

In the past year, much has been said about what James Hardie did and sought to do in relation to the establishment of the Medical Research and Compensation Foundation ("the Foundation") and James Hardie's subsequent group restructuring. These were complex transactions which have frequently been misunderstood or misrepresented, as have the company's actions and objectives.

To facilitate a more informed understanding, we have set out below some of the key events and their context.

## **PRIOR EVENTS**

### **16 February 2001**

The Board of James Hardie Industries Limited ("JHIL", now ABN 60) established the Foundation to provide financial compensation for those with asbestos-related diseases and, at the same time, to assist James Hardie to focus on the pursuit of international growth opportunities by removing asbestos liabilities from its balance sheet.

The Foundation was created as a dedicated organisation to manage and deal with the asbestos liabilities of the former subsidiaries of JHIL which were transferred to it.

As part of considering the establishment of the Foundation, the JHIL Board commissioned and received actuarial advice as to the actuarial best-estimate of future asbestos claims. That advice was believed by the JHIL directors to be a reliable actuarial report, partly because

it was broadly consistent with previous such reports provided to JHIL over a number of years. Taking into account that advice, the Foundation was provided with A\$293 million of cash funds as well as income-producing assets, including additional funding provided by JHIL itself, to meet the actuarial best estimate of future claims.

The money provided to the Foundation included funds for medical research aimed at finding treatments and cures for asbestos-related diseases and it continues to be involved in this area.

The board of JHIL at the time considered these arrangements were in the best interests of both JHIL and asbestos claimants.

### **29 October 2003**

In the course of filing its year-end financial accounts, the directors of the Foundation announced that they had obtained revised actuarial advice which predicted a future total liability of A\$1.089 billion which resulted in an estimated funding shortfall of approximately A\$800 million. This shortfall was at odds with the actuarial advice that JHIL directors had previously received and which they had thought was reliable.

In considering how it could offer the Foundation further funding, in the interests of all stakeholders, James Hardie directors needed to work through a huge range of complex factors, which took (and which continue to take) considerable time.

### **25 February 2004**

The NSW State Government announced that Mr David Jackson QC would conduct a Special Commission of Inquiry (SCI) into the establishment of the MRCF (the Foundation). James Hardie welcomed the SCI but expressed concern that the terms of reference failed to examine the impacts of the alleged blow-out in asbestos liability claims on all parties, including the NSW Government.

### **16 March 2004 (to 13 August 2004)**

The SCI held public hearings at which the Commissioner and representatives of all those admitted to appear questioned individuals about the events being considered by the SCI. James Hardie pursued a policy of dealing with the issues to be addressed in the Commission and not in the media. We sought at all times to be respectful of the Commission and complied with all requests that the Commission made of us in terms of providing information and making available company officers and employees.

### **7 June 2004**

The different actuarial estimates, which led to varying shortfall figures, and the known excesses in the claims system, did not provide any basis for assessment of affordability and certainty for the Board to consider the development of a funding proposal that might be put to shareholders. Therefore, James Hardie commissioned a new actuarial report from KPMG Actuaries, and submitted it to the Commissioner on

# Special Commission of Inquiry and Asbestos Compensation

This document does not aim to present arguments for or against the company's voluntary funding proposal. These will be the subject of a separate Explanatory Memorandum which will be provided to holders in advance of an Extraordinary General Meeting which will be called to allow debate and voting on the proposal.

7 June 2004. The report provided an independent actuarial review of future asbestos liabilities of the former James Hardie subsidiaries Amaca and Amaba, as well as KPMG Actuaries' view of historical and then-current projections by other actuaries and highlighted "an unforeseeable upward trend" in claims numbers and average claims costs in recent years.

Based on the information that would have been available to actuaries, Trowbridge, at the time it prepared its actuarial report for JHIL in February 2001 (and upon which the funding for the Foundation was based), KPMG Actuaries believed its best estimate would have been in the order of A\$694m. The equivalent Trowbridge figure at that date was A\$323m. James Hardie directors expressed their concern at the different figures, and announced they were considering the implications of the report.

#### **30 June 2004**

Following hearings, but in advance of the deadline for submissions from all parties, Counsel Assisting the SCI released his Issues Paper, making contentions about the actions of the company and its officers. In accordance with the processes of the Commission, James Hardie undertook to respond to these contentions in its submission to the inquiry.

#### **14 July 2004**

The Board announced that it would recommend that shareholders approve the provision of additional funding to enable an effective statutory scheme to be established to compensate future claimants for asbestos-related injuries caused by former James Hardie Australian subsidiary companies. The company confirmed its willingness to contribute to a resolution in the best interests of all parties, including current and future Australian asbestos claimants against the Foundation, James Hardie shareholders and other constituents.

A submission discussing these issues was provided to the SCI in response to Term of Reference 4. The submission did not propose a cap on payments to claimants and did not impose detailed requirements by the company because the Board believed it best to make the broad proposal and to leave the details for subsequent discussion. It did,

however, seek a significant reduction in legal costs in light of these being a large component of the total liabilities and the extensive cost savings that it had identified could be achieved without detracting from the rights of claimants.

#### **19 July 2004**

The Board announced the establishment of a Board Special Committee to oversee the company's further participation in the SCI, including reviewing the SCI's report and recommending appropriate actions in response to its findings; and overseeing any developments or discussions of suitable arrangements to ensure all legitimate claimants receive fair and equitable compensation.

#### **28 July 2004**

All parties' submissions to the SCI were released. In its submissions, James Hardie vigorously defended the company, its directors and officers against allegations made in others' submissions and confirmed the company's earlier proposal for a Board recommendation that shareholders approve the provision of additional funding if an effective statutory scheme was established. The submission outlined the key principles of a proposed scheme which, again, did not include a cap on payments to claimants.

#### **11 August 2004**

James Hardie Chairman, Alan McGregor, resigned due to ill health and Meredith Hellicar was named as the company's Chairman. In public statements following her appointment, Ms Hellicar apologised to those affected by asbestos for the stress and uncertainty caused because the Foundation set up to meet their claims proved to have insufficient funding, and confirmed plans to put to shareholders a proposal that the compensation to which these people are entitled be continued to be provided in a manner that is speedy, fair and equitable.

#### **12 August 2004**

In its concluding submissions to the SCI, James Hardie provided more detail about the scheme proposed in its 14 July offer to recommend to shareholders that they fund an appropriate scheme. While affirming the company's legal position, the

Board said it believed the proposal would be in the best interests of asbestos claimants and their families, as well as the best interests of James Hardie shareholders.

#### **13 August 2004**

In response to questions from Mr Jackson in the SCI, James Hardie provided additional information about its funding proposal.

#### **10 September 2004**

James Hardie deferred a resolution to adopt its annual Dutch GAAP accounts for the year ended 31 March 2004 at its upcoming AGM to provide the opportunity, if necessary, to accommodate any impact the SCI's report might have on the company's financial statements. The company also announced that its Audit Committee had commissioned an internal investigation, to be conducted by independent legal and other advisors, to investigate any potential impacts on the financial statements of the various allegations of illegal acts made during the SCI's proceedings.

#### **15 September 2004**

James Hardie Chairman, Meredith Hellicar, delivered her address to the company's Annual Information Meeting of Security Holders in Sydney. Ms Hellicar reassured holders that the Board was focussed on finding a solution that:

- addressed in an affordable way, the issue of funding compensation for victims of asbestos-related diseases caused by James Hardie's former Australian subsidiaries;
- addressed the concerns of the community; and
- allowed the company to meet its responsibilities to its shareholders and employees.

#### **21 September 2004**

Mr David Jackson QC presented the SCI Report to the NSW Government.

In relation to *Terms of Reference 1: Adequacy of the MRCF funding*, Mr Jackson found there was a significant estimated funding shortfall in relation to the asbestos related liabilities of Amaca and Amaba. In part this was based on an actuarial report prepared by KPMG Actuaries, commissioned by James Hardie for the purpose of the SCI indicating that

the discounted value of the central estimate of the asbestos-related liabilities of Amaca and Amaba was approximately A\$1.5 billion. Mr Jackson accepted this figure as the minimum central estimate but concluded that a significantly greater sum would be required to provide a high degree of assurance that all future claims would be met. He found that the net assets of the Foundation and ABN 60 (estimated to be \$179.2m as at 30 June 2004) were not sufficient to meet these prospective liabilities and were likely to be exhausted in a relatively short timeframe (the first half of 2007).

In relation to *Terms of Reference 2: Separation of the MRCF*, Mr Jackson observed that James Hardie was “perfectly entitled to seek a means whereby it could pursue its business aims without being perceived, rightly or wrongly, as associated with ongoing asbestos liabilities”. He also indicated that the establishment of the Foundation and the establishment of the ABN 60 Foundation were legally effective and that, accordingly, although any liabilities remained with Amaca, Amaba or ABN 60 (as the case may be), no significant liabilities for those claims could likely be made directly against James Hardie or any of the other entities in the James Hardie Group.

Mr Jackson also found that it was not possible, in money terms, to say that separation directly resulted in, or contributed to, a possible insufficiency

of assets to meet the future asbestos-related liabilities of Amaca and Amaba; however, he expressed an opinion that “in practical terms” the separation was likely to have had such an effect because if separation had not taken place in February 2001 he thought that it seemed likely that, for the indefinite future, the asbestos-related liabilities would have been treated, as they had been for years, as one of the annual expenses of the James Hardie Group.

In relation to the circumstances of the establishment of the Foundation, Mr Jackson made certain adverse findings against, amongst others, Mr Macdonald (the former CEO of ABN 60 and James Hardie) and Mr Shafron (the former General Counsel of ABN 60 and James Hardie and former CFO of James Hardie). In particular, Mr Jackson noted that he found it difficult to accept that JHIL management “could really have believed that the funds of the Foundation would have been sufficient to enable it to pay all future legitimate asbestos related claims against Amaca and Amaba”. Accordingly, Mr Jackson considered that certain elements of press releases issued by JHIL at the time of the establishment of the Foundation, which conveyed that the Foundation had been provided with sufficient funds, were “seriously misleading”.

It is important to note, however, that the SCI also found that the alleged conduct did not cause any material loss to the Foundation or to the

asbestos claimants which would create a valuable cause of action against, and therefore a material liability of, any James Hardie entity or would lead to any of the restructuring arrangements being reversed. Mr Jackson noted that there were significant hurdles, which might be insuperable, to establishing any liability in respect of these claims against James Hardie, ABN 60 or their respective directors, and that even if such liability were established there were further hurdles which might prove to be insuperable against any substantial recovery or remedy by such potential claimants in respect of them.

In relation to *Terms of Reference 3: Corporate Restructures*, overall the SCI report found that the relevant corporate restructures conducted by JHIL and James Hardie over several years were for valid business reasons and did not adversely affect the Foundation’s ability to meet its current and future liabilities.

On *Terms of Reference 4: Adequacy of current arrangements*, Mr Jackson concluded that the current insolvency arrangements available to the Foundation under the Corporations Act would not assist the Foundation to manage its liabilities. He went on to note that the best long term solution for satisfying the asbestos-related liabilities of Amaca, Amaba and ABN 60 would be a scheme, for which that proposed by James Hardie during the SCI hearings might be a starting point.

## Special Commission of Inquiry and Asbestos Compensation

The company issued a statement acknowledging the seriousness of the findings and comments of the Commissioner and advised that the Board Special Committee and the Board would review the report accordingly and, after undertaking a full analysis, issue a response.

The statement noted Mr Jackson's remarks about the scheme proposed by James Hardie and reconfirmed the company's funding proposal and its willingness to work with all relevant stakeholders in developing a satisfactory compensation solution for asbestos claimants against its former subsidiaries which it could put to shareholders for approval.

The NSW Government rejected James Hardie's proposal for a statutory scheme, stating it would not consider implementing any proposal advanced by James Hardie unless it was the result of an agreement reached with the union movement acting through the ACTU, UnionsNSW as well as representatives of the asbestos claimants. These groups rejected the statutory scheme.

#### **28 September 2004**

Three working days after James Hardie directors around the world received a copy of the SCI report, the Board announced that, effective immediately, Peter Macdonald would stand aside as Chief Executive Officer and Peter Shafron would stand aside as Chief Financial Officer.

In a separate statement to the ASX, Peter Macdonald said he would vigorously defend himself against the allegations at the appropriate time, and that he would continue to work in the best interests of the company and its shareholders to ensure the company continued to grow and perform.

#### **1 October 2004**

James Hardie representatives began discussions with the ACTU, UnionsNSW and a representative of asbestos disease groups to try to reach an agreement on an appropriate manner in which the company might fulfil the original intention in the establishment of the Foundation.

The Board considered this move to be consistent with its duties to shareholders and, where applicable, other stakeholders, particularly given the original intentions in the establishment of the Foundation, the disruptive effects of adverse publicity, product bans and boycotts and the uncertainty regarding the scope or impact of any legislation that could be introduced in the absence of any further action by the company.

#### **18 October 2004**

In response to comments by the ACTU, James Hardie re-confirmed its commitment to achieving a sustainable long-term compensation solution for asbestos disease sufferers as quickly as possible. The company said it wanted an outcome that was not only acceptable to the ACTU and asbestos disease sufferers, but also one that could be supported by shareholders and financiers.

#### **22 October 2004**

After a review conducted by external legal advisers did not result in any finding that Mr Macdonald had breached the terms of his employment agreement with the company in relation to the activities and transactions under review (noting the administrative status of the SCI), Peter Macdonald resigned from the company and received his contractual entitlements.

Mr Macdonald was engaged as a consultant for an initial term of three to six months to assist in the efficient transition of his duties as Chief Executive Officer to his successor, and then for a further 24 months to provide advisory or consultative services requested by the company. Louis Gries was appointed interim CEO.

Peter Shafron also resigned from the company, and was engaged as a consultant for a period of 24 months to provide advice to the company in relation to the work attended to by Mr Shafron while he was General Counsel of the company. Russell Chenu was appointed interim Chief Financial Officer.

#### **25 October 2004**

Although the Foundation had a shortfall in the longer term, it had sufficient funding at the increased rate of claims and costs for a number of years. Indeed no person entitled to compensation has gone unpaid. Despite this fact, James Hardie wrote to the Foundation reaffirming its preparedness to provide assistance for its claimed interim liquidity position and reiterated that it is in no-one's interests to have the Foundation placed in a position where it is unable to pay legitimate claimants.

#### **16 November 2004**

James Hardie offered new arrangements to the Foundation to ensure asbestos victims with legitimate claims would have access to further funding.

Following public statements by the Foundation that it required additional cash funding to remain solvent, James Hardie offered an indemnity to the ABN 60 Foundation directors to facilitate the immediate provision by ABN 60 of \$88.5 million in cash to the Foundation.

In addition to offering the indemnity to ABN 60, James Hardie advised the Foundation that, should its funds prove insufficient to meet legitimate claims, James Hardie intended to provide interim funding on a month-to-month basis to enable those claims to be met.

#### **18 November 2004**

James Hardie had been trying to convince the NSW Government to address the inefficiencies in the claims system. Finally, the NSW Government announced a Review of Legal and Administrative Costs in Dust Diseases Compensation. James Hardie noted that the reduction of legal, administrative and other costs was an important factor in the future affordability and sustainability of the company's proposal for the long-term funding of claims.

James Hardie welcomed the government's involvement and expressed its hopes to achieve an outcome suitable to all stakeholders.

### **22 November 2004**

Announcing its results for the second quarter of fiscal year 2005, James Hardie advised that the internal investigation into allegations of illegal conduct raised during the SCI and any impact on financial statements had been completed, and there was found to be no impact on the company's current financial statements.

### **8 December 2004**

In response to public speculation questioning James Hardie's commitment to achieving a long-term financial agreement as soon as is possible, James Hardie provided an update on the then current state of negotiations between the company, the ACTU, UnionsNSW and asbestos support groups. The update outlined key points contained in a draft Heads of Agreement presented by James Hardie to the ACTU on 3 November and called on the NSW Government to join negotiations.

### **21 December 2004**

James Hardie signed a Heads of Agreement with the ACTU, UnionsNSW, asbestos support groups and the NSW Government, outlining the key provisions and terms on which the company proposed to provide voluntary long-term funding of asbestos related personal injury claims against former James Hardie subsidiaries.

These included:

- establishment of a Special Purpose Fund (SPF);
- initial funding of the SPF by James Hardie on the basis of the November 2004 KMPG Actuaries' report (with a net present value central estimate of A\$1.5 billion); the actuarial assessment is to be updated annually;
- a two year rolling cash buffer in the SPF;
- a cap on the annual payments made by James Hardie to the SPF, initially set at 35% of operating cash flow; and
- no cap on individual payments to proven claimants.

A key principle underlying the agreement was the fact that, to achieve the long-term funding, James Hardie had to remain profitable and strong and be able to continue to successfully grow its business.

The arrangement is subject to a number of conditions precedent, including implementation of the findings of the NSW Government's Review of Legal and Administrative Costs; other legislation to facilitate the effectiveness of the voluntary funding arrangement; entry by the principal parties into a long-term funding agreement; the obtaining of tax deductibility for payments by the company; recommendation of the voluntary funding proposal by the Board, following receipt of a report from an independent expert of its review and analysis of the funding

proposal; and approval of the voluntary funding proposal by the Company's shareholders and lenders.

Based on current actuarial estimates and market expectations of James Hardie's future financial performance, the proposed annual payment caps are intended to allow payments to claimants not only to be properly funded but also to have the benefit of significant contingency provisions. However, because the number of claimants and the amounts that the courts may award cannot be known specifically in advance, and James Hardie may not perform as the directors might hope, no absolute assurance on this can be given.

### **8 March 2005**

The NSW Government announced the results of its Review into the Legal and Administrative Costs of Dust Diseases Compensation. James Hardie acknowledged the recommendations as a positive first step towards establishing a more efficient system.

### **31 March 2005**

James Hardie and the Premier of New South Wales, the Hon Bob Carr, provided updates on the timing of the Principal Agreement to be signed between James Hardie and the NSW Government. The updated timetable had the signing of the Principal Agreement to occur in early June, reflecting the complexity of the legal and administrative issues surrounding the establishment of the Special Purpose Fund.

# Special Commission of Inquiry and Asbestos Compensation

## **POST 31 MARCH 2005 EVENTS**

### **15 April 2005**

The Board confirmed that the SPF would cover proven claims by members of the Baryulgil community (former asbestos mine workers and residents) against the former Australian subsidiary, Asbestos Mines Pty Ltd for the period during which it was owned by James Hardie (until 1976). Further, the Board decided to expand the coverage of the SPF to assume coverage for the subsequent period of the mine's operation, during which Asbestos Mines Pty Ltd was owned by Woodsreef Mines Ltd (now Mineral Commodities Ltd). This was because Asbestos Mines Pty Ltd (since renamed Marlew Mining Pty Ltd) went into liquidation in 2002 and there was therefore uncertainty regarding the availability of funds from its parent, Mineral Commodities Ltd, for future asbestos claims relating to Asbestos Mines Pty Ltd during its period of ownership.

James Hardie proposed that any such valid and proven claims against Asbestos Mines Pty Ltd not otherwise recoverable from any assets of Asbestos Mines Pty Ltd; or any insurers of Asbestos Mines Pty Ltd; or other parties from whom the claimant can recover compensation, would be able to be covered by the SPF. Any such claims against the SPF would also need to be funded within the cash flow cap set out in the Heads of Agreement.

### **16 May 2005**

As part of its 4th Quarter and Full Year results presentation, James Hardie provided the market with an update on the voluntary asbestos funding proposal, reporting considerable effort and steady progress on the finalisation of the Principal Agreement. The update noted that the timetable announced on 31 March 2005 now appeared to be ambitious, given the complexity of some of the issues being dealt with.

At the same time, James Hardie released an updated report from KPMG Actuaries, providing a Net Present Value estimate of liability at 31 March 2005 of A\$1,684.9 billion. The figure had not been adjusted for estimated savings from the NSW Government Costs Review.

### **21 June 2005**

James Hardie and the NSW Premier separately announced an updated timetable which had the signing of the Principal Agreement scheduled for late July/early August and the shareholder meeting to consider the voluntary funding proposal being held in late September/early October 2005.

The further delay was attributed to complex issues including the interaction of Australian, Dutch and US law.

### **Other**

The Board believes that the company cannot commit to providing any funding support to address the funding shortfall affecting the Foundation in the absence of shareholder approval, because:

- Under Dutch law, a commitment made to such a proposal would have an impact on the identity or character of the company, in particular by adding asbestos liability issues to the company, and in such circumstances Dutch law requires shareholder approval;
- It is consistent with the corporate governance practices of the company and the expectations of the company's shareholders; and
- In the absence of a current legal obligation to make such payments, it is simply prudent, in light of their significance, for directors to have their business judgment considered through a shareholder approval process.

Holders will receive additional information about the proposed scheme and meeting in a separate mailing.