ARTICLE

Shareholder class actions: the Myer decision – no 'one size fits all' when it comes to damages

In late 2019, the first superior court judgment in a shareholder class action in Australia was handed down by Justice Beach of the Federal Court of Australia in TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Ltd.[1]

The seminal decision clarified several important questions that had been 'known unknowns' until that point, offering important lessons to economists, solicitors and in-house counsel.

More than two years later, and despite more recent decisions, the Myer Decision still provides the most comprehensive reasoning with respect to causation, loss and damage. This paper explores the decision's implications from a forensic, economic and accounting perspective – and touches on the unsolved mysteries that may be resolved in a future Australian judgment.

We hope it assists solicitors and in-house counsel to prepare effectively for future shareholder damages cases.

SUMMARY OF KEY LEARNINGS

The Myer decision:

- Confirms it may not be safe to simply assume the market for a security is efficient without the required underlying economic analyses. Defendants can rebut the claim of an efficient market.
- Confirms "semi-strong form efficiency" as the standard in Australian shareholder litigations and discusses some criteria for demonstrating the market efficiency.
- Suggests Australian shareholder class actions do "not require reliance at all."[2] Market-based causation is a valid mechanism to evaluate causation claims in matters alleging inflation in stock price. Applicants need only prove the respondents' misstatement or omission artificially inflated the company's stock price to seek damages.
- Means that if applicants seek to claim inflation-based damages, they should review all publicly available information related to alleged misrepresentations or omissions (and not just the disclosures from the defendants) and assess whether proposed counterfactual disclosures inform the investors about something new about the company's prospects.
- Endorses an 'event study' approach for market-based causation analysis, although the choice of inflation methodology depends on the facts and circumstances of a particular matter and there can be no 'one size

[1] TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747

[2] Myer Decision, ¶1500.

fits all' approach. Here, we note that while an 'event study' can play an important role in assessing inflation, an expert should examine whether an event study by itself can estimate purported inflation, given facts and circumstances of that matter.

— Confirms that, in Australia, loss per share for a shareholder is connected to the price at which a shareholder acquired his interest. For an inflation based measure, loss per share equals the 'price paid' and the market price that would have prevailed but for the contraventions.

— Acknowledges both constant dollar and constant percentage as a potential measure of inflation and confirms that particular choice of the inflation measure in a matter will depend on the nature of proposed counterfactual disclosures and facts and circumstances for that matter.

— Suggests that the Dura methodology may not be directly applicable to Australian shareholder actions. This implies that shareholders can claim a loss even if they have sold a share prior to any corrective disclosure.

— Demonstrates the difficulties of instructing experts on issues of quantum before the Court has decided the question of liability.

— Underscores the importance for in-house counsel of 'taking stock' during rapid decision making to document a detailed and robust audit trail that will survive a forensic examination.

THE MYER CASE

Myer is one of Australia's largest department store groups, operating 60 stores across Australia. On 11 September 2014, in a session with analysts and financial journalists, Myer's Chief Executive Officer, Bernie Brooks, disclosed that he expected Myer's FY2015 NPAT to be higher than FY2014 NPAT, which was announced that day to be $98.5m.

On 2 March 2015, Myer told analysts the company was assessing its continuous disclosure obligations with reference to analyst NPAT consensus.

On 19 March 2015, Myer announced that the company expected its NPAT to be between $75 million and $80 million, excluding one-time costs. Following this announcement, the Myer share price declined by more than 10%. Finally, on 1 September 2015, Myer reported FY15 NPAT of $77.5 million.

The applicant claimed that Myer's representations caused losses to its shareholders by artificially inflating the Myer stock price between 11 September 2014 and 19 March 2015. Shareholders also claimed that Myer should have instead made a series of counterfactual disclosures.[3]

The Court's decision: Continuous disclosure breach – but no loss

The Court concluded that, while Myer did breach its continuous disclosure obligation, the applicant failed to prove that the shareholders suffered any recoverable loss due to the breach.

The decision means companies cannot walk away from their disclosure obligations simply because they think that information at issue was already public, as they can still be found to have breached the continuous disclosure rules. However, it also matters for applicants considering filing class actions. If the impact of the counterfactual disclosure is already factored into the share price on the date it should have been issued, the applicants won't be able to recover any damages under an inflation-based measure for estimating shareholder losses.

LEARNINGS FOR ECONOMIC ANALYSES

Semi-strong market efficiency demonstration is required

The Myer decision confirms that experts cannot simply 'assume' that the market is efficient. They need to demonstrate market efficiency through economic analyses. Both the market-based causation theory and the event-study methodology require the relevant security to trade in an efficient market.[4]

There are three types of market efficiency, and the Myer Court accepted semi-strong form as the appropriate standard. The Court decided that the applicants must demonstrate that the security at issue trades in a semi-strong efficient (henceforth simply "efficient") market. Under a semi-strong efficient market, "all publicly

[3] The Federal Court of Australia decision in the "TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited [2019] FCA 1747" dated 24 October 2019 ("Myer Decision"), ¶16.

[4] Myer Decision, ¶20. The Court accepted that an event study can be used to assess the materiality of events and alleged share price inflation.

available information is quickly and fully reflected in the price of a traded asset."[5]

The Court recognised that an efficient market is a rebuttable presumption and noted that, while developed markets generally exhibit price behaviour consistent with efficient markets, a firm's shares with relatively low trading may not trade in an efficient market.[6]

The Court assessed the efficiency of the market for Myer shares using five factors based on the decision in the U.S. matter Cammer v. Bloom: average weekly trading volume, analyst coverage, presence of institutional investors and arbitrageurs, market capitalisation and insider holdings, and price reaction to unexpected news.[7]

The Australian Court agreed with the Cammer decision that price reaction to unexpected news is most important because that factor "after all, is the essence of an efficient market and the foundation for the fraud on the market theory".[8] For this factor, the Court accepted the applicant's expert's analysis, which compared the proportion of news and non-news days exhibiting statistically significant price reactions.

Relatedly, we note that, in its discussion, the Court seems to offer a new test for demonstrating price reaction to unexpected news. The Court noted that "price reactions on days on which information about a company was released, either positive or negative, will typically be larger than price reactions on days without company-related disclosures," which is a testable proposition.[9] Under this test, one can examine whether the average price reactions on days with positive news is greater than the average price reaction on non-news days at a 95% confidence level. Similarly, one can examine whether the average price reaction on days with negative news is smaller than the average price reaction on non-news days at a 95% confidence level. These additional tests can bring more rigor to market efficiency demonstration as most of the Cammer factors are simply an indirect indicia of market efficiency.

The Court did not discuss how defendants can rebut a market efficiency claim. We discuss two rebuttal approaches that have been accepted by the U.S. Courts.

In the Freddie Mac securities litigation, the Court determined that the plaintiffs failed to show that the security at issue traded in an efficient market even though "the less important Cammer... factors support an inference of efficiency."[10] The Court concluded that "a cause-and-effect relationship between unexpected news and market price ... is the critical factor -- the sine qua non of efficiency". However, the lead plaintiff's expert could not demonstrate that the price for the security at issue reacted to unexpected news.[11]

In the PolyMedica Corporation securities litigation, the Court clarified the market efficiency definition and explained that if all publicly available information is fully reflected in prices, it means that the "market price responds so quickly to new information that ordinary investors cannot make trading profits on the basis of such information." The Court accepted violations of put-call parity as evidence of the market not being efficient. This is because one can use call and put options to create a synthetic stock whose payoff, in an efficient market, should mimic the payoff of the stock underlying these options. When a put-call parity is violated, this means that investors can make trading profits, which demonstrates that the stock is not trading in an efficient market.

The above examples illustrate the nature of the economic analysis required to demonstrate the efficiency of the market - a requirement confirmed to be relevant in Australian shareholder class actions by the Myer decision.

Market-based causation is acceptable to evaluate causation and potential

Turning back to the Myer case, the Court accepted market-based causation as a mechanism for examining causation claims of applicants proffering inflation as a measure of damage claims. The Court viewed the market-based

[5] Myer Decision, ¶675.

[6] Myer Decision, ¶¶676-677

[7] Based on five indicia identified in the decision in the U.S. matter Cammer v. Bloom, 711 F. Supp. 1264 (D.N.J. 1989) [8] Myer Decision, ¶687.

[9] Myer Decision, ¶687.

[10] In re Federal Home Loan Mortgage Corp. (Freddie Mac) Securities Litigation ["Freddie Mac Series Z Decision"], p. 21. The court deemed following factors as less important: a) average weekly trading volume, b) listing on a major exchange (NYSE), c) market capitalisation, d) rating agency reports, e) bid-ask spread, f) market capitalisation, and g) public float.

[11] Freddie Mac Series Z Decision, pp.23 -24.

[12] Myer Decision, ¶1528.

causation approach as essentially "a 'but for' approach... or a 'common sense' approach."[12] The Court confirmed that, for an inflation scenario, the causation approach works as follows:[13]

- A company fails to disclose material information;
- The listed price of its securities becomes inflated; and
- Investors purchase securities "on market" at the inflated price.

The Court distinguished the market-based causation approach from the "fraud on the market" doctrine, which was accepted by the U.S. Supreme Court as an alternative way of demonstrating reliance in its seminal decision in Basic Inc v Levinson.[14] The doctrine "embodies a rebuttable presumption that investors have relied on the integrity of the market price when deciding to purchase on market."[15] The Court noted that Australian shareholder class actions do "not require reliance at all."[16] In other words, applicants need only prove that the respondents' misstatement or omission artificially inflated the company's stock price to seek damages.

From an economic point of view, both market-based causation and fraud on the market doctrines rely on the market efficiency principle.

As the Court notes, "[i]t is not in doubt that the efficient capital market hypothesis underpinned" the Court's analysis in accepting the fraud on the market doctrine in Basic v. Levinson.[17]

For the market-based causation approach to work, it must be true that impact of material information is promptly reflected in the prices of the securities. In other words, the doctrine implicitly assumes that the security at issue is trading in an efficient market. The Court correctly notes, "[t]he efficient capital market hypothesis is relevant to market-based causation forensically."[18]

The Myer Decision refers to an article that outlines four possible ways to rebut market-based causation by demonstrating that:[19]

- The security at issue did not trade in an efficient market;
- The alleged misstatement or omission did not affect the market price (if the applicants are claiming losses under an "inflation-based" measure);
- The individual applicant or other group members would have still paid the same price for the security at issue despite knowing the allegedly corrective information; and
- The individual applicant or other group members "actually knew the information that was not disclosed".

Of these, Myer demonstrated the second, i.e., no inflation. One of the reasons that the Court found no loss was because the Court arrived at a different counterfactual scenario than the one pleaded by the applicant. The Judge agreed that Myer's disclosure was incorrect but ruled that the applicants were not using the correct counterfactual disclosure to assess whether any loss was suffered. The Court decided that there was no inflation in the Myer share price because information in the correct counterfactual disclosure was publicly available at the time Myer should have made that counterfactual disclosure, and, therefore, already reflected in the Myer share price.

Assessing loss per share

In the Myer matter, the applicant only offered an inflation-based measure for its loss analysis, and the court accepted that. There are other loss per share measures that the applicant could have offered. The Myer Decision articulates four different methodologies for assessing loss per share.

	MEASURE	ACTUAL SCENARIO	HYPOTHETICAL SCENARIO
1	True value	Price at which shareholder acquired interest	True value of the interest
2	Inflation-based	Price at which shareholder acquired interest	Market price that would have prevailed but for the contraventions
3	Left in hand	Price paid for shares	Whatever is left in hand upon a sale of the shares
4	No transaction	Position the shareholder is in at the date of the trail as a result of acquiring the shares	Position he would have been in if he had not acquired the shares

[13] Myer Decision, ¶1524. From this description, it seems that applicants can offer the market-based causation for all securities of a firm, not just its stock.

[14] Basic Inc v Levinson 485 US 224 (1988)

[15] Myer Decision, ¶1532.

[16] Myer Decision, ¶1500.

[17] Myer Decision, ¶1627.

[18] Myer Decision, ¶1629 (emphasis in original) also noting "So, if it is not a good assumption in a particular case involving a particular class of securities, factually market-based causation and the "inflation-based measure" of loss in that case may fail."

[19] Myer Decision, ¶1668

The Court did not express a preferred method. So that will be one of the issues left for another judgment. But at least now we are dealing with a set of 'known unknowns' rather than 'unknown unknowns'.

In our view, the most significant implication of the decision is the confirmation that, for all potential loss per share measures, the loss per share for a shareholder depends on the 'price paid' when the shareholder acquired his interests.

For an inflation-based measure, experts in Australian shareholder matters can estimate losses per share as the inflation at the time of purchase (i.e., the cash outflow that would not have occurred but for the misconduct) taking into account any offsetting gains if shares are sold at an inflated price. As we discuss later, the inflation would vary with 'price paid' if constant percentage inflation is deemed appropriate.

Beyond the event study - no one size fits all approach for measuring inflation

The Court agreed that share price inflation is measured as the difference between the observed price, and its true value, i.e., the price at which the shares would have traded following the correct counterfactual disclosure.

The Court endorsed an 'event study' approach for assessing inflation. However, in our opinion, an event study of alleged disclosures may not always be an appropriate tool for measuring inflation. For example, if information proposed in counterfactual disclosures is publicly available at the time of those disclosures, there would be no inflation. If the proposed information came out prior to the alleged corrective disclosures, a mechanical event study of those disclosures will be moot.

An event study merely computes the stock return that can be reliably associated with a company's announcement ("abnormal return"). Therefore, even when it is appropriate to use an event study, an assessment of inflation may require additional steps beyond the event study.

The abnormal return is calculated through statistical regression analysis, whose results are influenced by several expert choices (e.g., estimation period, choice of market and industry indices, etc.). These choices depend on the facts and circumstances of a matter and can be an area of dispute between the experts. To compute inflation from the abnormal return, an expert may need to perform additional analyses. For example, one would need to exclude the impact of confounding information, if present, and account for economic differences, if any, between the alleged corrective information and the proposed counterfactual disclosures.

The expert would also need to decide whether the inflation should be measured using a constant percentage, constant dollar, or some other approach. Experts often disagree on the appropriate approach. Many articles have been written about the differences between these approaches, so we will not describe them here in any depth. Suffice it to say for our purposes that they can sometimes produce materially different results.

The important point for future proceedings in Australia is that in the Myer matter, the Court observed that both constant dollar and constant percentage are acceptable approaches and "whether to adopt the constant dollar approach or constant percentage approach to estimate share price inflation depends upon the nature of the announcement that is being assessed."[20]

In our view, the choice of inflation methodology depends on the facts and circumstances of a particular matter and there can be no 'one size fits all' approach.

What is '"Dura" and does it apply in Australia?

One of the other 'unknown unknowns' until now had been whether the so-called 'Dura cap' applies in Australia. In Dura Pharmaceuticals, Inc. v. Broudo, the U.S. Supreme Court found that a mere purchase of a security at an inflated price does not lead to a recoverable loss because "the inflated purchase payment is offset by ownership of a share that at that instant possesses equivalent value"[21] and selling "the shares quickly before the relevant truth begins to leak out, the misrepresentation will not have led to any loss".[22]

The decision makes a distinction between inflation and loss causation, noting that a plaintiff's losses are limited to

[20] Myer Decision, ¶760.

[21] Dura Pharmaceuticals., Inc. v. Broudo, 544 U.S. 336, 342 (2005).

[22] Dura Pharmaceuticals., Inc. v. Broudo, 544 U.S. 336, 342 (2005).

part of inflation removed by the revelation of the allegedly corrective information ("Dura cap"). In other words, under the Dura cap, a shareholder is only deemed to suffer a loss if he or she is holding a share when a share price correction occurred, and not when purchased.

The Dura decision has set the methodology for assessing loss in securities class actions in the U.S., leading to some experts assessing damages based on Dura cap adjustments in Australia.[23]

The Dura cap was not at issue per se in the Myer matter because in the Myer case, group members were defined to be only those that bought Myer shares at an allegedly inflated price and held those shares on the date of the disclosure.[24] However, group members in other Australian shareholder class actions have been defined differently, and therefore this issue is relevant for other cases.

Experts in the US typically interpret the Dura decision as an endorsement of the inapplicability of the constant percentage inflation approach and support for the constant dollar method.[25] In some Australian cases, experts have put forward opinions stating that the constant dollar method has been endorsed by the US courts as the 'correct' method.

In the Myer matter too, some US cases were cited to argue that "the constant percentage approach has been discredited."[26] His Honour has specifically called this out as a "misconception" in relation to Australian cases. His Honour noted that the estimation of damages under the Dura methodology relates to "the assessment of damages under particular US legal requirements, as distinct from the determination of the appropriate estimate of inflation in the price of a security."[27] This discussion suggests that in the views of His Honour, the Dura cap may not necessarily apply to Australian shareholder actions in assessing loss per share.

Absent the Dura cap, experts can calculate damages for a share as inflation in the price at the time of purchase for that share without considering whether the share was held through an alleged corrective disclosure. If shares are sold prior to the inflation being fully removed from the share price, the damages should be reduced by gains, if any, from selling the share at an inflated price because the gains would not have occurred but for the conduct.

Absent the Dura cap, there can be damages for shares bought and sold prior to a corrective disclosure in the case of the constant percentage inflation method. When inflation is a fixed percentage of share price, the dollar amount of inflation will vary as the price changes and therefore, the dollar amount of damages can be very different even for investors buying on the same day but at different prices. In other words, the 'price paid' will play a role in determination of a shareholder's losses.

Consider, for example, a scenario in which inflation is determined to be constant at 10% and there are two shareholders who buy the stock at $10 and $11, respectively, on the same day. The dollar amount of inflation at purchase will be $ 1 and $1.10, respectively. Let us assume that they both sell the shares next day at $9 and thereby get $0.90 as the benefit of inflation at the time of sale. In other words, the shareholders would be entitled to damages of $0.10 (equals $1 less $0.9) and $0.20 (equals $1.10 less $0.90), respectively. Thus, the damage for shareholders also depends on the price paid at the time of purchase for a constant percentage inflation. This issue does not arise for constant dollar method as all shares are assumed to have same dollar amount of the inflation irrespective of the purchase price.

More importantly, shareholders can have loss claims even when they sell their shares prior to a corrective disclosure.

We will have to wait for a decision in another matter to see how this principle is ultimately articulated with respect to the mechanics of calculating losses per share.

Learnings for solicitors

The Myer case is also a good example of the difficulties solicitors face in instructing experts on issues of quantum before the Court has decided the question of liability.

In our experience, one of the most difficult aspects of assessing loss (in any type of litigation) is articulating an appropriate counterfactual scenario and quantifying

[23] Dura Pharmaceuticals., Inc. v. Broudo, 544 U.S. 336 (2005).

[24] Myer Statement of Claim, ¶¶2 & 27 available at http://myerclassaction.com.au/wp-content/uploads/2018/03/VID1494.2016-Statement-of-Claim.pdf accessed 31 October 2020.

[25] Jeff G. Hammel & B. John Casey, "Sizing Securities Fraud Damages: 'Constant Percentage' on Way Out?", New York Law Journal, Jan. 21, 2009.

[26] Myer Decision, ¶769.

[27] Myer Decision, ¶¶768-769.

the related damages. The Myer case makes it clear that instructing solicitors need to take care to ask the right questions from their experts.

With respect to the 'how' to instruct experts, the Myer decision emphasises that the assumptions need to be grounded in commercial reality. The Court went to great lengths to establish, in detail, the typical trading cycles and reporting patterns of the company. Instructing solicitors and their experts should examine whether the inflation analysis for the proposed counterfactual disclosure requires a great deal of assumptions (some of which may depend on other assumptions). The presence of excessive assumptions may be an indication that the counterfactual is 'too hypothetical' and not grounded in reality, and there is a risk that if one set of assumptions doesn't hold, the rest can come down like a house of cards.

As to the 'when' to instruct experts, often the Court's decision on liability is required in order to identify the appropriate counterfactual scenario to quantify. This is sometimes addressed by having experts model multiple scenarios from the beginning, by bifurcating a hearing between questions of liability and quantum, by referring the issue of quantum to a special referee, or by having experts undertake further work on quantification after a decision has been handed down. In the Myer judgment, his Honour has stated a clear preference for having two opposing experts as opposed to one Court-appointed expert or special referee. However, this case also provides a good example of a scenario whereby the Court's decision on the correct counterfactual analysis had a direct impact on the appropriate analysis of quantum by the experts. It is therefore an example of the benefit of post-hearing expert analysis.

Learnings for in-house counsel

Continuous disclosure obligations in complex organisations have always been very challenging. The current need to respond rapidly to volatile market conditions makes it even harder for in-house Counsel to manage this issue.

However, the Myer case underscores the importance of "pressing pause" during rapid decision making to create detailed disclosure chains that will survive a forensic audit.

In reaching its decision, the Court undertook a very detailed and forensic analysis of 'who knew what when'. Weekly and daily financial information was examined, looking at how that information was factored into the company's financial forecasts as well as what, when and how it was presented to the Board.

The Court looked not only at the official minutes of the Board meetings, but also at the communications before and after the meetings. It even considered the recollections of Directors about the context of the discussions.

In-house counsel need to ensure the organisation can balance the competing priorities between supporting the disclosure audit trail and practicing good 'information governance'. On the one hand, the need to retain support for their disclosure audit trails means ensuring that the necessary data is retained. On the other hand, good information governance includes a data retention and disposal policy that retains only what is necessary. To properly protect the organisation, in-house counsel needs to know what data is held, why it is held, and where it is held.

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