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MYER SHAREHOLDER CLASS ACTION

BRIEFING PAPER

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Myer shareholder class action

On 24 October 2019, Justice Beach of the Federal Court of Australia delivered the first judgment in a shareholder class action in Australia.

The decision in *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited* [2019] FCA 1747 provides some initial clarity on unsettled areas of Australian law and is an important reminder to companies, directors and officers about the operation of aspects of the continuous disclosure regime.

It is an interesting historical footnote that the Myer decision was handed down on the 90th anniversary of the 1929 Wall Street crash. The Great Depression led to tighter securities regulation in the United States, including legislation that now includes provisions which were the catalyst for the US concept of “fraud on the market”.

In the Australian context, the Myer decision supports securities regulation, describing the key purpose of the continuous disclosure laws as being: “*to produce a well-informed market leading to greater investor confidence*.”

However, whether the decision changes the landscape for shareholder class action activity in Australia remains to be seen. The acceptance of market-based causation removes potential obstacles for applicants, but the decision exposes the significant complexity surrounding measuring and proving loss, a critical consideration for those considering the commercial viability of claims and the decisions around how to run and defend them.

In addition, it has to be borne in mind that the case involves unusual underlying factual circumstances, in which the company’s CEO provided “de facto” guidance to the market notwithstanding the Board’s decision that the company would not do so, and the updated guidance which the Court has concluded *should* have been provided was no more negative than the assessments the analysts were making in any event.

The facts

As matters evolved prior to and during the trial, the lead applicant’s claim ultimately centred on statements made by Myer’s CEO during earnings calls with equity analysts and financial journalists on 11 September 2014. These calls took place at the time of Myer’s FY14 results announcement.

Myer’s practice at that time was not to issue earnings guidance. Instead, it sought to comply with its continuous disclosure obligations by monitoring analysts’ consensus.

At a Board meeting on 10 September 2014, Myer’s directors resolved (consistently with the company’s practice at the time) not to provide earnings guidance. A draft ASX announcement which contained earnings guidance was also amended to remove the reference to earnings guidance.

Despite this, Myer’s CEO publicly represented through statements he made on the earnings calls that, in his opinion, Myer’s FY15 net profit after tax (NPAT) would likely exceed its FY14 NPAT (of $98.5 million). The Court considered the CEO’s statements to be “de facto” earnings guidance by Myer.

On 19 March 2015, Myer announced that its NPAT for FY15 would likely be in the range of $75 to $80 million excluding one off costs. After the announcement, Myer’s share price fell materially.

Myer shareholders who purchased shares on or after 11 September 2014 and still held their shares on 19 March 2015 alleged that, by making the NPAT forecast in September 2014 and failing to correct it, Myer engaged in misleading or deceptive conduct and breached its continuous disclosure obligations under the Corporations Act.

The findings

In summary, the Court found that:

- There were reasonable grounds for the representation made by Myer's CEO on 11 September 2014;
- However, Myer's continuous disclosure obligations were engaged when, at various later points in time, Myer became aware that its earnings would be materially different to the CEO's representation that FY15 NPAT would likely exceed FY14 NPAT;
- From 21 November 2014 until 19 March 2015, Myer breached its continuous disclosure obligations and engaged in misleading or deceptive conduct by failing to correct the 11 September 2014 representation at various intervals;
- Despite Myer's contraventions, the breaches by the company may not have caused any loss to shareholders;
- Myer's expectation as to its NPAT during the period prior to 19 March 2015 was either above or not materially different from the Bloomberg consensus figure. As the market had already factored in a lower earnings outlook, there was no evidence before the Court that the company's breaches caused loss to shareholders;
- On 19 March 2015, the market price for Myer securities fell, not because the company revealed that it would not meet the NPAT forecast made on 11 September 2014, but because the announced guidance was below consensus.

Significantly, the Court accepted the concept of market-based causation, which negates the need for shareholders to prove that they read or relied on the company's misinformation to establish their loss.

Despite the acceptance of market-based causation, the evidence available to the Court did not establish that the price of Myer's securities was inflated by reason of the company's breaches.

Continuous disclosure

The Myer decision addresses a number of aspects of Australia's continuous disclosure regime. The relevant obligations are set out at sections 674 and 675 of the Corporations Act and in ASX Listing Rules 3.1 and 3.1A. ASX Guidance Note 8 is also relevant to the practical application of the rules.

Consensus

Listed disclosing entities may choose whether or not to provide earnings guidance.

From 2012 and at the time of the FY14 results announcement, Myer's practice was not to provide earnings guidance. Myer instead tracked analyst consensus, and monitored whether its internal forecasts were out of line with consensus.

According to Myer, at no time prior to 18 March 2015 did it hold an expectation that its NPAT was likely to be less than consensus.

The Court agreed that, absent the CEO's statements, Myer was not required under its continuous disclosure obligations to disclose its internal NPAT forecasts.

However, once "de facto" earnings guidance had been provided by the CEO on 11 September 2014, it was *that guidance* which needed to be monitored to ensure that Myer's continuous disclosure obligations were not breached.

The fact that Myer's internal forecasts were in line with consensus prior to 18 March 2015 did not change the position that Myer should have updated its guidance from 21 November 2014.

The Court considered this to be consistent with ASX Guidance Note 8, which provides: "*How does an entity determine what the market is expecting its earnings for the current reporting period to be? ASX considers that the best and most appropriate base guide to use for these purposes is: if an entity has published earnings guidance for the current period, that guidance.*"

In other words, notwithstanding that the Board had not intended to provide guidance at the time of the FY14 results, and notwithstanding Myer's practice of monitoring consensus, once guidance had been provided by the CEO (even if only verbally), the guidance became the benchmark.

The Myer decision highlights that listed companies have a positive obligation to update their guidance even if consensus:

- has already shifted to a more negative outlook; and
- is in line with the company's own (current) expectations.

> “I do not accept that consensus was the sufficient benchmark to assess materiality and Myer’s continuous disclosure obligations”
>
> **JUSTICE BEACH**

Guidance

Myer contended that the statements made by its CEO on 11 September 2014 were not published guidance or “de facto” earnings guidance as contemplated by the ASX. In addition, it argued that the CEO’s statements did not identify a firm number or a specific range and neither did Myer’s results announcement.

The statements made by the CEO included:

- “*We will therefore not only have anticipated sales growth, but anticipated profit growth this year.*”
- “*Now what we’re saying to the market is we’re going to get topline growth and net profit growth.*”
- The response “*That is correct, yes*” to an analyst’s question that Myer was “*guiding for a net profit increase 2015 on 2014 ... Is that correct?*”

The Court held that these statements were specific enough to constitute earnings guidance.

The Court’s approach provides important reminders that:

- Forecasts do not need to be numerical. Statements such as “more than last year” are sufficient to constitute de facto guidance.
- A verbal statement can be guidance. A statement does not need to be in writing or included in an ASX announcement for it to constitute guidance.
- An officer or director may be considered to be providing guidance even where the Board has not approved the statements and even if the Board has expressly decided not to provide such guidance.
- Once verbal guidance is provided, the company must monitor and update it.

The view of the Court was that in the context of the 11 September 2014 representation:

- on 21 November 2014, Myer should have disclosed to the market that its likely FY15 NPAT would not be materially above FY14 NPAT; and
- at various points in time between 21 November 2014 and 27 February 2015, Myer should have disclosed to the market its expected FY15 NPAT based on internal forecasts.

This constitutes the “counterfactual” disclosure which the Court considers should have been provided (see paragraph [16] of the judgment).

Opinions

The judgment also provides additional clarity on the issue of how the continuous disclosure regime applies to information in the nature of opinions.

The Myer decision considered the nature of the statements made by Myer’s CEO and Justice Beach was in no doubt “*that the 11 September 2014 representation was …a statement of opinion with respect to a future matter.*”

Justice Beach also expressed the view that the: *“language used by [Myer’s CEO] to describe Myer’s FY15 profit expectations was not that of mere personal opinion. Rather, his language confidently conveyed Myer’s considered expectation of improved FY15 NPAT performance.*”

The applicant argued that Myer was aware, or ought to have been aware, that its likely FY15 NPAT would not exceed FY14 NPAT, and failed to disclose this.

Justice Beach held that a company’s earnings expectation is an opinion about the future.

On 11 September 2014, Myer did not breach its continuous disclosure obligations by failing to disclose an opinion that it was unlikely to achieve FY15 NPAT in excess of FY14 NPAT because Myer did not hold an opinion to that effect.

The judgment confirmed that:

- a person cannot be found in breach of their continuous disclosure obligations if they fail to disclose an opinion they never actually held, even if they “ought to have held it”; and
- while “awareness” for the purposes of the ASX Listing Rules extends to “ought to have been aware”, that is not the same thing as “ought to have formed an opinion”.

In other words, with regard to information that comprises an opinion, Listing Rule 3.1 is not engaged where the relevant officers should have, but did not, realise the implications of information of which they were aware.

Materiality

A particularly complex aspect of the judgment concerns the issue of materiality. Information is not required to be disclosed unless it is material.

Information will be material if a reasonable person would expect it, if it were generally available, to have a material effect on the price or value of the entity's securities.

As we discuss further below, the Court found that there was no evidence that Myer's share price was inflated by reason of its contraventions.

Despite this, the Court found that a contravention had occurred, which must mean that the information which the Court considers should have been disclosed (the counterfactual disclosure) was price sensitive information.

Justice Beach explained the position as follows:

"I have found against Myer in terms of materiality. Now you might ask how then I could not find for the applicant on loss. But the answer is relatively straight-forward. … the test for materiality is looser and lower as s 677 reveals. Even if consensus had been factored into market price, that does not deny the materiality of Myer's changed expectation or opinion in relation to its own NPAT estimate in light of the 11 September 2014 representation."

Section 677 of the Corporations Act provides that a reasonable person would be taken to expect information to have a material effect on the price or value if the information would, or would be likely to, influence persons who commonly invest in securities in deciding whether to acquire or dispose of the securities.

In deciding that the updated internal forecasts were material irrespective of the Bloomberg consensus, the Court reasoned that:

- "mum and dad" investors may not be aware of consensus figures; and
- Myer has a large retail shareholder base.

These investors, according to Justice Beach, would likely have been influenced by the updated internal forecasts which the Court considers should have been disclosed.

Continuous disclosure – key points

- Disclosures made outside ASX announcements, such as comments made in briefings with analysts, investors and the media and statements made at annual general meetings, are actionable.
- Directors and officers need to prepare for and exercise caution when presenting and responding to questions at briefings.
- ASX announcements should be made before analyst briefings, and if verbal guidance is provided in a briefing, an ASX announcement setting out the guidance should be issued immediately.
- Once guidance is provided, a company must expressly update it, even if the market appears to have factored in adjusted expectations.

Reasonable grounds

The Myer decision also addresses important issues relating to the application, in the disclosure context, of the Corporations Act prohibitions on misleading or deceptive conduct.

To avoid being misleading, a statement as to a future matter (a forward-looking statement) must be made on reasonable grounds.

Because the applicant failed to prove that Myer lacked reasonable grounds for making the 11 September 2014 representation, the Court rejected the applicant's contentions that the 11 September 2014 representation amounted to misleading or deceptive conduct.

The judgment provides some assistance in the interpretation of the reasonable grounds requirement:

- In determining whether a person held reasonable grounds for a representation of opinion, the relevant inquiry is whether the facts the person possessed were capable of supporting the opinion.
- A person will have reasonable grounds for making a representation with respect to a future matter if there are facts sufficient to induce that state of mind in a reasonable person.
- The question whether there were reasonable grounds for the making of a profit forecast is to be resolved by looking at whether the director or officer had made a genuine assessment as to the appropriateness of the forecast. If a genuine assessment had been made, there would be reasonable grounds to support the making of the forecast.

However, the Court concluded that Myer engaged in misleading or deceptive conduct by not correcting the 11 September 2014 representation through the disclosure of the information set out in the counterfactual disclosure discussed above. That counterfactual comprises opinions which, in the view of the Court, Myer *did* hold at the dates in question.

Causation

A critical unsettled area of law in the securities class action context has been the issue of causation.

At a high level, the concept of causation is straight-forward: it is the link or the relationship between the contravention and the loss suffered. Causation is a necessary element that must be established.

To receive compensation in a shareholder class action, claimant shareholders must prove that the company's contravention of the continuous disclosure or misleading or deceptive conduct provisions of the Corporations Act caused their loss. Shareholders have sought to establish causation in different ways.

In the Myer decision, Justice Beach found that market-based causation is available as a matter of law. We discuss the difference between reliance and market-based causation below.

> "I have accepted the market-based causation theory"
>
> **JUSTICE BEACH**

Reliance

Traditionally in misleading or deceptive conduct cases, where a person claims to have been induced to enter into a transaction (including a transaction involving the acquisition of shares), the person must show that they relied on the misleading statement or conduct. To prove reliance a shareholder would need to show that they read and relied on the misstatement when purchasing shares.

The claim in the Myer case did not assert that shareholders relied on Myer's conduct when purchasing their shares. Rather, the claim was advanced only on the basis of market-based causation.

The Court's decision finds that while reliance may be sufficient to establish causation, it is not a *necessary* condition. In other words, reliance is one way of establishing causation but not the only way.

Market-based causation

In shareholder class actions claimants have advanced theories of causation which seek to establish the requisite link between the misconduct and the loss *indirectly*. The indirect or market-based theories of causation do not require that investors directly relied on the company's disclosure failure when the shares were purchased.

While claimants have advanced various iterations of market-based causation theories over the years, essentially the concept involves the following propositions:

- by purchasing securities on a publicly traded securities market,
- at a time when the market price for the company's securities was inflated by the company's contraventions,
- shareholders suffered loss by overpaying for their securities.

In the Myer decision, Justice Beach described the steps required to establish market-based causation as follows:

Non-disclosure of material information by the company to the market

↓

The listed price for the securities being inflated by such non-disclosure

↓

Investors purchasing the securities "on market'' at the inflated price

Justice Beach summarised the causation case of the applicant and group members as follows: *"it is said that the applicant and group members suffered loss because they overpaid for their [Myer] securities, having acquired them in a market where the price had been inflated as a result of Myer's conduct."*

In accepting the applicant's position on causation, Justice Beach accepted the concept of market-based causation and made it available as a matter of law for future class actions.

> "It is said that the applicant and group members suffered loss because they overpaid for their [Myer] securities, having acquired them in a market where the price had been inflated as a result of Myer's conduct."
>
> **JUSTICE BEACH**

Implications

As we have commented previously elsewhere, the market-based theory of causation advanced in Australian shareholder class actions (and accepted in the Myer decision) is not the same as the "fraud on the market" theory. The latter features in United States class actions and provides plaintiff shareholders with the ability to rely on a rebuttable evidentiary presumption.

Potentially, the market-based causation theory accepted in the Myer decision is less stringent than the approach in the United States.

The fraud on the market theory requires that shareholders have relied on the integrity of the market price. Any finding that a shareholder was not relying on the integrity of the market price (for example, because it was a short seller or because the shareholder knew the true position and proceeded anyway) will break the chain of causation.

The Myer decision does not expressly require shareholders to rely on the integrity of the market price. According to Justice Beach:

"*It might also be said that permitting such a theory means that, strictly, an investor may have a right to recover even if he did not hold any belief as to the integrity of the market price … But practically, most investors, if asked, would say that they held such a belief (or at least that their broker or agent held such belief) at the time of acquisition.*"

However, Justice Beach suggested that:

- actual knowledge of the true position;
- a lack of belief in the integrity of the market price; or
- purchases that would have been made even if the true position had been known;

may be circumstances which break the chain of causation but these issues and others "*are yet to be worked out*".

Causation – key points

- Market-based causation is available as a matter of law.
- Shareholders may, but are not required to, prove that they relied on the company's statements when purchasing securities.
- The circumstances within which the chain of causation will be broken in a market-based causation context are yet to be decided.
- The acceptance of market-based causation means the rate of filings of securities class actions will continue unabated.

Loss

A further important aspect of the judgment involves the Court's consideration of the appropriate method for measuring and proving loss. In the absence of judicial guidance, these issues have remained controversial and uncertain.

The Myer decision starts to bring some judicial clarity to these questions, which are key to the commercial assessments made in determining whether to commence or fund actions, and whether to defend or resolve them.

> "As the applicant only advanced a market-based causation theory and an inflation-based measure for its loss analysis for itself and on behalf of group members, all claims for damages would appear to fail."
>
> **JUSTICE BEACH**

Measuring loss

In actions to date, shareholders have alleged the measure of their loss in different ways, often pleading a number of loss measures as alternatives:

Loss measure alternatives	
inflation-based	the difference between the price at which the shareholder bought his or her interest and the market price that would have prevailed but for the contraventions
'true value'	the difference between the price at which the shareholder acquired his or her interest and the 'true value' of that interest
'left in hand'	the difference between the price paid and what is 'left in hand' upon a sale of the shares
'no transaction'	the difference between the shareholder's position as a result of having acquired the shares and the position he or she would have been in if they had not acquired the shares

Proving loss

Parties advance expert evidence in shareholder class actions to address (among other things):

- whether the alleged misstatement or non-disclosure was 'material'; and
- the impact which the alleged misstatement or non-disclosure had on the market price or 'true value' of the shares.

Applicants to date have typically relied on event study evidence, and in some cases have advanced a fundamental value analysis and/or evidence from an 'experienced investor':

- an event study uses statistical methods to seek to identify the impact of particular information released into the market on the value of a company's shares;
- a fundamental value analysis attempts to quantify, through discounted cash flow analysis, the rational value that an investor would be willing to pay for an asset if they had full knowledge of its inherent characteristics and earnings potential.

Findings

Importantly, the Myer decision accepts an inflation-based loss measure and the use of event study analysis as a means of proving such loss.

This approach, and this tool, have been central to the ways in which litigants and stakeholders have assessed the potential value of claims to date.

As no other loss measure was advanced in this case, it is not clear whether alternative loss measures will also be accepted by Courts.

> "I have also accepted and found to be valuable event study analysis in terms of assessing materiality and share price inflation."
>
> **JUSTICE BEACH**

Notwithstanding the Court's acceptance of the inflation-based loss measure and the use of event study analysis, on the facts of this particular case and the evidence before it, Justice Beach concluded that Myer's contraventions may not have caused shareholders any loss.

The reasons for this conclusion in summary are:

- the expert evidence did not prove that any share price inflation was caused by Myer's contraventions:
  - the disclosure which the applicant said should have been made (which formed the basis for the applicant's event study analysis) was not found by the Court to be the disclosure the company should have made;
  - the correct counterfactual found by the Court (being the disclosure the Court found should have been made) was not tested in the evidence;
- on the basis of the evidence that was presented, it could be concluded that there was no share price inflation as a result of the contraventions because Myer's expectation as to its NPAT at all relevant times was either above or not materially different from the Bloomberg consensus NPAT figure;
- because the market had already factored in a lower earnings outlook, there was no evidence before the Court that the company's contraventions caused any loss to shareholders.

Given the nature of these findings, more detailed questions about the practicalities of measuring and proving loss in the shareholder class action context remain matters for determination in another case. These issues include:

- the treatment of sales of shares made during the period in which the market price was inflated (and the need to net these off to avoid overcompensation); and
- the appropriate inventory methodology (LIFO, FIFO or netting) to use to determine the number of impaired shares held by claimants at the time of the corrective disclosure.

Further developments?

Various passages of the decision indicate that Justice Beach has not foreclosed the existence of loss or damage in the Myer case — for example, the statements that "the applicant and group members *may not have* suffered any loss" and that "all claims for damages *would appear to* fail" (emphasis added).

The parties have been permitted to provide short submission on a range of matters, including "*further proceedings on loss and damage*".

This seems to leave open the possibility that the applicant may be permitted to advance additional arguments concerning alternative loss measures and perhaps present additional expert evidence.

This aspect of the decision, and any further developments in this regard, may be significant, including for the way in which these cases are assessed, prepared and conducted.

Conclusion

As the first judgment in an Australian shareholder class action, the Myer decision has been much anticipated.

Whether the decision changes the landscape for shareholder class action activity in Australia remains to be seen. On the one hand, the acceptance of market-based causation resolves an area of uncertainty in favour of applicants, but the decision exposes the significant complexity surrounding measuring and proving loss, a critical consideration for those considering the commercial viability of claims and the decisions around how to run and defend them.

The decision may be limited in the extent to which it establishes wider principles of more general application given that disclosure cases, and the issue of loss in particular, are highly fact-driven inquiries.

Nevertheless, the decision provides some initial clarity and marks the start of substantive judicial guidance on important issues in securities class actions.

Loss – key points

- An event study is a useful tool for assessing loss.
- The expert evidence presented at trial did not establish that Myer's share price was inflated.
- Because the market had already factored in a lower outlook, the company's contraventions may not have caused any loss to shareholders.
- There may be further developments in the case relating to the issue of loss and damage.

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