen had they turned their mind to the issue, as a possibility - but a possibility as to which there had not been serious consideration or a final decision: cf JH 14.4.11. But the Commission is now apprised of the manner in which JHIL and JHINV engaged in debate, analysis and self-criticism when it was in the process of seriously contemplating a step. That had not occurred.

Perpetual not terminable capital

H4.27 The "perpetual not terminable" submission ignores the inherent susceptibility of capital to be reduced, and the evidence of Mr Peter Cameron that this was obvious (referred to above) and for that reason alone should be rejected. The matters set out in H3 above in response to the Unions' submissions apply here.

H4.28 The MRCF places reliance on the express terms of the partly paid shares in support of the proposition that the references to their being available only in the event and to the extent necessary to avoid the insolvency of JHIL amounted to a representation that they would survive the liquidation or administration of JHIL: MRCF, 50.64, 50.65, 50.67. That is partly true. The partly paid shares were there to preserve the position of creditors. However, they could be cancelled provided the interests of creditors were not prejudiced. That could have occurred in circumstances where it was or was not necessary to provide some other form of funding or security. It does not follow from the fact that the position of creditors was to be preserved that the partly paid shares were held out as perpetual.

H4.29 Further, very clear language would be required to found a representation that these shares were special in that they, unlike all other forms of capital, were not susceptible to reduction. The terms of the shares do not impliedly exclude them from the scope of s256B, nor would any such representation have been conveyed to any informed shareholder or to the Court.

The put option

H4.30 The non-disclosure of the put option was addressed in chief at JH 14.5.

I. Cancellation of the Partly Paid Shares and establishment of the ABN 60 Foundation

I1 Overview – Cancellation of the Partly Paid Shares

I1.1 This subject is addressed in chief by parties as follows:

(a) section 16 of the James Hardie submissions (pp 203 – 215);

(b) section 3, [42] – [77] of Counsel Assisting's submissions (pp 3-13 to 3-25);

(c) chapter 8 of the Unions' submissions (pp 90 – 104); and

(d) section 55 of the MRCF's submissions (pp 455 – 475).

I1.2 There are substantial differences in the submissions made by Counsel Assisting, the MRCF and the Unions. Those submissions range from the relatively measured (from Counsel Assisting) to the extreme (from the MRCF and the Unions). Nevertheless, most of the submissions are fully answered by JHINV / ABN 60's submissions in chief.

I1.3 It is convenient to put submissions in reply by dealing with the various themes that emerge from submissions from other parties. The themes may be identified as follows:

(a) Who is a creditor under s256B of the *Corporations Act*, and who were ABN 60's creditors when the partly paid shares were cancelled?

(b) Were Amaca and Amaba creditors of ABN 60 at the time of cancellation?

(c) Was JHINV a shadow director of ABN 60 in relation to the cancellation?

(d) Did Mr Morley and Mr Salter breach any of the duties that each of them owed under the *Corporations Act*?

(e) Did the cancellation occur to defeat the MRCF's rights upon a winding up?

(f) What are the consequences of any breach of the *Corporations Act*?

I2 Creditors under s256B

I2.1 The Commission has the advantage of a thoughtful memorandum of advice from Mr Archibald QC dated 20 December 2002, which addresses the question of the meaning of the word "creditors" in the context of s256B of the *Corporations Act*: Ex 187, tab 57, p 547. Counsel Assisting suggest that the opinion is likely to be right: CA, Section 3, [45]. The MRCF submit that the opinion is correct: at MRCF, 55.45. There is also the helpful memorandum of advice from Allens dated 31 January 2003, which deals with the subject and which went to the Board of JHINV: Ex 187, tab 57, p 535.

I2.2 Those advices indicate that there was then no authority on the meaning of the word "creditors" in s256B. That is still the case today. Mr Archibald and Allens advised that the

word is likely to be construed in a broad fashion rather than a narrow one. Thus, Mr Archibald concluded that:

> persons who, by reason of prior exposure to asbestos, are reasonably likely to manifest such symptoms at a later time, and who have not instituted a claim or indicated an intention to institute a claim, are also included in that category.

Mr Archibald speaks of "a real likelihood that a prospective liability will be established". He also suggests, correctly, that the matter should be approached in a commercial and realistic way. There is an absence of that in some of the submissions that have been put against ABN 60 and JHINV, as is demonstrated below.

I2.3 Allens' concluded view on this subject, prepared following receipt of Mr Archibald's advice, is set out in its letter of advice to the directors of JHINV dated 31 January 2003: Ex 187, tab 57. That advice includes the following:

> We agree, however, with Mr Archibald that "creditors" is likely to be interpreted broadly when used in s 256B(1), largely for the reasons he gives. In those circumstances, and although no case appears to have gone so far, we think it is likely that a court would hold that "creditors" includes persons who are likely to bring a claim even if those persons cannot be identified and there is only a statistical likelihood of a claim being brought.
>
> On this broad interpretation, we think that pre-1937 claimants should be included as creditors. We think it is sufficiently certain that there will be claimants in this class whose claims succeed to justify taking that approach. Consequently, the directors need to make an assessment of the value of those claims and should ensure that ABN 60 retains sufficient assets to meet them.
>
> The advice that ABN 60 has received from us is that it is more likely than not that claims arising out of the events of the 1970s and 1980s, if they are brought, will fail. In those circumstances, we think the better view is that the relevant claimants are not "creditors".
>
> Although, as we have said, there are some statements which suggest that a lower threshold may be applicable, none of those statements has been made in a context which addresses the question whether a greater than 50% chance of success is necessary. Rather, they have been made in a context where the expectation is that a claim by an identifiable person will be made and will succeed. In our view, it is not consistent with the purpose of s 256B to require a company to consider a claim and make some allowance for it where the expectation is that it will fail. To require a company to do that would be to require the company to disregard what would be in the interests of shareholders in favour of persons who are not expected to exist.
>
> Notwithstanding the views that we have expressed, there remains a real risk that a court will reach the opposite conclusion. Obviously, that risk could be reduced if ABN 60 retains sufficient capital to satisfy those claims or has adequate insurance coverage from a well rated insurer.
>
> The most conservative approach would be to attempt to quantify the liability of Amaca and Amaba for post mid-1970s claims and to assume that those claims will also succeed against

ABN 60, applying appropriate discounts having regard to factors such as the apportionment of responsibility between Amaca and Amaba on the one hand and ABN 60 on the other. However, we think the better approach would be to limit the analysis to claims that might be brought by employees.

I2.4 ABN 60 and JHINV followed the advice of Allens.

I2.5 The MRCF's submissions at Part D include an analysis of the meaning of the word "creditors" in the content of various parts of the *Corporations Act*. The MRCF submits, in short, that the "vast bulk" of the companies' estimated liabilities fall into the category of "expected debts": MRCF, [64.11]. The MRCF submits, in effect, that an expected creditor is relevantly a creditor, at least in the context of those parts of the *Corporations Act* concerned with company administration.

I2.6 Furthermore, in proceedings on foot before the Supreme Court, the directors of the MRCF are contending that those persons who have been exposed to asbestos in the past but have not yet contracted an asbestos disease are not creditors under the *Corporations Act* for the purposes of determining who can prove in a winding up. That narrow approach to the meaning of the word might in due course be accepted as the correct meaning of the word in s256B of the *Corporations Act*.

I2.7 This also highlights the point that the word “creditors” may mean different things in different sections of the *Corporations Act*. Throughout the submissions put against JHINV/ABN 60, it is apparently assumed that for all purposes "expected debts" give rise to creditors, whose interests must be taken into account. The MRCF's submissions in Part D show that that assumption is likely to be incorrect.

I3 Were Amaca and Amaba creditors of ABN 60?

I3.1 In relation to whether Amaca and Amaba were creditors of ABN 60, Counsel Assisting suggests that the real question appears to be whether Amaca and Amaba could be viewed as being reasonably likely to have a claim or claims against ABN 60: CA, Section 3, [47]. They suggest that the answer appears to be yes. For the reasons provided in detail in the submissions in chief and by these submissions generally, it is submitted that, even after all of the evidence from the Commission has been considered, the better view is that the MRCF and its subsidiaries are not now, and were not on 15 March 2003, creditors of ABN 60.

I3.2 Of course, one should approach the question in a commercial and realistic way. That requires some attempt to place oneself in the position of ABN 60 and JHINV as at 15 March 2003. At that time, both companies had been given advice by Allens that “we think it will be very difficult for the directors to establish that they or Amaca or Amaba have a right to a substantial remedy”: Ex 187, tab 57, p 559. It is submitted that that advice was and is correct.

I3.3 The submission, made most strongly and repeatedly by the MRCF, that, prior to 15 March 2003, the MRCF had foreshadowed a $200 million law suit against ABN 60 is inconsistent with the evidence. The MRCF was not as strident in March 2003 as it is now and the MRCF's submissions incorrectly project their current position to an earlier point in time.

I3.4 The MRCF submits (MRCF, 59.55) that the probability of legal action emerges from the formal last paragraph of the letter dated 10 February 2003 from Amaca to Mr Macdonald (Ex 3, vol 1, tab 13) which reads:

> This letter has been considered by and has the complete support of the Amaca Board and we believe that there is an opportunity to positively address this situation should the directors of James Hardie acknowledge the position and take fast and responsible action accordingly.

This is put as the high point of the so-called claim by the MRCF: MRCF, 59.55. But it is no assertion of a legal entitlement. The communications from the MRCF are consistent with an appeal for more money on moral and not legal grounds. All of the JHINV executives who were involved in communications with the MRCF maintained in their evidence that the MRCF was pressing a moral claim and not a legal one. Whatever view might ultimately prevail on the proper construction of s256B, one can be sure that a person owed no more than a moral debt is not a creditor at law.

I3.5 It is also appropriate to re-emphasise that, as at March 2003, the MRCF's own legal advice was that it did not have a valid claim against ABN 60. On 31 March 2003, Mr Farlie from Mallesons Stephen Jaques reconfirmed that, in his view and in the opinion of Mr Walker SC, Amaca and Amaba did not have the basis to claim for damages: Ex 297, tab 14. His advice was that the remedy for the directors was not to bring a claim but to resign. They chose not to follow that advice.

I3.6 In circumstances where:

(a) ABN 60 and JHINV had legal advice that Amaca and Amaba did not have a compensable claim;

(b) none of the correspondence or communications from the MRCF prior to 15 March 2003 asserted a legal entitlement to damages; and

(c) Amaca's own advisors were given unqualified advice that there was no entitlement to damages,

it lacks substance for the MRCF (or for the Unions) now to submit that it should have been obvious to the officers of ABN 60 and JHINV that Amaca and Amaba had a claim and that they conducted themselves so as deliberately to defeat that claim. Once this thread of the MRCF's analysis of the events from March 2003 is exposed as wrong, the whole of the analysis begins quickly to fall apart, as is demonstrated below.

I3.7 Nor does the fact that the MRCF's grievances had not been fully ventilated mean that the MRCF was a contingent creditor, as is apparently suggested in the Union's submissions: Unions 8.9. As at 15 March 2003, Amaca and Amaba either had then a complete claim or they did not; there was no trigger that was necessary to give rise to a present liability.

I3.8 Save for the obligations under the DOCI, neither Amaca nor Amaba was a creditor (contingent or otherwise) of ABN 60 as at 15 March 2003. At the very least, the directors of JHINV and ABN 60, acting commercially and realistically, were entitled to conclude that Amaca and Amaba were not creditors of ABN 60 when the partly paid shares were cancelled.

I3.9 Whatever be the proper construction of s256B in the context of the cancellation of partly paid shares where no specific consideration is identified and passes to the shareholder, the directors of ABN 60 and JHINV did address the question whether the reduction materially prejudiced JHIL's ability to pay its creditors. On one view that was more than they were required to do at law.

I3.10 The MRCF assert that it was false to say that the shares were cancelled for no consideration: MRCF, 55.28ff. The submission that is made by the MRCF is that extinguishment of liability under the partly paid shares was consideration and that is required by the scheme of Ch 2J of the *Corporations Act*. Section 256C(2) provides:

> If the reduction is a selective reduction, it must be approved by either:
>
> (a) a special resolution passed at a general meeting of the company, with no votes being cast in favour of the resolution by any person who is to receive consideration as part of the reduction or whose liability to pay amounts unpaid on shares is to be reduced, or by their associates; or
>
> (b) a resolution agreed to, at a general meeting, by all ordinary shareholders.
>
> If the reduction involves the cancellation of shares, the reduction must also be approved by a special resolution passed at a meeting of the shareholders whose shares are to be cancelled.

I3.11 The word "or" in part (a) appears to indicate that what is contemplated is that a reduction of liability to pay amounts unpaid on shares is not the same thing as receiving consideration. There would be no need for the reference to the reduction of liability to pay amounts unpaid if that constituted the receipt of consideration. The scheme of Ch 2J contemplates that capital might be reduced by cancelling uncalled capital and that this may occur without the passing of consideration.

I3.12 The MRCF also submits that JHINV executives deliberately withheld Allens' advice of 31 January 2003 concerning the prospects of a suit from Amaca and Amaba from the JHINV Board, on the hypothesis that it may impede the decision to cancel the shares:

MRCF, 55.17. This is speculation that does not withstand any scrutiny. The evidence reveals:

(a) Allens provided two advices dated 31 January 2003. One of them was addressed to the directors of JHINV. It was included in the February and March Board papers. The other was addressed to the management of ABN 60 and JHINV. It was not included in the Board papers: Ex 76, tabs 159 and 160.

(b) The advice provided to the Board referred to the other advice. It was identified clearly and it was hardly "obscure", as suggested by the MRCF.

(c) Mr Morley's evidence was that he has a recollection, albeit only a vague one, that Mr Macdonald spoke to the Board about Allens' advice concerning the position of the MRCF: T2049.45.

(d) Mr McGregor's evidence was that the substance of the advice was communicated to the directors: T1522.14.

(e) The minutes of the meeting held on 12 February 2003 indicate that Mr Robb joined the meeting and that:

> Mr Macdonald discussed recent communications with the [MRCF]. The board discussed each of the issues associated with a transfer of ABN 60 and the cancellation of the partly paid shares: Ex 121, tab 135, p 3241.

It is likely that Allens' advice was discussed in this context.

(f) When the Allens' advice of 31 January 2003 concerning the MRCF was circulated to various Board members on 28 March 2003 (Sydney time), there was apparently no sense of shock or concern that the advice had been withheld from the Board up to that point in time. That is most likely to be because the content of the advice had already been made known to the board members earlier, at least orally.

The submission that the advice was deliberately withheld by JHINV executives from the JHINV Board is unfair and should be rejected.

I3.13 Amaca was not turned into a creditor merely because it could have a claim against ABN 60. A person is not a creditor merely because he or she has a "potential claim", to use Counsel Assisting's language at CA, Section 3, [72].

I4 Was JHINV a shadow director of ABN 60?

I4.1 The submission that JHINV was relevantly a shadow director of ABN 60 should also be rejected. In order for the submission to succeed, it would be necessary to show that the *locus* of ABN 60's effective decision making, in relation to the cancellation, lay with JHINV and that Mr Morley and Mr Salter, in their capacity as directors, merely danced to JHINV's tune or simply accepted the decisions which had effectively been made by JHINV: see *Standard Chartered Bank of Australia Ltd v Antico* (1995) 38 NSWLR 290 at 328.

I4.2 A holding company is not a director of its subsidiaries merely because it has control of how the boards of its subsidiaries are constituted: *Standard Chartered Bank v Antico* (at 327). Nor does a parent company become a shadow director merely because it asks a subsidiary to do something and the subsidiary does it. If the subsidiary simply accepts the decision made by the parent and does what is asked without making a separate decision, then the parent may well be a shadow director. But if the subsidiary makes up its own mind to agree to the request, then the parent is not relevantly a shadow director.

I4.3 The critical question on which to focus in the present case is whether the actual decision made by the directors of ABN 60 on 15 March 2003 to cancel the partly paid shares was made not by Mr Morley and Mr Salter in their capacity as directors of ABN 60 but was in truth made by JHINV. The submissions put against JHINV and ABN 60 tend to focus on evidence that was given in relation to the period leading up to that day and overlooks the firm evidence given by Mr Morley and Mr Salter about the actual decision to cancel.

I4.4 Mr Morley and Mr Slater were firm in their evidence that at the time of cancellation, each of them considered that they were free to make and did make a decision as directors of ABN 60: T1932.50; T1997.31; T1942.37 (Mr Salter); T2052.36; T2118.17; T2119.54 (Mr Morley); see JH 16.3.32 - 16.3.34. It is unfair to take some of Mr Salter's answers to very general questions, and concerning other points in time (eg T1926.27-.30) to suggest that he simply followed the instructions of JHINV. His evidence on the critical question was firm.

I4.5 The Commission should not find that JHINV was a shadow director of ABN 60.

I5 Did Mr Morley and Mr Salter breach any duties?

I5.1 Counsel Assisting points out that Mr Wilkinson concludes that as at June 2003, Amaca had discounted liabilities in respect of the *Wren* period of $125.7 million net, of which $1.5 million related to workers' compensation claims: CA, Section 3, [46]. They submit that those liabilities may effectively be considered to be liabilities of ABN 60 on the basis of Allens' advice. The reference they give is to the draft advice from Watson Mangioni (which does refer to an Allens' advice). Any contention that Mr Morley did not follow the advice that had been provided by Allens is wrong. Allens' concluded views on this subject, prepared following receipt of Mr Archibald's advice, are set out in its letter of advice to the directors of JHINV dated 31 January 2003: Ex 187, tab 57. Relevant parts of that advice are set out above.

I5.2 Mr Morley followed the advice given by Allens. His calculations, which are suggested now by some to be a farce and a sham, estimated the relevant liabilities to be up to $10.753 million: Ex 121, [317]. The issue has now been addressed by an actuary, whose conclusion is that the relevant figure is $1.5 million. That serves to demonstrate and confirm the extremely conservative way in which Mr Morley approached the exercise of

calculating ABN 60's exposure to creditors. In calculating the liability of ABN 60 in respect of workers' compensation claims, Mr Morley was conservative at every step, including doubling estimates "for conservatism": Ex 121, [317(b)].

I5.3 Counsel Assisting submit that s181(1) of the *Corporations Act* may be breached by conduct which, viewed objectively, was not in the best interests of the corporation as a whole, even if the director who engaged in that conduct honestly believed that it was: at CA, Section 3, [58]. That does not correctly state the effect of s181(1). The obligation is to exercise powers and discharge duties "in good faith in the best interests of the corporation". Counsel Assisting's formulation omits the words "good faith", which are at the heart of s181(1). There must be an absence of good faith in order for there to be a contravention of the section.

I5.4 It is also critical that the constitution of ABN 60 provided that:

> If the Company is a wholly owned subsidiary of another company, the directors of the Company may, whilst it is a wholly owned subsidiary, act in the best interests of such holding company: Ex 187, tab 77, p852.

This meant the directors of ABN 60 were taken to act in good faith in the best interests of ABN 60 even though they were acting in the interests of the parent, provided ABN 60 was not insolvent at the time the directors act and does not become insolvent because of the directors' act: s187 of the *Corporations Act*. No-one appears to submit that ABN 60 was insolvent on 15 March 2003, or became insolvent because of the cancellation. For the reasons put by the MRCF in section 64, it could not correctly be submitted that ABN 60 was insolvent. For this reason, the suggestion that Mr Morley and Mr Salter acted in contravention of s181 of the *Corporations Act* is misconceived. The MRCF elsewhere describes the s187 protection as "failsafe": MRCF, 35.32.

I5.5 The argument that Mr Morley may have acted in contravention of ss180 and 181 of the *Corporations Act* in failing to obtain an independent actuary report loses its force once it is appreciated that Mr Morley's calculations were so conservative that his estimate of liability vastly exceeded what is now shown to be an appropriate forecast by Mr Wilkinson.
Mr Morley was within his rights to take the actuarial information that he had, which by then was nearly 3 years old and to take account of more recent information from Mr Cooper and Mr Attrill (Ex 121, tab 143) and then adopt a series of conservative assumptions in order safely to estimate the likely high side of the amount owed by ABN 60 to its creditors. His efforts have been shown to have been successful.

I5.6 The suggestion that Mr Morley did not seek more specific information from the MRCF because he did not want to tip them off about the cancellation (MRCF submissions at 55.34, 55.36-55.37) ignores the fact that that the MRCF knew all about the proposed cancellation: see JH 16.3.37.

I5.7 Mr Morley's calculations were not absurd, as contended by the MRCF at 55.35. They were sophisticated and thoughtful. Indeed, in another context, the MRCF described the analysis as thorough, discussed with some external authorities as a check and fully disclosed to the Boards of both ABN 60 and JHINV: MRCF, 58.22. The calculations did include an arithmetical error (of no consequence) and there were undoubtedly other ways of going about the analysis. Mr Morley admitted that the analysis could have been done differently. Those admissions are to his credit. But critically, Mr Morley stood by his calculations as a bona fide attempt by him to calculate the liability of ABN 60 to its creditors. His evidence should be accepted.

I5.8 Mr Morley gave close consideration to identifying the creditors of ABN 60. He did this on advice from Mr Archibald, Allens and Watson Magnioni about the question of whether a reduction of capital materially prejudiced the company's ability to pay its creditors within the meaning of s256B of the *Corporations Act*. A creditor on 15 March 2003 included persons who could reasonably be expected to have a valid claim against ABN 60. For the reasons given above, Amaca was not a creditor of ABN 60 (apart from the debt due under the DOCI). The directors of ABN 60 had no duty to consider the interests of persons who were not creditors, and indeed having regard to the interests of persons other than creditors could put them in breach of their duties.

I5.9 It is important to recognise that the inquiry that is made in the context of s256B(1)(b) of the *Corporations Act* is not identical to the inquiry that must be made in relation to creditors under s181. This point is recognised at paragraph 23 of Mr Archibald's opinion: Ex 187, tab 53, p 527. The directors of ABN 60 had a duty to consider the interests of creditors and to avoid action contrary to their interests where ABN 60 was insolvent or nearing insolvency, or where a course of action would jeopardise its solvency: *Nicholson v Permakraft (NZ) Ltd (in liq)* [1985] 1 NZLR 242; *Kinsela v Russell Kinsela Pty Ltd (in liq)* (1986) 4 NSWLR 722. In *Kinsela*, Street CJ also relevantly stated (at 733):

> Courts have traditionally and properly been cautious indeed in entering boardrooms and pronouncing upon the commercial justification of particular executive decisions.

That is a word of caution that should be given full weight in the context of the present Inquiry.

I5.10 If MRCF's submissions to the Court of Appeal made on 23 July 2004 are correct, then the future sufferers of asbestos disease are not creditors of Amaca or Amaba for the purposes of considering the solvency of those companies. It likewise must follow that the same persons were not creditors of ABN 60 in March 2003. And for the reasons given above, the MRCF was not a creditor either.

I5.11 As noted above, it is neither fair nor correct, having regard to the evidence as a whole, to conclude that Mr Salter simply accepted what was put to him by JHINV (see CA, Section 3, [75]). Mr Salter did not undertake all of the analysis that was undertaken by Mr Morley and

was not as close to the detail. But that does not mean that he was in breach of any duty. Mr Salter studied the relevant documents and turned his own mind to Mr Morley's calculations and to the documents relevant to the decision: see JH 16.3.30. That was sufficient to discharge fully his duties as a director of ABN 60.

I6 Was the cancellation intended to defeat the MRCF as a creditor?

I6.1 This submission, which is propounded by the MRCF from 55.21, fails at the outset because the MRCF was not and was not considered to be a creditor.

I6.2 The MRCF persist in the assertion that ABN 60 and JHIL kept the cancellation a secret: 55.55-55.56. Moreover, it submits that the secrecy bespeaks a design to prejudice the interests of creditors. The notion that the cancellation was a secret is another thread that underpins much of the MRCF's analysis of the events from March 2003. It is a notion that has been debunked. As JHINV and ABN 60's submissions in chief show, the MRCF was told in writing on more than one occasion about the proposal to cancel the partly paid shares. It was told that the cancellation had occurred immediately after the shares were cancelled: JH, 16.3.17, 16.3.36-16.3.37.

I6.3 In any event, it is wrong to think that the cancellation of the partly paid shares could be kept secret. ABN 60 was required to notify ASIC of the alteration to its share capital and did so: Ex 297, tab 13(20). Anyone conducting a company search of ABN 60 would immediately become aware of the cancellation. In light of the evidence, it is both striking and telling that the MRCF can now submit that it was unaware of the cancellation. It substantially undermines the reliability of the MRCF's submissions.

I6.4 The Unions make the same error. They too submit that the cancellation was to be kept secret "at all costs": Unions, 8.38(d). That secrecy is said to give rise "a flagrant breach" of director's duties and conduct that was "heinous in its disregard for the legitimate interests of a significant class of persons (many of whom are as yet undiagnosed) who have contracted asbestos related diseases through the negligence of James Hardie": Unions, 8.41. Those submissions are far removed from reality. They are serious allegations that should not have been made. The Union's submissions do not trouble with the clear evidence that the MRCF was aware of the proposed cancellation. Rather, the submissions essentially rest upon the email from Mr Macdonald of 18 March 2003 ("No communication with the MRCF for now"): Ex 122, tab 26. When placed in context, the email is shown to be completely innocent: see JH, 17.1.3. Nor do the Union's submissions trouble to explain how ABN 60, as opposed to Amaca and Amaba, is liable to those who suffer asbestos related disease. They simply refer generically to "the negligence of James Hardie".

I6.5 It is also unfair to submit that the decision in relation to the cancellation of the shares "appeared to attract minimal consideration on the part of [JHINV's] board": Unions, 8.42. The Board was provided with detailed papers concerning the cancellation and the subject

was discussed by the Board at meetings on 12 February 2003 and 11 March 2003 and by a Board Committee on 14 March 2003: Ex 122, tabs 135-139. In any event, the decision to cancel the shares was taken by Mr Morley and Mr Salter as directors of ABN 60, as described above.

I7 Remedy

I7.1 All of the submissions put against ABN 60 and JHINV are lacking in any detail on the question of remedy.

I7.2 Counsel Assisting and the Unions submit that the alleged breaches, or alleged arguable breaches, would give rise to an order for compensation in favour of ABN 60 under s1317H(1) of the *Corporations Act*: CA, Section 3, [76]; Unions 8.28.

I7.3 Counsel Assisting suggest that damage would arise if a claim were made against ABN 60 which it could not meet but which could have been met had the partly paid shares not been cancelled. That submission appears to recognise that damage has not yet arisen. It may never arise. If one were today to try to estimate the potential damage, one would have to undertake the kind of analysis that Mr Morley conducted in March 2003. It is by no means clear that the analysis today would produce a different result.

I7.4 The Unions also submit that the sanctioning and orchestration of the cancellation was unconscionable conduct on the part of JHIL, its directors and advisors and by JHINV and its directors and advisors: Unions, 8.44-8.45. This imprecise and broad-sweeping assertion appears primarily to rest on the alleged secrecy of the cancellation. As has been noted, the alleged secrecy is a myth. The Unions submit that all the persons identified are liable to "persons aggrieved" and the amount of the liability is no less than that recoverable as a consequence of the events of February 2001 concerning the establishment of the MRCF and the alleged consequent misleading of the Supreme Court: Unions, 8.47. This is mere assertion. There is no attempt to analyse the alleged liability.

I7.5 The MRCF submits that ABN 60 is entitled to an order under s1324(1) of the *Corporations Act* reinstating the partly paid shares: MRCF, 55.60. Presumably, the argument is that JHINV had engaged in a contravention of the civil penalty provisions of the *Corporations Act* and it should be ordered to take such steps as are required to reinstate the partly paid shares. The submission is contrary to authority. *Re Mesenberg v Cord Industrial Recruiters Pty Ltd* (1996) 39 NSWLR 128 is authority for the proposition that s1324 is not available in respect of breaches of the civil penalty provisions of the *Corporations Act*. Even if that decision is wrong, there is a vast array of complex issues that would need to be addressed by a Court before an order was made under s1324(1).

I7.6 The MRCF also submits that the transaction is an "uncommercial transaction" within the meaning of s588FB and will be an insolvent transaction if and when ABN 60 "is unable to meet a judgment against or proceedings brought by Amaca or Amaba": MRCF 55.60. The

MRCF submit that the transaction is voidable at the suit of a liquidator of ABN 60, under s588FF: MRCF, 55.60. These submissions do not provide any detailed analysis of the alleged prospective operation of Pt 5.7B of the *Corporations Act*. This is something that would require careful attention before any conclusion could be drawn that the cancellation is liable to be avoided. For instance, it is not correct to say that s588FF gives to a liquidator the right to avoid a transaction. Rather, it gives to the liquidator the right to apply to the Court for orders. Many considerations (including discretionary considerations) would come into play on such an application.

I8 Overview – Establishment of the ABN 60 Foundation

I8.1 The circumstances surrounding the creation of the ABN 60 Foundation are not included in Counsel Assisting's List of Issues (save in so far as the cancellation of the partly paid shares is part of the creation of the Foundation). Only two parties address the subject in their submissions. Section 17 of the submissions of ABN 60 and JHINV sets out a narrative of the events concerning the formation of the ABN 60 Foundation and the execution of the DOCIA. Chapter X of the MRCF's submissions concerns the ABN 60 separation. The MRCF make a series of serious allegations about the conduct of various persons, which when considered are shown to be without merit.

I8.2 Section 56 of the MRCF's submissions is introductory. It seeks to draw some parallels between the establishment of the MRCF Foundation and the ABN 60 Foundation. There are some parallels: technically, there were similarities between the two transactions and so parallels are to be expected. But in many ways they differ. The transactions need to be considered separately on their merits. When that is done, the alleged parallel deeds of misconduct are shown to be wrong.

I8.3 Chapters 57 to 59 of the MRCF's submissions address the position of the outgoing directors and the execution of the DOCIA, the ABN 60 separation from the perspective of the JHINV Board and dealings with the incoming directors. These subjects can be addressed in turn.

I9 The outgoing directors and the DOCIA

I9.1 The MRCF alleges that Mr Morley and Mr Salter breached their duties to ABN 60 as directors, in various respects, at the time of entry into the DOCIA and at the separation of ABN 60.

I9.2 There are at least three important general criticisms of the MRCF's analysis that serve to undermine that analysis.

I9.3 First, the MRCF substantially overstates that nature of the MRCF's so-called "claim" as at March 2003. The MRCF's submissions speak of:

> a potential claim against ABN 60 of perhaps $250m on the horizon.

In MRCF's submissions dealing with the establishment of the MRCF Foundation (esp 39.43 to 39.45), there is no attempt to identify how any potential claim may be formulated in terms of remedy or relief: see B13.2 above. The submission above substantially overstates the nature of the communications between the MRCF and JHINV in the period up to March 2003. On the very day that the DOCIA was executed, the MRCF was given legal advice that it had no legal basis for a claim: Ex 297, tab 14. The conduct of Mr Morley and Mr Salter is judged by the MRCF against a claim that had not been put.

I9.4 Secondly, Mr Morley and Mr Salter were authorised under the ABN 60 constitution to act in the best interests of its holding company: Ex 1, tab 65.

I9.5 Thirdly, the MRCF does not give full play to the fact that, up to 17 March 2003, there had been substantial negotiations between the MRCF and JHINV and ABN 60 about the transfer of ABN 60 to Amaca and the negotiations were on the cusp of success. The chronology is considered in the submissions in chief in section 16. Those negotiations included the terms of a DOCIA. The transaction had reached the point where Allens was able to provide to Mallesons a bundle of documents for completion. Those documents indicated that some of the steps had already been taken (including the cancellation of the partly paid shares) and completion of the remaining steps was thought to be imminent: Ex 297, tab 13.

I9.6 The fact that Amaca and Amaba were aware of the cancellation of the partly paid shares and were aware of the terms of a proposed DOCIA between JHINV and ABN 60, but did not then make any application to prevent or unwind the cancellation serves, to confirm that the MRCF did not believe that it had a claim against ABN 60 and did not say to ABN 60 or JHINV that it had a claim. If the MRCF's submissions which are now made are accepted, the conduct of the directors of Amaca and Amaba in March 2003 was deficient.

I9.7 The negotiations with the MRCF had reached the stage where two DOCIA's were contemplated. One was between JHINV and Amaca and Amaba. The other was between JHINV and ABN 60. Both documents were forwarded to the solicitors for MRCF: Ex 187, tab 62. Plainly, no promises were being contemplated as between Amaca and ABN 60; there wa,s for instance, no covenant not to sue. When the MRCF pulled out unexpectedly at the last minute, JHINV and ABN 60 intended to proceed by executing a DOCIA that relevantly gave to ABN 60 the benefits that had been negotiated by the MRCF. That was raised expressly between Mr Shafron and Mr Morley: Ex 76, [22]. Thus, the DOCIA as executed was based on a document that had been produced by an arms length negotiation and was not worse for ABN 60 than the agreement that ABN 60 was expecting to enter into at the date the partly paid shares were cancelled (see, in particular, the form of the indemnity at Ex 187, tab 62, p 644).

I9.8 It may have been sensible for Mr Morley and Mr Salter to have insisted that the cancellation of the partly paid shares were contractually interdependent: MRCF, 57.31.

The transactions were not legally interdependent in the sense that the cancellation was conditional as a matter of contract on execution of the DOCIA. But, in commercial terms, the transactions were interdependent. As at the date of cancellation, a DOCIA was in what was thought to be final or very close to final form and Mr Morley and Mr Salter fully expected and trusted JHINV to enter into the DOCIA. The precise form of the DOCIA had to change following the departure of the MRCF from the transaction, but the DOCIA as ultimately executed was in substance the same as the DOCIA contemplated as at 15 March 2003 (save for the error that was later the subject of the deed of rectification). Mr Morley's and Mr Salter's trust in JHINV was well-placed. Indeed, it would have been a breach of the trust for Mr Morley and Mr Salter to seek to negotiate more from the DOCIA than had been in contemplation when the partly paid shares were cancelled, which is what the MRCF says should have occurred: eg at MRCF, 57.30.

I9.9 As a stand alone transaction, the DOCIA plainly provided a substantial commercial benefit to ABN 60. It received a covenant not to sue and an indemnity in respect of real matters, which it did not previously have: T1949.20. It is hard to understand the submission that the directors did nothing to protect creditors in respect of non-asbestos liabilities when those are the very thing covered by the indemnity: see MRCF, 55.28.

I9.10 When the partly paid shares were cancelled, it was not contemplated by anyone (including the MRCF) that ABN 60 would get an indemnity from JHINV in respect of claims by Amaca or Amaba. The thinking in relation to that matter has been addressed above: in short the view legitimately taken was that the MRCF had no compensable claim. Mr Salter's evidence was that (T1997.37):

> We believed that we'd identified all the prospective creditors, I believed we'd gone through all the necessary steps to investigate what had needed to be investigated.

Mr Salter is not in breach of his directors duties merely because he left some of the detailed investigations to Mr Morley.

I9.11 The MRCF also criticise Mr Morley and Mr Salter in relation to the carve out for the cancellation of the partly paid shares, so that JHINV does not indemnify ABN 60 for liabilities associated with the carve out: MRCF [57.40]-[57.41]. The puzzling thing about this submission is that the MRCF does not submit that ABN 60 has a liability in respect of the cancellation. Rather, the submission is that other persons are liable to ABN 60: see MRCF, 55.58-55.59. That means that the carve out appears to have no practical significance whatsoever.

I9.12 Once all of these matters are appreciated, it should be concluded that the alleged contraventions of the Corporations Act lack substance: MRCF, 57.63-57.66.

I9.13 The MRCF's submissions under the heading "causation" (at 57.67-57.70) suffer the same problems as the submissions at [55.60], which are addressed above.

I9.14 Finally, in relation to this matter, the MRCF submit that Mr Morley and Mr Salter breached their directors' duties in relation to "the little reduction of capital": MRCF, 57.72-57.75. It is suggested that the matter "has largely gone unnoticed in the course of the evidence". That is perhaps code for a concession that it was not the subject of cross-examination. Mr Morley dealt with it, albeit briefly, in his evidence at Ex 121, [329]. The relevant minutes of the meeting of directors of ABN 60 explain the consideration given to the issue by directors and, certainly in the absence of any testing, the minutes should be accepted at face value: Ex 122, tab 45, p 330. It was in this context that Mr Morley reconsidered his quantification of the workers compensation claims and provided a memorandum to Mr Salter: Ex 121, tab 150. For the reasons given in that evidence, the capital reduction was authorised by s256B of the *Corporations Act*.

I10 The perspective of the JHINV Board

I10.1 The MRCF submit that senior executive management deliberately withheld information from the full JHINV Board. The non-disclosed matters are said to be the warnings from Allens that the cancellation of the partly paid shares may raise the question whether JHINV had misled shareholders and the Supreme Court at the time of the scheme of arrangement and "the substance and urgency of the current dispute with the MRCF": MRCF, 58.2. These submissions can be disposed of quickly – they suffer the same underlying flaws that have already been addressed above.

I10.2 The first alleged non-disclosed matter (the warnings from Allens), is not taken up in the MRCF's detailed submissions. Thus, the MRCF does not identify the particular warnings and does not identify when the warnings were communicated to senior executives. Without those particulars, the allegation (which is tantamount to an allegation of fraud) should not be countenanced.

I10.3 The second alleged non-disclosed matter (the claim by the MRCF) suffers from the fatal flaws that:

(a) it substantially overstates the effect of the communications from the MRCF (see paragraph I3.4 above); and

(b) it assumes, contrary to the fact, that the substance of Allen's advice of 31 January 2003 concerning the MRCF was not brought to the attention of the Board (see paragraph I3.12 above).

I10.4 Contrary to the submission of the MRCF at 58.17, the evidence firmly indicates that:

(a) the Board was kept informed about the communications from the MRCF. In particular, the subject was discussed at the 12 February and 11 March 2003 meetings (which were attended by Mr Gillfillan): Ex 121, tab 135, p 3241; tab 138, p 3408

(b) at least the substance of Allen's advice of 31 January 2003 was disclosed to the Board; and

(c) Mr Morley discussed his quantification analysis with the Board, particularly with the Board Committee that had been established in relation to this transaction: Ex 121, tab 139.

I10.5 The criticism of Mr Macdonald's oral evidence at MRCF, 58.19-58.23 is not justified. There was no contradiction in the evidence. His position was that, save for the approximately $20 million that was contemplated as being available for the MRCF through ABN 60, he was not prepared to recommend a higher payment. On this, Mr Macdonald was clear and consistent: T2424.58-2425.51.

I10.6 There is one striking submission made by the MRCF that must be separately addressed. In the context of a submission that as at March 2003, the MRCF had foreshadowed a claim of $200 million (which cannot be supported by the evidence), the MRCF submits that JHINV should have asked the MRCF to provide a better indication of its claim, including quantum: 58.23. The MRCF submits that if JHINV had made that inquiry in March 2003, JHINV would have received a letter in terms similar to that received on 18 September 2003. Further, the MRCF submits that the only reason such a letter had not been sent was because the negotiations were then inconclusive. This submission should be firmly rejected. If JHINV had asked the MRCF in March 2003 about the so-called claim, a full and honest answer from the MRCF would have been that the MRCF has received advice from Mallesons and Senior Counsel that the MRCF has no claim against ABN 60. No doubt JHINV would have found some comfort in the fact that Mallesons and Senior Counsel had come to the same conclusion as Allens.

I10.7 The MRCF also allege that JHINV failed to make proper disclosure to the market: MRCF, 58.26ff. The basis for the allegation is that JHINV wanted to keep the cancellation of the partly paid shares and the ABN 60 separation a secret. The first part of this theory has already been addressed in these submissions. As to the ABN 60 separation, the idea that it was a secret is shown to be without basis by the fact that on 2 April 2003, just two days after the separation, JHINV wrote to Amaca and Amaba and told them that the separation had occurred: Ex 7, vol 7, p 73.

I10.8 The MRCF points to the evidence that demonstrates that JHINV gave careful attention to the question of whether JHINV was required to make a disclosure to the market: MRCF, 58.27-58.28. There is no irony in Mr Baxter's conclusion that "separate disclosure of the creation of ABN 60" is not justified, as the MRCF submits at 58.27. Mr Baxter was speaking of disclosure separate from the disclosure of the MRCF Foundation. There is really no basis for suggesting that the consideration given to the question of disclosure lacked bona fides, or was incorrect.

I11 Dealing with incoming directors

I11.1 The heart of this lengthy part of the MRCF's submissions is the allegation that the whole of the conduct of JHINV in relation to the ABN 60 separation constituted a deliberate concealment from the incoming directors of the MRCF's claim, the cancellation of the partly paid shares and the intended operation of the DOCIA: MRCF, 59.19, 59.22. The submissions also return to the theme that JHINV set about to defeat the rights of creditors, particularly the MRCF: 59.21.

I11.2 There is an irony in the submissions put on this topic. It is submitted by the MRCF that in connection with the MRCF Foundation, Mr Cameron was one of the persons who participated in the withholding of information: eg MRCF, 44.11. In the context of the ABN 60 Foundation, Mr Cameron becomes, according to the MRCF, one of the persons duped by JHINV. If the officers of JHINV had behaved as alleged, the last person who would have been selected as a candidate for a directorship of ABN 60 was Mr Cameron.

I11.3 This section of the MRCF's submissions also is very substantially or wholly undermined by overstatement by the MRCF of the nature of the communications between the MRCF and JHINV prior to 31 March 2003. To say that "a very substantial claim was not just possible but probable" is a significant overstatement: MRCF, 59.45. The objective evidence concerning the communications indicates that the way the position was put by Mr McGregor to Mr Macphillamy (Ex 273, [12]):

> although no threat to commence proceedings had been made at that time, it was possible that the Medical Research & Compensation Foundation's claims would subsequently develop into legal action.

This is a fair statement of the position. A fair reading of the MRCF's letter of 10 February 2003 goes no further: Ex 3, vol 1 tab 13. Moreover, once a realistic approach is taken to the communications, the evidence of Mr McGregor and Mr Macphillamy can be reconciled.

I11.4 The MRCF also makes unsustainable submissions in this regard concerning the communications between Mr Robb and the incoming directors: MRCF, 59.38ff. Mr Robb and Mr Blanchard met with Mr Don Cameron and Mr Macphillamy on 26 March 2003. Mr Robb reported to Mr Macdonald (copied to Mr Shafron and Mr Morley) by email: Ex 187, tab 74. The MRCF suggests that the terms of the report are remarkable: 59.38. They submit that the report is indicative of "joint thinking". But the inferences that the MRCF would draw are simply not open. The statement that:

> We gave a full description of the transaction (although we did not go into detail on your recent difficulties with the Foundation or the Foundation's concerns about funding promises)

is benign. It indicates that the transaction was fully described, save in one respect where the matter was not addressed in detail, ie only superficially. It is hardly consistent with the suggestion that Mr Robb and Mr Macdonald were employing a deliberate strategy "to tell

them a little and then wait and see what they asked for": MRCF, 55.41. As to the matter where the description was not provided in detail, the explanation given for the omission by Mr Robb was reasonable and plausible. He said he felt it was a matter for his client to raise: T2880.7. That point was confirmed by Mr Macdonald who said he had felt it was a matter best raised by Mr McGregor, Mr Morley and Mr Shafron and had instructed them to do so: T2450.32-55. That is also how Mr Shafron reads the email: T1399.10. Read as a communication between honest men, as it should be read, Mr Robb's email is clearly putting Mr Macdonald on notice that there is an outstanding matter that should be taken up with the directors.

I11.5 On Sunday 30 March 2003, Mr Robb made an email inquiry of Mr Macdonald about Mr McGregor's conversation with Mr Macphillamy: Ex 187, tab 87. It is apparent that Mr Robb was told of the conversation before he sent his email. It is likely that he was told that Mr McGregor would provide the additional commercial information that needed to be brought to the attention of the incoming directors. Mr Macdonald later informed Mr Robb that (Ex 187, tab 87):

> Alan says John is aware of the background of both Foundations and is fine with that.

Once again, read as a communication between honest men, as it should be, the email is perfectly adequate to convey the fact that Mr McGregor had provided to Mr Macphillamy a fair and accurate description of the matters that were left out by Mr Robb on 26 March 2003. To suggest that the email has a "studied vagueness" is to read far too much into the email. It also ignores the fact that there were telephone communications as well as email communications and brief email communications often convey more than is apparent without the oral context.

I11.6 The MRCF also submit that Mr Shafron misled the incoming directors in relation to insurance: MRCF, 59.67-59.73. This submission is really an after-thought. It was not taken up in the evidence. It seems to rest on the premise that Mr Shafron would anticipate that Mr Stevenson would not adequately undertake his retainer. In the circumstances, this submission should be ignored.

I11.7 In then end, the MRCF's submissions fail because they involve the proposition that Mr Macdonald, Mr Shafron, Mr McGregor and Mr Robb failed to inform the incoming directors of a probable claim by the MRCF in the amount of some $200m. It is true that no such statement was made. That was because none of them, reasonably, believed that to be the fact.

I11.8 The next so-called species of misleading conduct concerns information about the cancellation of the partly-paid shares: MRCF, 59.77-59.105. The MRCF submits that information about the cancellation of the partly paid shares was kept from Mr Macphillamy, Mr Cameron and their solicitor, Mr Stevenson. That is incorrect:

(a) Ms Saltos' note of the meeting involving Mr Macphillamy, Mr Stevenson, Mr Donavan, Mr Robb, Mr Blanchard and Ms Saltos (Ex 124) notes: "ABN 60 has undertaken a reduction of K partly paid share". Plainly, the subject was expressly raised at the meeting, almost certainly by Mr Robb.

(b) There is a reference to the cancellation of the partly paid shares in the draft DOCIA which was provided to Mr Stevenson when he was instructed: Ex 124, tab 2.

(c) One should infer that a description of the cancellation was included in Mr Robb's "full description of the transaction" provided on 26 March 2003 (even if the parties to the conversation cannot specifically recall it): Ex 187, tab 75.

I11.9 There is also in evidence a copy of a special purpose financial report as at 31 March 2003 for ABN 60: Ex 122, tab 152. The report was signed by Mr Cameron on 31 July 2003 and was audited by PwC. The Directors' report records that during the year the company "cancelled its partly paid shares". The cancellation is also identified in note 11 to the accounts. No liability to the MRCF is identified as an actual or contingent liability (apart from the obligations under the DOCI).

I11.10 The evidence does not support a conclusion that the cancellation was kept secret from the incoming directors. Indeed, it is rather strange to suggest that JHINV executives were intent to keep secret things that were inevitably to come to the attention of the incoming directors.

I11.11 The MRCF further submits in this context that JHINV planned to achieve the cancellation independently of but before any separation of ABN 60: 59.80. Once again, the evidence is to the contrary. The negotiations between the MRCF and JHINV and ABN 60 show that cancellation was always a part of a single transaction that included the transfer of control of ABN 60 to Amaca: Ex 297, tabs 10, 12 and 13. At the time of cancellation, the JHINV Board expected the transfer to occur and, if it did not, it contemplated that it would exercise the put option in the DOCI: Ex 122, tab 138.

I11.12 Cancellation was an element of and a step towards separation. The shares were cancelled at a time when it was expected that Amaca would assume control over ABN 60 and in circumstances where Amaca knew all about and were free to scrutinise the proposed cancellation. The MRCF's submissions continually overlook this point and draw inferences that are simply not open: eg MRCF, 59.86. Moreover, when the MRCF walked away from the transaction on 17 March 2003, it was natural for JHINV to consider how separation could otherwise be achieved: cf MRCF, 59.80.

I11.13 It is also unrealistic to suggest that separation could be achieved without cancellation, MRCF, 59.83. If ABN 60 came to be owned outside the JHINV group and the partly paid shares subsisted and were not transferred, ABN 60 could have been used by its new owners to engage in whatever speculative business they cared for with a $1.9 billion lifeline

to bail it out if required. Contrary to the MRCF's submission, the only commercially feasible way to separate without cancellation was by exercising the put. However, Mr Shafron sensibly recommended to the Board that it was not appropriate to put the shares to the MRCF because it could never meet the entire uncalled amount involved: Ex 122, tab 136, p 3247.

I11.14 The third species of alleged misconduct in the dealing with the incoming directors is said to concern the suppression of the view held by some JHINV management that the DOCIA was intended to exclude claims by the MRCF: MRCF, 59.106. The MRCF's theory in this context is particularly farfetched.

I11.15 The precise form of the alleged non-disclosure is peculiar. Why would it matter what the intentions of some managers were? What is important is the terms of the DOCIA, objectively determined. As will be seen, the MRCF is compelled to put the allegation in this rather meaningless way in order to seek to attack the deed of rectification.

I11.16 The MRCF submit that JHINV executives faced a conundrum. The conundrum was said to arise because the existence of the MRCF's claim had been deliberately withheld from the incoming directors but at the same time the executives wished to carve out that kind of claim from the indemnity that was being provided to ABN 60. It has already been shown that the first part of this reasoning is incorrect, which really destroys the whole of the MRCF's analysis. A similar theory is put in relation to the cancellation of the partly paid shares: MRCF, 59.128. It suffers from the same flaw.

I11.17 In any event, the MRCF submits that the conundrum was handled "with the utmost delicacy" by the combined efforts of each of Mr McGregor, Mr Macdonald and Mr Shafron to "try and get past" Mr Stevenson, Mr Macphillamy and Mr Cameron a DOCIA that excluded claims by the MRCF, without any of them noticing: MRCF, 59.110. It is suggested that Mr Robb was knowingly concerned but that he did not understand the way in which he was being controlled: 59.111.

I11.18 The MRCF points to evidence that is said to demonstrate the delicacy of the touch of the JHINV executives, which includes anaesthetising Mr Stevenson: MRCF, 59.134. What the evidence shows is not the kind of scheming and manipulative conduct that is alleged to have occurred. Rather, it shows a few accidental blunders. Even the MRCF cannot resist pointing out one instance where Mr Shafron "misunderstood Mr Macdonald's email", which is hardly consistent with the MRCF's theory of what transpired: MRCF, 59.116. The MRCF refers to Mr Macdonald's statement (at Ex 189, p728) that:

> I guess JHINV's directors would want to be working with ABN 60'2 directors to properly demonstrate that the decision to cancel the partly paids was properly made.

The MRCF seeks to cast this as a momentary acquisition of conscience on the part of Mr Macdonald: [59.115]. It should be seen for what it is: a willingness and desire on Mr Macdonald's part to be open with the incoming directors.

I11.19 The biggest blunder of all was that the DOCIA as executed did not in fact exclude from the indemnity claims by Amaca or Amaba. This outcome, and the mistakes that led to it, are addressed in chief at JH, 18.2. Such a result could not have been part of the strategy that is postulated by the MRCF. So much for utmost delicacy.

I11.20 It is true that JHINV did not make it clear, in the terms of the DOCIA, that the indemnity in favour of ABN 60 was not to include claims by Amaca and Amaba. That should have been made clear. It was the intention of the parties who entered into the DOCIA to exclude such claims. But the failure of the form of the DOCIA was an accident and no-one was misled.

J. Rectification of the Deed of Covenant, Indemnity and Access

This subject is addressed in chief by parties as follows:

(a) Section 18 of the James Hardie submissions (pp 222-229);

(b) Section 3, [78]-[100] of Counsel Assisting's submissions (pp 3-26 to 3-33);

(c) Chapter XI of the MRCF's submissions (pp 587-659).

There is passing mention of the subject on pp123-124 of the Union's submissions, which are directed at Mr Stevenson and do not call for any response by JHINV or ABN 60.

J1 Counsel Assisting

J1.1 Counsel Assisting's submissions on these issues are brief. In many respects they make observations that are consistent with the submissions for ABN 60 and JHINV. There are some short points that need to be made in response.

J1.2 Counsel Assisting submits that there is no evidence of any claims against ABN 60 that would be covered by the DOCIA as rectified but not otherwise: CA, Section 2, [93]. The evidence is that Mr Salter was probably not on notice of a specific claim at that time but that there was a steady stream of expenses relating to businesses that ABN 60 had disposed of in the past: T1949.30. These expenses were covered by the indemnity as rectified. Further, there was a concern about the cost of a tax audit. This is something that Mr Macphillamy in particular was concerned about: Ex 173, [7]. The evidence about which party gained most from the rectification is equivocal.

J1.3 Counsel Assisting's submissions point to evidence that supports the rectification: CA, Section 3, [95]. Nevertheless, they submit that the evidence "does not permit a conclusive answer to be given to the question whether a court would have rectified the DOCIA in the terms of the deed of rectification": CA, Section 3, [96]. The more important question for the Commission is whether it can conclude that the rectification was improper and liable to be set aside. Counsel Assisting do not suggest that this question could be answered in the affirmative. In any event, the evidence identified in JHINV's and ABN 60's submissions in chief would enable the Commission to conclude that a Court would have rectified the DOCIA: see JH, 18.2.4. The common intention was to exclude from the indemnity any claims by Amaca or Amaba.

J1.4 Counsel Assisting suggest that Mr Cameron and Mr Macphillamy may have breached their duty of care and diligence (s180) and good faith (s181) in causing the deed of rectification to be executed: CA, Section 3, [97]. On the other hand, Counsel Assisting also identify good reasons why there is no breach. In addition to those reasons, Mr Cameron and Mr Macphillamy could be confident that executing the deed was appropriate because it would put the DOCIA into a form that was consistent with their understanding of how it was intended to operate: JH, 17.1.28, 18.2.15.

J2 The MRCF

J2.1 One then turns to the submissions of the MRCF.

J2.2 The MRCF's submissions under this heading cut a wide swathe. A great deal of the material was not properly addressed during the course of the Commission, either in the statements or in oral evidence. The MRCF seeks to pick snippets of the evidence to construct a theory that was never properly ventilated during the course of the hearing. The Commission should not be tempted to seek to address the matters that are now raised by the MRCF.

J2.3 The MRCF submit that in November 2003 to February 2004, JHINV was placed in another "conundrum", which demanded "deft handing" of a "delicate" issue. The task this time was said to be "Herculean": MRCF, 60.4-60.6. The problem was said to arise because, notwithstanding the delicate skills of JHINV executives, they had failed to "get past" Mr Stevenson and sneak into the DOCIA the intended carve out of claims by Amaca and Amaba from the indemnity in favour of ABN 60. What was called for was a deed of rectification that perfected the plan that had been hatched in March 2003 but failed.

J2.4 It would appear that on the MRCF's view of things, there were two critical components to the JHINV plan in late 2003:

(a) confidence that Mr Cameron would flagrantly breach his duties to ABN 60 by acting solely in the interests of JHINV at the expense of ABN 60, including by withholding information from his fellow director, Mr Macphillamy and his solicitor, Mr Stevenson; and

(b) confidence that Mr Stevenson would not do his job properly.

J2.5 As to the first component, this serious allegation has no evidentiary foundation. It has not been tested during oral evidence. For example, it is submitted that Mr Cameron did not pass on the letter dated 18 September 2003 from Clayton Utz to Mr Macphillamy or Mr Stevenson: MRCF, 63.44; Ex 3, vol 1, tab 26. That was a letter addressed to Mr Ball of Allens. Mr Ball responded by letter dated 8 October 2003: Ex 3, vol 1, tab 28. He did so on behalf of both JHINV and ABN 60. It was never suggested to Mr Cameron or Mr Macphillamy that this correspondence was kept from Mr Macphillamy or their solicitor.

J2.6 Moreover, the fact that Mr Macphillamy was involved in the rectification and provided with documentation is evident from this answer (at T2676.50):

> I had meetings with Don Cameron relating to the request for rectification. I think we received a draft deed of rectification at the time. There was also, I think, one or two letters from Mr Macdonald which outlined what was proposed.

Minutes of meetings of the directors of ABN 60 reveal that MRCF information requests were discussed: Ex 173, tab 7, p 19.

J2.7 As to the second component, namely the suggestion that JHINV had brazenly calculated that Mr Stevenson would not give proper and careful advice, again there is really no basis for drawing the conclusion that that is what occurred.

J2.8 The MRCF also seeks to rely on Mr Morley's and Mr Cameron's "continuing duty to Amaca and Amaba … to provide to those entities the benefit of their knowledge as directors": MRCF, 61.13. The MRCF does not identify the source of this duty. It is submitted that there was no duty of that kind, particularly in a context where solicitors for Amaca and Amaba had already brought into question the propriety of the conduct of the former directors: Ex 3, vol 1, tab 22.

J2.9 The submissions of ABN 60 and JHINV in chief present a sensible evaluation of the evidence and demonstrate that the persons involved in the rectification of the DOCIA were behaving rationally and innocently. A contrary view, particularly one as extreme as the one presented by the MRCF (but by nobody else), should not be given any credence.

K. 1995 to 1998 Transactions

Counsel Assisting and the MRCF are the only parties, other than JHINV and ABN 60, who have made submissions in relation to the 1995 to 1998 transactions.

K1 Whether JHIL was a shadow director of Coy

K1.1 Both Counsel Assisting and the MRCF submit that JHIL was a shadow director of Coy between 1995 and 1998: CA, Section 4, [13] to [23]; MRCF, 7.3 to 7.30.

K1.2 The bases upon which Counsel Assisting relies for that conclusion are:

(a) JHIL had control of Coy and appointed its directors;

(b) the James Hardie group operated at the JHIL Board level from a financial point of view;

(c) the system under which JHIL's subsidiaries paid management fees;

(d) JHIL treated the James Hardie group as a consolidated group from a financial point of view when sourcing income from its subsidiaries;

(e) JHIL made decisions about the strategic restructuring of the James Hardie group, including decisions involving Coy; and

(f) JHIL, it is submitted, effectively directed Coy not to develop business opportunities and not to purchase assets which it would otherwise have developed and acquired.

K1.3 The bases relied upon by the MRCF are similar. The MRCF also relies upon JHIL's role in "managing Coy and Jsekarb's asbestos liabilities" (7.26) and in purchasing group insurance policies (7.27).

K1.4 For the reasons below, those submissions should be rejected. As a preliminary point, it should also be noted that, contrary to the MRCF's submission (5.7), the law concerning shadow directors is not an "exception to the corporate veil". No liability arises from a finding that JHIL was a shadow director of Coy without a subsequent finding that JHIL breached a duty imposed on it as a shadow director.

K1.5 *First*, if correct, Counsel Assisting and the MRCF's submissions would have the result that nearly every parent company in Australia was a shadow director of its subsidiaries. In particular, with regard to (a) and (e) above, it is clear that a parent company's ability to control its subsidiary does not render it a shadow director of the subsidiary: *Standard Chartered Bank of Australia Limited v Antico* (1995) 38 NSWLR 290.

K1.6 *Secondly*, with regard to (b), (c) and (d), Dr Barton's evidence was that when determining what dividends and management fees would be paid by Coy, he would:

(a) consider what JHIL wanted; and

(b) consider what Coy needed to retain in order to continue to operate and pay its creditors: T2693.26.

K1.7 That evidence is inconsistent with a proposition that Coy acted at the direction of JHIL in paying dividends and management fees. On the contrary, it indicates that the directors of Coy took into account the wishes of Coy's sole shareholder (quite properly) but nevertheless gave independent consideration to the question of whether Coy should pay the dividend or fee: cf *Australian Securities Commission v AS Nominees Limited* (1995) 133 ALR 1 at 52 . There is no basis for Counsel Assisting's submission (in [22]) that Dr Barton's answers should be understood as describing his decision-making process as a director of JHIL when it is clear from the question that Dr Barton was being asked about actions taken by Coy. This is further supported by [9] of Dr Barton's supplementary statement (Ex 175), where Dr Barton states that the Board of Coy would "*ensure that adequate funds would be available for claims which had been lodged or notified*" when declaring dividends.

K1.8 *Thirdly*, with regard to (e) and (f) above, the fact that JHIL made decisions regarding the restructuring of the James Hardie group, including decisions which affected Coy, does not make JHIL a shadow director of Coy. In particular, a decision by JHIL not to invest further capital in Coy – which may have had the consequence that Coy was not able to pursue an opportunity which Coy would otherwise have pursued – is just that: a decision by JHIL. It is not evidence of the directors of Coy acting in accordance with the wishes of JHIL; such a decision by JHIL does not involve Coy doing, or refraining from doing, anything.

K2 Transfer of the Building Boards technology to James Hardie Research Pty Limited in 1995

K2.1 No party has made submissions opposing the making of a finding to the effect suggested in [52] of Counsel Assisting's Issues Paper, that is that the transfer of Coy's core technology to James Hardie Research Pty Limited in 1995:

(a) was for fair value;

(b) was made for legitimate commercial purposes; and

(c) was approved by the directors of Coy consistently with their directors' duties.

K2.2 See CA, Section 4, [9]. For a reason which is not apparent, the MRCF states that the MRCF accepts that a finding to the effect of paragraphs (a) and (b) above should be made but is silent regarding paragraph (c): MRCF, 9.1 and 9.2. However, the MRCF does not advance any submissions as to why a finding in terms of paragraph (c) should not also be made.

K2.3 The Commissioner should make a finding in the terms suggested in paragraph 52 of the Issues Paper.

K3 The 1995 and 1996 Dividends

K3.1 Counsel Assisting does not submit, and no other party submits, that the Commissioner should find that the 1995 and 1996 dividends were paid otherwise than out of profits: CA, Section 4, [24] (in respect of the 1995 dividends) and [73] (in respect of the 1996 dividend); MRCF, 11.12 (in respect of the 1996 dividend).

K3.2 Counsel Assisting identifies two potential causes of action arising out of the payment of the 1995 dividends and 1996 dividend:

(a) breach of duty by the directors of Coy; and

(b) that the dividends were paid under a mistake.

K3.3 Of the two types of cause of action identified, the question of whether JHIL was a shadow director of Coy is relevant only to the first and not to the second.

K3.4 In addition to the causes of action identified by Counsel Assisting, the MRCF submits that JHIL is, or was, liable to pay equitable compensation to Coy in respect of breaches of fiduciary duties owed by JHIL to Coy. The MRCF submits that JHIL owed those fiduciary duties to Coy as the result of a "joint venture" which he submits existed between JHIL and Coy between 1990 and 1998.

K3.5 Each of those submissions is considered in turn.

Breach of directors' duties

K3.6 Counsel Assisting puts the argument for a breach of directors' duties in respect of the 1995 dividends as follows.

(a) It was a breach of s232(4) of the Corporations Law and the corresponding general law duty of care and diligence not to obtain an actuarial report identifying the assets Coy needed to have available in order to be reasonably confident of being able to pay all future creditors prior to paying the 1995 dividends: CA, Section 4, [50].

(b) If the directors of Coy had received such an actuarial report, they could not have authorised payment of the 1995 dividends without contravening s232(2) of the Corporations Law or the corresponding general law duty to act in the best interests of the company as a whole: CA, Section 4, [54].

K3.7 The argument put by Counsel Assisting in respect of the 1996 dividend is the same: CA, Section 4, [81] and [82]. Obtaining the October 1996 Trowbridge report did not discharge the Coy directors' duties, Counsel Assisting submits, because that report was inadequate for the purpose of assessing Coy's future asbestos liabilities: [81]. Further, the implication is that the Coy directors should have known the October 1996 report to be inadequate.

K3.8 The analysis by which Counsel Assisting seeks to make out a breach of duty in connection with the payment of the 1995 dividends and 1996 dividend is artificial and incorrect. The flaw in the analysis is that the real cause of any loss to Coy was the payment of the dividends and not the failure to obtain an actuarial report. Counsel Assisting's attempt to repair the chain of causation in this respect is unpersuasive: CA, Section 4, [63]. The correct approach is to ask, in respect of each dividend: in all the circumstances, did payment of the dividend constitute a breach of duty by the directors of Coy?

K3.9 Two points arise from that approach.

(a) First, the evidence of Dr Barton and Mr McGregor as to whether they would have allowed Coy to pay a dividend had they known, in 1995 and 1996, the full extent of Coy's asbestos liabilities (relied upon by Counsel Assisting in [58] and [59]) does not determine the question of whether payment of those dividends constituted a breach of duty. It may well be that, upon receipt of Counsel Assisting's hypothetical actuarial report, Dr Barton and Mr McGregor would have taken a more conservative approach than the law required. It does not follow that payment of the 1995 and 1996 dividends constituted a breach of duty by the directors of Coy. That is not to say that the advice which would have been obtained from actuaries, had it been sought in 1995, is irrelevant to the question of whether those dividends were paid in breach of duty. That issue is considered below.

(b) As Counsel Assisting notes, the balance of authority favours the view that s 232(2) of the Corporations Law will not be contravened by a director who honestly believed he was acting in the best interests of the company: *Corporate Affairs Commission v Papoulias* (1990) 20 NSWLR 503. Consequently, the question of whether the directors of Coy contravened s232(2) in resolving to pay the 1995 and 1996 dividends must be determined without reference to the contents of a hypothetical actuarial report which did not exist at the time the dividends were paid: CA, Section 4, [51]. On the other hand, it is accepted that the six matters referred to in paragraphs [44] to [49] of Counsel Assisting's submissions are relevant to the question of whether the directors of Coy could honestly have believed that payment of the dividends was in the best interests of the company as a whole.

K3.10 Consequently, it is submitted that the relevant question is whether, in all the circumstances, it was a breach of the Coy directors' duties to pay each of the 1995 and 1996 dividends.

K3.11 Counsel Assisting appears to contend that the directors of Coy could not, consistently with their duties to the company, have paid the 1995 and 1996 dividends unless they were "reasonably confident of being able to pay all future creditors" after paying those dividends: CA, Section 4, [25(a)(i)] and [31]. That test is, with respect, without foundation in law. The relevant principle is not controversial. It is that the directors of a company are required to have regard to its creditors' interests if the company "is insolvent, or near insolvent, or of

doubtful solvency, or if a contemplated payment or other course of action would jeopardise its solvency": *Kinsela v Russel Kinsela Pty Limited (in liq.)* (1986) 4 NSWLR 722; *Nicholson v Permakraft (NZ) Ltd (in liq.)* [1985] 1 NZLR 242; *Linton v Telnet Pty Limited* (1999) 30 ACSR 465; *Sycotex Pty Limited v Baseler* (1994) 13 ACSR 766. Moreover, it is clear that that is the principle to which Dr Barton in fact had regard when resolving to pay the 1995 and 1996 dividends: T2693.27.

K3.12 It is not possible, on the evidence before the Commission, to conclude that the directors of Coy ought reasonably to have taken the view that Coy was of doubtful solvency in 1995 or 1996, or that payment of the dividends would jeopardise its solvency.

(a) Dr Barton's evidence was that at the time the dividends were paid he was of the view that Coy had a strong business and was able to pay its debts – including its asbestos liabilities – as and when they fell due: T2694.3, T2699.26. Dr Barton was an experienced company director and the Commission should be cautious in substituting its own assessment of Coy's financial position for that of Dr Barton at the time.

(b) While it is accepted that the directors of Coy knew, or ought to have known, that it was certain that Coy would incur substantial asbestos liabilities in the future (CA, Section 4, [45] to [49]), it was not unreasonable for the directors to form the view, in 1995 and 1996, that Coy would be able to meet those asbestos liabilities as and when they fell due. It was not unreasonable for the directors to form that view, without an actuarial report, by having regard to the amounts which had historically been paid by Coy on account of asbestos claims relative to Coy's revenue and operating profit. At the time the 1995 dividends were paid, the following information (relating to Coy) would have been available to the directors.

	Revenue[1]	Operating profit (before tax and abnormals)	Asbestos liabilities[2]
	($000)	($000)	($000)
YEM 1990	265,364	32,206	549
YEM 1991	139,198	24,903	3,959
YEM 1992	232,728	7,574	3,815
YEM 1993	247,538	25,612	4,244
YEM 1994	257,242	17,506	9,774
YEM 1995	283,495	33,227	12,208

At the time the 1996 dividend was paid, the directors would also have been aware of the following further information.

	Revenue ($000)	Operating profit ($000)	Asbestos liabilities ($000)
YEM 1996	n/a	18,365	12,470

At the time the 1995 and 1996 dividends were paid, Coy's annual revenue and profit were many times greater than its asbestos liabilities. Nothing in the above figures would have caused a reasonable director to form the view that Coy was in imminent danger of failing to meet its asbestos liabilities or would be if the dividends were paid.

(c) For the reasons above, it was reasonable for the directors to pay the 1995 dividends without an actuarial report. However, even if an actuarial report had been obtained, it would not have prevented the Coy directors paying the 1995 dividends consistently with their duties to Coy. The following points are relevant.

(i) First, it is clear that no actuarial report obtained by Coy in 1995 would have assessed Coy's asbestos liabilities at $2 billion: cf CA, Section 4, [28], [30] and [54]. To seek to judge the Coy directors' conduct by reference to such a figure is meaningless.

[1] Revenue and profit figures have been taken from Coy's annual accounts: Ex 1, vol 1. Coy's accounts for the year ended 31 March 1996 do not disclose its revenue: Ex 1, vol 1, tab 7.

(ii) Secondly, the other hypothetical figure referred to by Counsel Assisting – $530 million – is also attended by difficulties. Even assuming that it were reasonable to take the October 1996 report as the basis of an actuarial assessment in August 1995 (CA, Section 4, [29]), the figure of $530 million is not a figure which appears in that report. Instead, Counsel Assisting appears to have arrived at the figure by taking Trowbridge's most likely assessment ($230 million) and adding the allowances for high claim numbers ($107 million) and high claim inflation ($109 million) which appear on page 636 of Ex 2, without regard to whether such an addition is a mathematically sensible process. (It may be noted that the amounts do not total $530 million.) That exercise, with respect, amounts to no more than mere speculation as to what an actuarial assessment would have said of Coy's asbestos liabilities in August 1995. It is certainly not evidence on which the Commission should make a finding that Dr Barton and Mr McFadden breached their duties as directors in resolving to pay the 1995 dividends.

(iii) Thirdly, a more fundamental objection to Counsel Assisting's submissions in relation to the payment of the 1995 and 1996 dividends is that, for the reasons in K3.11 above, there was no need for any actuarial report obtained by Coy to seek to ascertain "the assets Coy needed to have available in order to be reasonably confident of being able to pay all potential future creditors". That was simply not a test to which the Coy directors were required to have regard when resolving to pay dividends.

On the contrary, had the Coy directors obtained an actuarial assessment in the form of Trowbridge's October 1996 report in August 1995, it would have been quite permissible for them to resolve to pay the August 1995 dividends on the basis that:

(1) the actuarial report indicated that future asbestos claims were likely to be distributed over a 30 year period;

(2) average annual claim costs were not expected to peak until some 10 years into the future, and then only at an amount which was roughly equal to Coy's average annual pre-tax profits;

(3) in the event that claim costs exceeded profits in any given year, Coy had available to it a substantial share capital which was available to meet those claims (still over $100 million after payment of the 1995 dividends: Ex 1, tab 7, p 105).

[2] Ex 2, vol 3, tab 12 (Trowbridge's October 1996 report), pp 667-668; TRO.026.

(iv) Fourthly, even if the assumptions made by Counsel Assisting to arrive at a figure of $530 million were able to be supported, it is incorrect to suggest that that figure could somehow be taken to represent an estimate of Coy's liabilities which the Coy directors might have been required to compare to Coy's assets: cf CA, Section 4, [38] and Counsel Assisting's reference to *Nicholson v Permakraft (NZ) Ltd (in liq.)* [1985] 1 NZLR 242. The figure of $530 million is suggested by Counsel Assisting to be the amount which an actuarial report would have suggested Coy put aside "in order to be reasonably confident of being able to pay all potential future creditors": CA, Section 4, [29]. As such, the hypothetical $530 million includes a buffer over and above Trowbridge's central estimate in order to provide a "reasonable degree of confidence"; it is not an *estimate* of Coy's future liabilities, it is a deliberate *overestimate* of those future liabilities.

(v) Fifthly, Counsel Assisting's submission that Coy's asbestos liabilities should have been compared to a net assets figure of approximately $347.3 million (CA, Section 4, [27]) ignores the substantial decline in the value of Coy's business which occurred between 1996 and 1998. Until 1996, Coy had a virtual monopoly over the sale of fibre cement in Australia: Morley, Ex 121, [73] and tab 20, p 896. That suggests it is inappropriate to seek to value Coy's business in 1995 using the goodwill of $16.5 million determined by Grant Samuel in 1998. If PwCs' valuation of Coy's goodwill as at January 1997 ($110 million to $125 million: Ex 121, tab 21) were used instead, the value attributed to Coy's net assets would have been approximately $448.3 million.

K3.13 Moreover, it is not irrelevant to this issue that the MRCF itself submits that Amaca is still solvent today and, indeed, "may never become insolvent": MRCF, 64.10(a).

Payment under a mistake

K3.14 Counsel Assisting and the MRCF submit that the August 1995 dividends were paid under a mistake. Counsel Assisting, but not the MRCF, also submits that the October 1996 dividend was paid under a mistake. Counsel Assisting and the MRCF rely on a range of supposed mistakes:

(a) "a mistaken understanding of the extent of the company's present and future asbestos liabilities" (CA, Section 4, [62] and [86]);

(b) "a mistake … as to whether in law there were profits out of which the dividend might be paid" (MRCF, 10.21); and

(c) "the mistaken belief that JHIL would meet any future liabilities which Coy was unable to meet from its own assets" (MRCF, 10.21).

K3.15 For the reasons which follow, those submissions should be rejected.

K3.16 The first point which should be made is that a dividend is a payment in the nature of a gift. It is not a payment of the type considered by the High Court in *David Securities Pty Ltd v Commonwealth Bank of Australia* (1992) 175 CLR 353. The High Court there held (at 378) that:

> … the payer will be entitled prima facie to recover moneys paid under a mistake if it appears that the moneys were paid by the payer in the mistaken belief that he or she was under a legal obligation to pay the moneys or that the payee was legally entitled to payment of the moneys. Such a mistake would be causative of the payment.

K3.17 The Court did not decide the question of whether a payment made by way of gift, without an intention to acquire a benefit or discharge a liability, could be recovered if paid under a mistake. It was not necessary to decide that question. Brennan J expressed the opinion (at 393) that such a payment should, in principle, be recoverable if paid under a mistake but conceded that that opinion was contrary to the decision in *Aiken v Short* (1856) 1 H&N 210. His Honour's opinion would also appear to be contrary to the decision of the Court of Appeal in *Morgan v Ashcroft* [1938] 1 KB 49.

K3.18 It was argued before Giles J in *Segenhoe Limited v Akins* (1990) 29 NSWLR 569 that Segenhoe Limited was entitled to recover a dividend from its shareholders on the grounds that it had been paid under a mistake (the mistake being whether there were sufficient profits out of which to pay the dividend). It was ultimately unnecessary for Giles J to decide that question. However, the cases considered by his Honour (at 583 to 587) provide some authority for the proposition that a dividend is not recoverable from a shareholder on the grounds that the dividend was paid under a mistake. In particular, the judgment of Lord Alverstone CJ in *Lucas v Fitzgerald* (1903) 20 TLR 16 which concerned dividends paid out of capital to three directors of the company, from which Giles J quotes (at 584), supports that proposition:

> Then comes the point whether a director who receives money, which, as it turns out, he ought not to have received, can be compelled to refund. Upon this point I am bound by the conclusive authority of *In Re Denham & Co (ubi supra)*, which decides that a director who receives money innocently cannot be compelled to refund it, either under s 165 of the *Companies Act* … or as money had and received, or on any other grounds.

K3.19 The cases discussed by Giles J suggest that a dividend will only be recoverable from a shareholder in circumstances where payment of the dividend involved a breach of duty on the part of the directors and was received by a shareholder with knowledge of that breach, so as to render the shareholder a constructive trustee for the company. Nevertheless, it is clear that Giles J did not regard those cases (which were older, English cases) as conclusive on the point (at 586C).

K3.20 The question of whether a dividend may be recovered from a shareholder on the grounds that the dividend was paid under a mistake is best regarded as open under Australian law. That appears to be the view of the authors of *Ford's Principles of Corporations Law*, who describe the availability of such an action as "a possibility": [18.100].

K3.21 In any event, it is unnecessary to decide the question in order to deal with the submissions of Counsel Assisting and the MRCF. For present purposes, it is enough to note that, in order for there to be a right to recover moneys paid under a mistake:

(a) there must be a mistake, rather than a mere misprediction or failure to make enquiries; and

(b) the mistake must have caused the payment to be made: *David Securities* at 373 and 378.

K3.22 In relation to the distinction between a mistake and a mere misprediction, Professor Birks has written:

> Suppose that the mistake which I make is not that Blackacre is already mine but that you will in future give it to me. That kind of mistake will never negative voluntariness. It is a mere misprediction as to the future, exactly the kind of "mistake" which you make when you clean my car believing wrongly that I will pay. A misprediction is nothing but the taking of a risk, an exercise of judgment which turns out badly rather than a judgment vitiated. That is why the law requires mistakes to be of present or past fact.

(See *An Introduction to the Law of Restitution* (1985), p 278.)

K3.23 Professor Birks' statement was expressly approved by Cooper J in *Strang Patrick Stevedoring Pty Limited v The "Sletter"* (1992) 38 FCR 501 at 524.

K3.24 Similarly, Mason and Carter have observed that "a mistake which is a mere misprediction as to the future is nothing more than the taking of a risk that comes home": *Restitution Law in Australia* (1995) at 118.

K3.25 Also relevant in this context is the situation in which a person makes a payment, choosing not to make further investigation of facts which might be relevant to his decision. Lord Abinger CB in *Kelly v Solari* (1841) 9 M&W 54 at 58 said:

> There may also be cases in which, although [the payer] might by investigation learn the state of facts more accurately, he declines to do so, and chooses to pay the money notwithstanding; in that case there can be no doubt that he is … bound.

K3.26 That statement is quoted with approval by Goff and Jones: *The Law of Restitution*, 6th Ed., 2002, [4-030].

A "mistaken understanding of the extent of Coy's present and future asbestos liabilities"

K3.27 The "mistake" suggested by Counsel Assisting – a mistaken understanding of the extent of Coy's present and future asbestos liabilities (CA, Section 4, [62] and [68]) – is not a mistake at all but rather a misprediction.

K3.28 At the time he resolved to pay the 1995 and 1996 dividends, Dr Barton knew the extent of Coy's future asbestos liabilities was uncertain: T2728.6. It was a matter which could only be the subject of prediction and estimation, whether by actuaries or laymen, including the directors of Coy. There is no evidence to suggest that Mr McFadden's understanding was any different.

K3.29 It is irrelevant to the question of mistake whether Dr Barton would resolve to pay the dividends if he had his time over again, knowing what he knows today about Coy's asbestos liabilities: cf CA, Section 4, [58], [59], [62] and [86]. Even if that is the case, it does not mean the directors of Coy were labouring under a mistake in 1995 or 1996. It simply means their then current assessment of those liabilities has ultimately proved to be too low. It was a misprediction. Whether that assessment was negligently arrived at is a question relevant to whether there was a breach of directors' duties. For the reasons in K3.6 to K3.13, there was no such breach. The issue of negligence is not relevant to mistake.

"A mistake as to whether in law there were profits out of which the dividend might be paid"

K3.30 The MRCF's submission that the August 1995 dividends were paid under a mistake as to "whether in law there were profits out of which the dividend might be paid" (MRCF, 10.21) may be dealt with shortly. The answer is that such a belief was not a mistake. It is clear from Coy's accounts for the years ended 31 March 1995 and 31 March 1996 that the August 1995 dividends were paid out of profits. In particular, Coy's accounts for the year ended 31 March 1996 record retained profits of $65.8 million, still available for distribution *after* payment of the August 1995 dividends: Ex 1, tab 7, p 104. Counsel Assisting accepts that these dividends were paid out of available profits: CA, Section 4, [24].

A "mistaken belief that JHIL would meet any future liabilities which Coy was unable to meet from its own assets"

K3.31 In the alternative to its submission above, the MRCF submits that the August 1995 dividends were paid under the mistaken belief that JHIL would meet any future liabilities which Coy was unable to meet from its own assets: MRCF, 10.21. The flaw in that submission, like the submissions of Counsel Assisting, is that the "mistake" relied upon is not a mistake at all but a misprediction as to the future. It is precisely the type of non-

mistake identified by Professor Birks – "the kind of 'mistake' you make when you clean my car believing wrongly that I will pay": see K3.22 above.

K3.32 A second flaw with the MRCF's submission, or perhaps just a second way of stating the first flaw, is that the mistake relied upon by the MRCF is not a mistake which could possibly have caused the 1995 dividends to be paid.

K3.33 The mistake suggested by the MRCF could only sensibly be a mistake as to JHIL's future intentions as at 1995. The MRCF does not submit that Dr Barton or the other directors of Coy were labouring under a mistake, in 1995, that JHIL was liable to meet Coy's future asbestos liabilities or that Coy had a legally enforceable right to compel JHIL to do so. In any event, such a submission would fly in the face of the only evidence on the question, which is Dr Barton's. He strongly resisted the proposition that he, as a director of Coy, had proceeded on the premise that Coy's asbestos liabilities would necessarily be met by JHIL - "they were clearly Coy's liabilities": T2698.7; T2738.29. He expressly rejected the proposition that it had been implicit that JHIL would meet Coy's future liabilities if Coy could not: T2698.37. Dr Barton never regarded JHIL has having committed itself in any way to meeting Coy's obligations to creditors: T2752.52; T2739.10.

K3.34 A claim framed in terms of a mistaken belief as to JHIL's future intention faces similar difficulties in light of the evidence on the question. In particular, Dr Barton's evidence was that he was not aware of any intention that JHIL would meet Coy's future liabilities: T2698.41; T2711.40. The issue simply did not arise because Coy was a going concern and there was no suggestion that Coy could not meet its liabilities. However, a claim framed in terms of a mistake as to JHIL's future intention suffers from a more fundamental difficulty, namely, that such a mistake cannot be said to have caused the payment of the dividends. The payments were "voluntary" in the sense described by Mason CJ, Deane, Toohey, Gaudron and McHugh JJ in *David Securities* (at 373-374) in that Coy chose to make the payments irrespective of whether JHIL was legally required to meet Coy's future liabilities.

Change of Position

K3.35 In any event, even if Coy had had a right to recover the 1995 and 1996 dividends on the basis that they were paid under a mistake, it is highly likely that JHIL would have subsequently passed on to its shareholders the amounts of those dividends by way of JHIL's own dividends and thereby changed its position to its detriment: see *David Securities* (at 385); see also *Ford's Principles of Corporations Law* (at [18.100]). JHIL paid dividends of over $360 million between the date of Coy's 1995 dividends and October 2001: see the Directors' Reports for the years ended 31 March 1996 to 2001 included in Ex 277. Counsel Assisting's submission (at [62]) that "there is no evidence which would suggest … that JHIL changed its position in a material respect having received the dividends" should be rejected.

K4 Management Fees

K4.1 The management fees paid by Coy in the years ended 31 March 1995 to 1998 were:

(a) $20.3 million in YEM1995;

(b) $21.5 million in YEM1996;

(c) $20.3 million in YEM1997; and

(d) $15.6 million in YEM1998.

(See Ex 103, tab 1.)

K4.2 The figure of $25.9 million stated by Counsel Assisting in respect of the year ended 31 March 1997 is incorrect.

K4.3 Counsel Assisting submits that Coy had available to it causes of action against its directors (including, Counsel Assisting submits, JHIL as a shadow director) in respect of the 1995 to 1998 management fees because:

(a) it was a breach of duty to pay *any* management fee in those years without obtaining an actuarial report "for the purpose of ascertaining the level of assets necessary or appropriate for Coy to have available in order to be reasonably confident of being able to pay all future creditors" (CA, Section 4, [90] to [99]);

(b) if such an actuarial report had been obtained, Coy would not have paid management fees beyond a fair arm's length price for the value of the services rendered by JHIL to Coy ([100] to [101]); and

(c) the management fees paid exceeded the fees which would have been agreed in an arm's length negotiation ([102] to [107]).

K4.4 For the reasons given in K3.8, Counsel Assisting's analysis is artificial and incorrect. The act which has caused Coy loss, if any, is the payment of the management fees, not the failure to obtain the hypothetical actuarial report suggested by Counsel Assisting. The relevant question is whether, in all the circumstances, the payment of each of the management fees involved a breach of duty by the directors of Coy. For the reasons given below, it did not.

K4.5 At the time the 1995 to 1998 management fees were paid, Coy's business produced revenues which were more than sufficient to allow Coy to meet its asbestos liabilities as they were incurred. It is not disputed that JHIL provided Coy with services which allowed Coy to run its business. To the extent the management fees paid by Coy represented fair value for those services, there can be no question but that they were paid consistently with the Coy directors' duties to the company as a whole; to suggest otherwise would be to suggest that the business should not have been operated at all, which would clearly have been to the detriment of Coy's creditors. To the extent, if any, that the management fees

paid by Coy exceeded fair value for those services, they were payments in the nature of a gift to JHIL. To that extent (only), they will have been paid in breach of duty if Coy could not have paid the same excess to JHIL by way of dividend.

K4.6 In relation to the last point, the considerations discussed in K3.9 to K3.11 also apply here.

(a) The evidence of Mr McGregor as to what management fees would have been paid after receipt of Counsel Assisting's hypothetical actuarial report is not determinative of the question of breach of duty: cf CA, Section 4, [101]. The relevant questions are (for the purpose of s232(2) of the Corporations Law) whether the Coy directors honestly believed the payment of the management fees to be in the best interests of the company as a whole and (for the purpose of the directors' duties at general law) whether an honest and intelligent person in the directors' position could have reasonably believed the payments were for the benefit of the company as a whole.

(b) The principle suggested by Counsel Assisting, that Coy was unable to pay dividends or management fees above fair value unless the directors had set aside sufficient assets to be "reasonably confident of being able to pay all future creditors", does not represent the law. The directors of Coy were entitled to have regard to its shareholder's interests unless insolvency was imminent. Neither Counsel Assisting nor the MRCF suggest it was.

K4.7 In relation to the question of whether the management fees exceeded fair value for the services provided by JHIL, the primary reason why Counsel Assisting submits that they did is that the apportionment of JHIL's costs by which the management fees were calculated did not allocate costs to JHIL's foreign subsidiaries, including its US subsidiaries: CA, Section 4, [104]. The calculations of management fees contained in the PwC and Grant Samuel valuations, upon which Counsel Assisting seeks to rely ([105] and [106]), each assumed that JHIL's costs should be allocated across the entire James Hardie group.

K4.8 The difficulty with that submission is that there were good reasons why a calculation of the fair value of services actually provided by JHIL to its subsidiaries should have drawn a distinction between Australian and foreign subsidiaries: see the submissions in chief of the James Hardie parties, 3.3.12. In particular, JHIL's foreign subsidiaries substantially operated on a stand-alone basis. Mr Salter's and Mr Macdonald's evidence was that around 5% - 15% of JHIL's corporate costs were attributable to its US operations: Salter T1994.25, Macdonald T2285.42 – T2287.30; see also JH, 3.3.12. On that basis, the approach taken to calculating Coy's management fees was not unreasonable; it was certainly closer to the mark than the approach taken by PwC and Grant Samuel, the latter of which attributed 58.2% of JHIL's costs to the US operations: Ex 121, tab 20, p 912.

K5 Transfers of Assets in 1998

K5.1 The three transfers of Coy's assets which took place in 1998 were:

(a) the transfer of plant and equipment to James Hardie Fibre Cement Pty Limited on 31 March 1998;

(b) the transfer of the Building Boards trademarks to James Hardie Research Pty Limited on 30 June 1998; and

(c) the transfer of Coy's business to James Hardie Australia Pty Limited on 28 October 1998.

K5.2 No party submits that either of the first 2 transfers took place other than for fair market value: CA, Section 4, [113] and [116]; MRCF, 13.1 and 14.1. Counsel Assisting alone questions whether the transfer of Coy's business in October 1998 was for fair market value but does not submit that the evidence allows a firm conclusion to be drawn. Rather, Counsel Assisting submits that 'the evidence tends to suggest the possibility' that the evaluation of Coy's goodwill (by Grant Samuel) used for the purpose of determining the consideration paid to Coy may have understated that goodwill: CA, Section 4, [134].

K5.3 However, Counsel Assisting does not submit that either JHIL or any of the directors of Coy as at October 1998 knew, or ought reasonably to have known, that Grant Samuel's valuation was understated (if indeed it was). Nor does Counsel Assisting submit that it is possible to allocate responsibility for any understatement in Grant Samuel's valuation to a particular party: [134].

K5.4 Counsel Assisting submits that the directors of Coy may have breached their duties to the company by causing Coy to sell its business in 1998, notwithstanding that the sale was for fair market value: CA, Section 4, [144]. That breach of duty is said to arise because the transactions were entered into for an improper purpose or were otherwise not in the best interests of the company as a whole, including Coy's creditors: [144].

K5.5 The improper purpose relied on by Counsel Assisting is that the transfers of Coy's assets in 1998 were carried out "to put the relevant assets beyond the reach of a particular group of Coy's creditors, asbestos plaintiffs": CA, Section 4, [144]. Counsel Assisting submits that the decision of the Full Court of the Supreme Court of Western Australia in *Jeffree v National Companies & Securities Commission* [1990] WAR 183 supports the proposition that transfers of Coy's assets for that purpose, even for fair market value, involved a breach of duty on the part of Coy's directors: [146]. Those submissions should not be accepted for the following reasons.

K5.6 *First*, the evidence does not support a finding that the purpose of Project Chelsea was to put Coy's operating assets beyond the reach of asbestos plaintiffs. Instead, the evidence indicates that it was considered important to the success of Project Chelsea as a whole

that the company to be floated on the New York Stock Exchange be free of asbestos liabilities: see JH, 4.1.34ff and Dr Barton's supplementary statement, Ex 175 at [12]. While that purpose inevitably had the consequence that Coy's operating assets would not be available to asbestos plaintiffs, that did not make the purpose of the transfer improper, having regard to the significant commercial benefits which it was believed would accrue to Coy's shareholder, JHIL, and the fact that the transfers were at fair market value.

K5.7 *Secondly*, the purpose considered by the Court in *Jeffree* was a purpose to defeat creditors: [1990] WAR 183 at 184.25 per Wallace J and at 193.24 per Brinsden J. There is no dispute that such a purpose is improper. However, a purpose to put certain assets beyond the reach of asbestos claimants is not, of itself, a purpose to defeat those creditors. That question depends on what consideration is to be received for the transfer of the assets and how it is to be applied. In *Jeffree*, the fact that the assets were transferred for fair market value (or close to it) was consistent with a purpose to defeat a particular contingent creditor's claim because the transferor company was "in a state of imminent insolvency" at the time of the transfer and the proceeds were applied to discharge existing creditors' debts with the intention of leaving no assets to meet the contingent creditor's claim. There is no evidence to suggest a similar purpose in relation to the transfers of Coy's assets in 1998. On the contrary, it is accepted that the proceeds received by Coy in 1998 have been, and continue to be, available to meet the claims of asbestos plaintiffs.

K5.8 *Thirdly*, the evidence does not support a conclusion that the Coy directors acted otherwise than in the best interests of the company as a whole. Counsel Assisting's submissions as to why the transfers were contrary to the interests of Coy's creditors – despite being at fair market value – are not persuasive and are readily answered.

(a) Counsel Assisting submits that "Dr Barton appeared to accept that the sale of Coy's core business deprived Coy of the opportunity to participate in the growth of the Australian business". That is not in dispute. The answer to the submission is:

(i) Coy received fair market value, as determined by Grant Samuel, for giving up that opportunity – a point that was made by Dr Barton in his evidence (T2747.10 and .20) that value took account of the prospects of growth; and

(ii) while Coy was deprived of the opportunity to participate in any future growth of the Australian business, that future growth was not guaranteed and the sale of Coy's business protected Coy (and its creditors) against the possibility of a future decline in Coy's business.

(b) Counsel Assisting refers to Mr Morley's evidence that "the internal rate of return James Hardie was aiming for in 1998 was probably between 15 and 20%, and that it was certainly much more than the rate at which the company was borrowing from the bank". To submit that Mr Morley's evidence suggests that the transfer was

contrary to the interests of Coy's creditors ignores the fact that there was a significantly higher risk attached to funds invested in the Australian business than was associated with funds more conservatively invested. The sale of Coy's business may well have meant that the funds available to meet the claims of Coy's creditors would no longer have the prospect of 15 to 20% per annum growth. On the other hand, Coy's ability to meet those creditors' claims was no longer dependent on the ongoing success of the Australian business. It is simply not possible to conclude that the sale was contrary to the interests of Coy's creditors. Coy had effectively replaced higher risk / higher return assets with low risk / low return assets. Indeed, given the long period of time over which Coy could expect to receive asbestos claims, it may well be that a decision to invest its funds in low risk / low return assets was positively in the interests of Coy's creditors as it increased the likelihood that there would be funds available to meet claims arising beyond the immediate future.

(c) Similarly, Counsel Assisting seeks to draw support from Mr Morley's agreement that, "as things stood at the date of the transfer of Coy's assets the opportunities for growth were in the assets that were transferred not in the money that was left behind". Again, weighing against the opportunities for growth were the possibilities of a decline in the business.

K5.9 Essentially, what Counsel Assisting seeks to argue by the above submissions is that Coy was not adequately compensated for giving up the opportunity to participate in the growth of the Australian business. However, that opportunity was precisely what had been valued by Grant Samuel. To suggest that the interests of Coy's creditors required that Coy receive more than the value of that opportunity suggests that the opportunity should have been valued without reference to the risk which was inextricably linked to it.

K5.10 *Fourthly*, even if it were assumed that the Coy directors approved the sale of its assets for an improper purpose, there is insufficient evidence to support a conclusion that Coy has a valuable cause of action as a result. Counsel Assisting does not identify the quantum of the claim which it is submitted Coy may have in respect of the sale of its business. Presumably, Counsel Assisting would submit that Coy should be placed in the position it would be in today had it not sold its business. However, Coy's business (the Australian business) has not experienced the strong growth achieved by the US business since 1998. Mr Morley's evidence was that revenues and profits of the Australian business have continued to decline in proportion to the total revenue of JHINV and Australian market share has continued to be eroded by competition: Ex 121, [113] and [114].

K5.11 The analysis performed by KPMG (Ex 314, Appendix C, p 11) suggests that, had Coy continued to own the Australian business, its net assets as at 30 June 2003 would have been approximately $58.4 million.

K5.12 That figure includes $15.5 million on account of royalties on sales of US products, attributable to the trademarks transferred by Coy in June 1998. Counsel Assisting acknowledges that there were legitimate commercial purposes behind that transfer: CA, Section 4, [136].

K5.13 Excluding those royalties, the KPMG analysis suggests that, had Coy continued to own the Australian business, its net assets would have been approximately $42.9 million as at 30 June 2003. That figure is not materially different to the $42.3 million of net assets actually reported by Amaca in its accounts for the year ended 30 June 2003: Ex 3, vol 2, tab 3, p 250; see also Ex 314, Annexure C, p 12.

K6 The MRCF's submissions on joint venture and agency

K6.1 The MRCF submits that JHIL and Coy participated in a joint venture: MRCF, 8.1ff. The MRCF further submits that, over the period from 1990 onwards, the affairs of the James Hardie companies were conducted on a group basis which gave rise to a joint venture; MRCF, 8.8(a).

K6.2 It is then said that this joint venture "gave rise to relevant fiduciary obligations": MRCF, 8.3. Those obligations are said to have been breached by JHIL during the period 1995 to 1998 and also in February 2001.

K6.3 For the reasons which follow, those submissions should be rejected.

K6.4 *First*, the MRCF's submission that JHIL came to owe a fiduciary duty to Coy through the operation of a joint venture between the two companies is fundamentally misconceived. The essence of a fiduciary relationship is that the fiduciary undertakes to act for or on behalf of or in the interests of another: *Hospital Products Ltd v United States Surgical Corp* (1984) 156 CLR 41 at 96-97; *Pilmer v Duke Group Ltd (in liq.)* (2001) 207 CLR 165 at [70]. It is the antithesis of the relationship which exists between a listed parent company and its operating subsidiaries, in which the subsidiaries operate for the purpose of passing profits to the parent company. Moreover, there is no evidence to suggest that JHIL in anyway undertook to meet Coy's future asbestos liabilities. Indeed, Dr Barton's evidence was to the opposite effect: "they were clearly Coy's liabilities", T2698.7; see also T2698.37, T2738.29, T2752.52 and T2739.10. While the MRCF's submission that "equity required a sharing of the burdens as well as the benefits" between JHIL and Coy (8.10) may have an emotive appeal, there is no basis for it in legal principle.

K6.5 *Secondly*, the facts which the MRCF identifies are insufficient to establish a joint venture of the type alleged between JHIL and Coy. The term "joint venture" connotes an association of persons for the purposes of a particular trading, commercial, mining or other financial undertaking or endeavour with a view to mutual profit, with each participant usually (but not necessarily) contributing money, property or skill: *United Dominions Corp Ltd v Brian Pty Ltd* (1984) 157 CLR 1 at 10. Whether or not the relationship between joint venturers is

fiduciary will depend upon the form which the particular joint venture takes and upon the content of the obligations which the parties to it have undertaken: *United Dominions* (at 11). Further, the subject matter over which fiduciary obligations extend is determined by the character of the venture or undertaking: *Birtchnell v Equity Trustees, Executors & Agency Co Ltd* (1929) 42 CLR 384 at 408 per Dixon J. The MRCF identifies the following facts as establishing a joint venture between JHIL and Coy:

(a) the sharing of the "valuable James Hardie name and the goodwill and the reputation that went with it": MRCF, 8.8(b);

(b) Coy's contribution as an operating business to the "joint venture of the name": MRCF, 8.8(c);

(c) Coy's contribution of funds by way of dividends and management fees: MRCF, 8.8(e);

(d) JHIL's contribution of "management services": MRCF, 8.8(f).

K6.6 Put at their highest, these are simply characteristics of a commercial relationship between different entities in a corporate group. They do not support the proposition that a joint venture existed between JHIL and Coy, let alone a joint venture which gave rise to fiduciary obligations.

K6.7 The existence of a joint venture is merely asserted with no attempt adequately to identify, with any sense of precision, the terms, parties or scope of any joint venture agreement which would satisfy the most simple test in *United Dominions*.

Implied contract / estoppel

K6.8 In the alternative to its submission that JHIL and Coy were operating a joint venture, the MRCF submits that there is an implied contract or estoppel between JHIL and Coy which requires JHIL to meet Coy's future asbestos liabilities: MRCF, 10.7. The difficulty with that submission, as with the submission concerning a joint venture, is that it flies in the face of the evidence before the Commission. Dr Barton was the managing director of JHIL during the period 1995 – 1998 and was also a director of Coy. His evidence was that he never regarded JHIL as having committed itself in any way to meeting Coy's obligations to its creditors: T2752.52; T2739.10.

JHIL as managing agent for Coy

K6.9 The MRCF also submits that "JHIL acted as a managing agent of Coy … pursuant to a broad grant of power which had developed over the years": MRCF, 8.2.

K6.10 That submission should be rejected.

K6.11 No evidence is cited in support of such a submission, nor could it be. There is no basis in fact for the making of such a submission.

JHIL as joint tortfeasor

K6.12 The MRCF submits that JHIL and Coy were joint tortfeasors in respect of injury suffered as a result of Coy's manufacture and sale of asbestos products and that JHIL had been, or should have been, advised by Allens of its liability as a joint tortfeasor: MRCF, 5.1-5.5. It is unclear exactly what conclusions the MRCF submits follow. MRCF, 5.5 appears to be as far as the matter is taken:

> All of the activities undertaken by JHIL on the advice of Allens from the mid-1990s to separate the asbestos-related liabilities from the ongoing profitable activities of the James Hardie Group and to shed the operating subsidiaries as empty shells were predicated upon the incorrect façade of an absence of liability by Coy [sic].

K6.13 The MRCF's submissions on this point are remarkable only for the fact that no attempt is made to support any of them by reference to the evidence. Nor could they be supported. The allegations as to advice given to JHIL have been flatly rejected by Mr Williams: statement dated 28 July 2004, [44] to [46]. Moreover, Mr Williams' opinion was that, with the exception of the period before 1937, and with the possible exception of the period 1980-1987, JHIL did not have any liability to sufferers of asbestos-related illnesses caused by products manufactured and sold by Coy or Jsekarb: [45]. The MRCF's submissions should be rejected.

K7 Leases

K7.1 Only Counsel Assisting submits that Coy may have a cause of action in relation to the grant of leases to James Hardie Australia Pty Limited in 1998: CA, Section 4, [148]ff. The only possible claim identified is a claim against JHIL, based on the assumption that JHIL was a shadow director of Coy. (It is submitted that that assumption cannot be maintained: see section K1 above.) Counsel Assisting does not submit that Coy had a cause of action against any of its appointed directors at the time the leases were entered into: CA, Section 4, [154].

K7.2 The first point which should be made is that there is nothing in Counsel Assisting's submissions which would suggest a conclusion different from that stated at JH 4.5.14, namely, that any loss which Coy might have suffered by virtue of the annual rent under the leases being less than fair market rent was more than offset by a 6.5-fold increase in the price Coy received for the sale of its business. Coy has now sold all of the properties (Cooper T19.43), less than 6 years after entering into the leases. There is no suggestion that Coy received less than fair market value on the sale of the properties. Consequently, Issues 68 to 71 of Counsel Assisting's Issues Paper are essentially non-issues: whatever might be said about the rental valuations and the assumptions on which they were prepared, it is clear that they have not in any way decreased the assets of Amaca which are available to meet the claims of asbestos victims today.

K7.3 That having been said, Counsel Assisting's submissions on these issues are addressed below.

K7.4 Counsel Assisting seeks to attack the assumptions on which JLW's valuations were prepared and then seeks to sheet home the fault for any deficiencies in those assumptions to JHIL on the basis that JHIL, through Mr Shafron, "instructed" (CA, [150], [153]) or "required" (CA, [152]) JLW to use those assumptions. The assumptions criticised by Counsel Assisting are:

(a) the assumption as to vacant possession;

(b) the assumption as to lease terms;

(c) the assumption that each property was too big for one tenant and would need to be leased to multiple tenants.

K7.5 As to (a), it is not disputed that JHIL asked JLW to assume vacant possession for the purpose of preparing their valuations. That assumption was made in order to obtain a valuation which would reflect the rent which would be agreed as the outcome of a "pseudo negotiated situation" between landlord and tenant: Shafron, T1797.17.

K7.6 As to (b) and (c), the conclusion that Mr Shafron instructed JLW to make the assumptions made by them is not a conclusion which is reasonably open on the evidence. Instead, those assumptions were determined by JLW, having regard to what, in their opinion, was appropriate for the purpose of their valuation of each property.

(a) Mr Shafron's evidence was that the issue of what assumptions should be used in the valuations was discussed with Mr Ellis of JLW: T1793.11, T1794.26. That evidence has not been contradicted. JLW's letter of 24 June 1998 (Ex 75, tab 25) said:

> Reference is made to our meeting on 19 June 1998.
>
> At this meeting *we* undertook to provide you with *our* assumptions for the rental valuations. These assumptions are as follows:
>
> 1. Vacant Possession – We are to assess the rental for the properties as if they are vacant. This may involve the imaginary sub-division of each property into what *in our opinion* is a marketable component. …
> 2. Letting Up – *We* are to provide *our* estimate of a letting up period.
> 3. Lease Term – *We* will provide *our* opinion of market lease terms and conditions.
>
> (Emphasis added)

(b) Similarly, in his letter of 15 June 2004 (Ex 239), Mr Ellis says:

> The assumptions we were instructed to make in arriving at our advice/opinions are summarised as follows:

1. Assume vacant possession,

2. Make appropriate allowances for letting up periods,

3. Advise on market lease terms and conditions … .

(c) Moreover, the very terms of the valuations upon which Counsel Assisting relies to support the submission that "JLW was instructed to assume … lease terms of generally between 3 to 5 years, and that each property was too big for one tenant and would need to be leased to multiple tenants in more marketable parcels" (CA, [150]) make it clear beyond doubt that the decisions to divide the properties for the purposes of the valuations and to assume lease terms of less than 10 years were decisions made by JLW in their capacity as expert valuers. For example, the valuation of the Carole Park property (Ex 75, tab 27, p 504) says:

> As instructed, we have assessed market rentals on the basis that the buildings are leased to a third party. The overall property is too large for one tenant to lease, so we have therefore hypothetically subdivided the various buildings into more marketable parcels and assumed numerous leases to various parties over the stated 10 year period.
>
> …
>
> Lease terms for the buildings would generally be for 3 to 5 years. The buildings are of inadequate quality to attract any long term tenants. … .

(d) The rental opinion for the Rosehill property (Ex 75, tab 28, p 521) is similar:

> We have been instructed to assess the rental as if the premises were being offered vacant to a third party. In doing so *we have been requested to assess* how the market would treat the property over a ten (10) year term, taking full account of all associated costs of letting and lost rental income to arrive at an effective rental annuity over the term.
>
> The site lends itself to subdivision into numerous marketable portions. Seeking a tenant for the site in [its] entirety would *in our opinion* limit its potential marketability.
>
> (Emphasis added)

(e) The rental opinion in respect of the Welshpool property, also relied on by Counsel Assisting, is to a similar effect: Ex 75, tab 29, p 542.

K7.7 The only conclusion available is that:

(a) Mr Shafron and Mr Ellis discussed what assumptions should be made for the purpose of preparing rental valuations of the properties;

(b) as a result of the discussion, Mr Shafron instructed JLW to prepare their valuations on the assumption that each property was being offered vacant for lease to a third party; and

(c) the other assumptions – as to lease terms and subdivisions of the properties – were determined by JLW in their capacity as expert valuers; that is, JLW made the

assumptions which, in their opinion, were appropriate for the purpose of preparing each valuation.

K7.8 Consequently, the worst that can be said of Mr Shafron is that he instructed JLW to value the properties on the assumption that they were vacant and being offered for lease to a third party when, in fact, he knew that they were occupied by James Hardie and that James Hardie wished to stay in possession. Counsel Assisting submits that, in light of that knowledge, that assumption was inappropriate for obtaining a fair market rental for the properties (CA, Section 4, [149] and [153]) and, implicitly, that Mr Shafron knew it was inappropriate ([154]). However, the appropriateness of that assumption is a question on which minds may differ. There are good reasons to support the approach taken by JLW and it was reasonable in the circumstances: JH, 4.5.12. Even if it were not, neither Mr Shafron nor, through him, JHIL had any reason to believe otherwise. Mr Shafron had discussed the question with Mr Ellis. Mr Shafron's evidence was (T1798.13-.21):

> Q. To put it shortly Mr Shafron, if you had wanted valuations that attempted to do the balancing exercise that you say you were trying to achieve, you would have had the valuations done on the basis that the premises were occupied by James Hardie on leases which had expired, and they wished to continue in occupation, isn't that right?
>
> A. Well I don't believe that was the guidance I had from Mr Ellis from JLW.

K7.9 Mr Shafron was entitled to rely on that advice.

K8 Limitation of Actions

K8.1 JHINV and ABN 60 accept the submissions of Counsel Assisting concerning limitation periods. Any cause of action available to Coy arising from the sale of its business to James Hardie Australia Pty Limited on 28 October 1998 will expire on 28 October 2004.

K8.2 The relevant limitation periods have expired in relation to any causes of action available to Coy arising from:

(a) the payment of the 1995 dividends (CA, Section 4, [64]);

(b) the payment of the 1996 dividend ([87]);

(c) the payment of management fees ([110]); and

(d) the transfer of plant and equipment to James Hardie Fibre Cement Pty Limited and the transfer of trademarks to James Hardie Research Pty Limited ([147]).

K9 Voidable Transactions

K9.1 Neither Counsel Assisting nor any of the parties to the Commission has submitted that there is any basis for concluding that any of the 1995-1998 transactions is voidable or might be the subject of some other remedy available to a liquidator of Coy (Issue 72) or

that any claim is available in respect of interest payments made by Coy to other group companies prior to 15 February 2001 (Issue 73).

K9.2 The Commissioner should make no findings in respect of these Issues.

AJ Meagher

MJ Leeming

PJ Brereton

C Mantziaris

29 July 2004