CHARTERED SECRETARIES
AUSTRALIA

Leaders in governance

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Dear Mr Kluver

Long-tail liabilities: the treatment of unascertained personal injury claims

Chartered Secretaries Australia (CSA) welcomes the opportunity to comment on the discussion paper, *Long-tail liabilities: the treatment of unascertained personal injury claims*, which deals with proposals for the treatment of long-tail liabilities for solvent companies and companies in external administration.

CSA is the peak professional body delivering accredited education and the most practical and authoritative training and information on governance, as well as thought leadership in the field. We are an independent, widely-respected influencer of governance thinking and behaviour in Australia. We represent over 8,000 governance professionals working in public and private companies, a number of whom have been involved in class actions or who have had to consider the impact of 'dangerous products', which at this point in time refers to asbestos. We have drawn on their experience in the formulation of this submission.

General comments

CSA notes that the rationale for both the referral of a proposal to extend existing statutory creditor protections to unidentified future personal injury claimants (UFCs) against companies where a mass future claim is afoot (Referred Proposal) and the discussion paper issued by the Corporations and Markets Advisory Committee (CAMAC) came from the *Report of the Special Commission of Inquiry into the Medical Research and Compensation Foundation* (the James Hardie Inquiry). The James Hardie Inquiry found that the current external administration mechanisms do not give adequate recognition to the existence of long-tail liabilities arising in the case of unascertained future creditors, including persons who have suffered injury through exposure to products where the injury does not manifest itself until after the time of the external administration.

In its initial submission, dated 17 February 2006, a copy of which is attached, CSA highlighted a number of concerns focused on the damage that could follow any undue delays in the winding up of companies.

At the time of the Referred Proposal, the situation with James Hardie was unfolding, and it was unclear if the current law was able to deal with long-tail liabilities and the treatment of unascertained personal injury claims. However, CSA notes that the current law did not fail in dealing with this issue, and that the passage of time since the Referred Proposal was formulated has clarified the capacity of the current law to achieve a solution.

CSA therefore strongly recommends that any amendment to the law in relation to long-tail liabilities and the treatment of unascertained personal injury claims should be limited to extreme cases only, where there are prescribed 'dangerous products' that have become publicly identified with the risk of UFC claims. CSA notes that, at the current time, the only 'dangerous product' that has been so identified is asbestos.

Any reform of the law on this issue should clearly not apply where there is only a chance of future claims or where claims only become apparent with hindsight and could not have been reasonably foreseen at the time.

Any amendment of the law beyond extreme cases has the potential to introduce profound uncertainty in relation to the decision-making of directors and the existing protections for creditors and shareholders. Such uncertainty would cause considerable paralysis in decision-making, which in turn would have a profound impact on the regular ongoing management of companies and the value of shares.

CSA also notes that the discussion paper states that it does not address taxation matters. CSA, however, firmly believes that CAMAC cannot make a final recommendation to the government on the issue of long-tail liabilities and the treatment of unascertained personal injury claims without reference to the taxation impact on shareholders. This would particularly be the case if the rights of shareholders to claim a capital loss upon liquidation of a company were to be deferred indefinitely while claims of UFCs were being tested.

CSA recommends that there be no determination in this area that disadvantages shareholders, including on taxation issues.

Definition of mass future claim

CSA does not believe that it is appropriate to have a 'mass future claim' threshold test for the application of additional protections for UFCs.

CSA recommends that definition by regulation be the approach that is taken, with the Corporations Regulations prescribing 'dangerous products' that have become publicly identified with the risk of UFC claims (including asbestos products). Any definition should be limited to dangerous industries and extreme cases.

Any other approach has the potential to introduce uncertainty and paralysis. The introduction of a 'mass future claim' threshold would invite speculative claims that would significantly impair the day-to-day operations of companies. The uncertainty of application would paralyse the process, no matter how valid the claim.

Solvent companies

CSA believes that a complete prohibition on capital management for companies with UFC claims would severely affect them and is not appropriate.

CSA recommends that solvent companies subject to claims by UFCs should only have to take into account the interests of UFCs in situations of significant capital reconstruction or insolvency. In these limited circumstances, directors should have to take all reasonable steps to take the interests of UFCs into account. CSA notes that a scheme of arrangement is a capital reconstruction.

CSA strongly opposes any requirement for solvent companies (whether or not facing a mass future claim) to disclose the existence of UFCs, as such disclosure would invite speculative claims, regardless of their validity.

CSA can see the merit of such disclosure in very limited circumstances where regulation has prescribed a 'dangerous product'.

CSA also strongly opposes any extension of UFC provisions to dividends, for the reasons outlined in the discussion paper on page 51. CSA notes that the Referred Proposal did not refer to dividends and CSA believes this was correct, given the interference with the regular ongoing management of companies and their operations that such a proposal would introduce.

CSA also notes that any extension of UFC provisions to dividends would cause loss of value to shareholders, and reiterates that any determination on the issue of long-tail liabilities and the treatment of unascertained personal injury claims should not disadvantage shareholders.

CSA does not support a new provision or possible new procedure to be utilised by companies that anticipate the likelihood of becoming insolvent in the future as UFC claims crystallise through the development of injury-related symptoms.

Liquidation

CSA opposes UFCs being categorised as preferred creditors.

CSA recommends the establishment of a contingency fund where a mass future claim is afoot and, in the context of a liquidation, that:

- while there is always a risk that the contingency funding will be underestimated, it is neither practicable nor desirable for the legislation to regulate such a risk. Moreover, this risk is balanced by the certainty granted to unsecured creditors who are not mass future claimants and shareholders that they need not wait many years for payment
- the distribution of any surplus from the contingency fund after UFCs have been paid should also be left to the determination of the fund administrator at the appropriate time
- the judge dealing with a class action involving mass personal injury claims should be granted the power to take into account the amount to be set aside in a contingency fund, which could be administered by the court or by a court-approved body, such as an insurance company or an external fund administrator, long after the winding up is completed
- any reform to introduce a contingency fund should ensure that it does not create any undue delay in the winding up of a company, which would disadvantage creditors and shareholders, for instance, by interfering with the liquidator's decision about how to deal with assets. There should be suitable mechanisms to allow the early crystallisation and assessment of UFC claims to permit liquidation to be completed within a reasonable time.

CSA supports the procedure set out in the discussion paper under 8.4 on page 89.

Anti-avoidance provision

While CSA had noted in its earlier submission of February 2006 that, in principle, it had no objections to the inclusion of an anti-avoidance provision in the Referred Proposal, the intervening months have clarified that the current law did not fail in relation to the James Hardie situation.

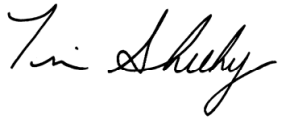
Within this context, CSA opposes the introduction of an anti-avoidance provision. CSA notes that the current law relating to capital reconstruction and insolvency already deals with creditor protection. Directors have a positive obligation to protect creditors' interests, which would include UFCs. If they do not protect creditors' interests, directors should be exposed to liability.

Conclusion

CSA continues to recommend that any reform in relation to long-tail liabilities and the treatment of unascertained personal injury claims should not interfere with existing creditors' or shareholders' rights, including taxation issues for shareholders.

CSA would welcome further contact during the consultation process and the opportunity to be involved in further deliberations.

Yours sincerely



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