

The appeal by the James Hardie directors and officers

Morley v ASIC (2010) 274 ALR 205; [2010] NSWCA 331

In December 2010, the NSW Court of Appeal handed down judgment¹ in the appeal by the non-executive directors, the chief financial officer and the secretary/general counsel of James Hardie Industries Ltd (JHIL) from the decision of Gzell J.²

Background – the misleading ASX announcement

In February 2001, JHIL issued an announcement to the ASX that it had established a foundation to meet the compensation claims of asbestos sufferers against former subsidiaries of JHIL. The announcement stated that the foundation had sufficient funds to meet all legitimate compensation claims and was ‘fully funded’. Gzell J found this to have been a misleading statement likely to affect market behaviour.⁴

At first instance, it had been found that the non executive directors had breached their duty of care and diligence in approving a draft of the ASX announcement at a board meeting on 15 February 2001. JHIL’s secretary/general counsel (Mr Shafron) and CFO (Mr Morley) were also found to have breached their duties as officers by failing to provide advice and information to the board in connection with the announcement.

The appeal

The Court of Appeal⁵ delivered one judgment. The non executive directors succeeded in their appeals. Mr Shafron had some success but the court nevertheless declared that he had breached his duty as an officer of the company. The CFO, Mr Morley, failed in his appeal.

The principal issue for the non executive directors was whether ASIC had established that the draft ASX announcement had been approved by the board at the meeting (as the minutes indicated had occurred). One of the non executive directors denied that he had voted in favour of any such resolution and the others did not admit it.

In particular, the court was required to consider the implications of ASIC’s failure to call three witnesses who had been present at the meeting. They were Mr Robb, a partner of Allens, (JHIL’s solicitors at the time), and two representatives of UBS, JHIL’s adviser in connection with the establishment of the foundation.



Before the hearing, ASIC had provided the appellants with lists of the witnesses it proposed to call at the trial. These included Mr Robb and the UBS representatives. However, a week or so into the hearing, ASIC informed the trial judge and the other parties that it did not intend to call Mr Robb or the UBS witnesses.

In this context, the court considered the obligations of a government regulator, such as ASIC, in the conduct of proceedings to enforce the civil penalty provisions of the Corporations Act.

No prosecutorial duty, but a duty to act fairly

The Court of Appeal rejected a submission that ASIC, in taking proceedings to enforce civil penalty provisions, was under a duty akin to a prosecutorial duty.⁶ However it did find, and indeed ASIC did not dispute, that, as a government agency enforcing civil penalty provisions, ASIC had an obligation to act fairly in the conduct of the proceedings. The particular content of the obligation would depend upon the circumstances of the case, although it could not rise higher than the duty imposed on prosecutors to call material witnesses.

The court concluded that ASIC had breached its duty of fairness in failing to call Mr Robb.⁷ The court then had to consider the implications this had for ASIC’s case.

Gzell J had, at first instance, come to conclusions on each of the issues raised without the need to draw, against ASIC, a *Jones v Dunkel* inference in respect of the evidence of Mr Robb and the UBS witnesses.⁸

The Court of Appeal noted that the application of *Jones*

v Dunkel leads only to an inference that the evidence of witnesses not called would not have assisted ASIC's case. Such an inference would be entitled to some weight but would not be of high, let alone determinative, significance.⁹ The court found that ASIC's failure to call Mr Robb went beyond a *Jones v Dunkel* inference. It affected the overall assessment by the court of the cogency of the evidence adduced by ASIC.

Significantly, there was no dispute that *Briginshaw* principles (and their statutory embodiment in section 140 of the Evidence Act) applied to ASIC's case, having regard to the gravity of the consequences of adverse findings against the directors.

The court described the consequences of a breach of the duty of fairness in the following terms:¹⁰

In order to be satisfied on the balance of probabilities within the meaning of s.140, the tribunal of fact must reach an affirmative conclusion, or a definite conclusion, or an actual persuasion. This state of mind turns on the cogency of the evidence adduced before it. Relevant to the cogency of the evidence actually adduced is the absence of material evidence of a witness who could have been called and in fulfillment of the duty of fairness should have been called. In *Whitlam v Australian Securities and Investments Commission* it was said that, absent diligence in calling available evidence, a court is left to rely on uncertain inferences. The case of the party in default suffers in its cogency, and it is made more difficult for the tribunal of fact to reach an affirmative conclusion, a definite conclusion or an actual persuasion: the more so if the *Briginshaw* principles involving the gravity of the consequences apply.

ASIC's failure to call Mr Robb critically undermined the court's assessment of the cogency of its evidence. It could not discharge its burden of proving that the non executive directors had voted in favour of the draft ASX announcement. Without this factual basis, the findings of breach against the non executive directors could not stand.

Findings of breach would have been made against the non executive directors if ASIC had discharged its burden of proof

The court held that, if ASIC *had* established that the non executive directors had approved the announcement, they would have been in breach of their duty of care

and diligence. They could not, in the circumstances of this case, have avoided liability by reliance on management. Even those directors who had joined the meeting by telephone would have been in breach of their duty by failing to familiarize themselves with the resolution (failing which, they should have abstained from the vote).

General counsel and CFO were 'officers' of JHIL

The Court of Appeal also confirmed the finding of the trial judge that the general counsel and CFO (neither of whom were directors) were both 'officers' of JHIL and therefore subject to the relevant statutory duties. The court did not accept that their role was limited to advising or informing the board and found that they had sufficiently participated in the decision to render them liable as officers of the company.

Special leave application

ASIC, Mr Shafron and Mr Morley have each filed applications for special leave to appeal the decision of the Court of Appeal.

By Vanessa Thomas

Endnotes

1. *Morley & ors v Australian Securities and Investments Commission* [2010] NSWCA 331.
2. *Australian Securities and Investments Commission v MacDonald (No 11)* [2009] NSWSC 207. On the appeal, this was referred to as the *Liability Judgment*. In a separate judgment, *Australian Securities and Investments Commission v MacDonald (No 12)* [2009] NSWSC 714, Gzell J made orders in relation to applications for relief from liability for contravention and on pecuniary penalties and disqualification orders. One of the directors, the CEO, Mr MacDonald, did not appeal from the findings of Gzell J.
3. In a separate judgment handed down at the same time (*James Hardie Industries NV v Australian Securities and Investments Commission* [2010] NSWCA 332), the Court of Appeal dismissed an appeal by the company from this finding.
4. Spigelman CJ, Beazley and Giles JJA.
5. At [678] to [700], seeing no reason to depart from its earlier rejection of it in *Adler v Australian Securities and Investments Commission*.
6. A majority (Spigelman CJ and Beazley JA) did not consider that the same duty required that ASIC also call the UBS witnesses. Giles JA did not agree, but this had no effect on the overall result of the appeal.
7. *Liability Judgment* at [1139], see Court of Appeal judgment around [633]. Gzell J considered that Mr Robb and the UBS witnesses were equally available to all of the parties.
8. At [731] to [732].
9. At [753].