Ashurst Australia
September 2014

Class Action Update

The causation conundrum: a corridor of uncertainty

Camping Warehouse Australia Pty Limited v Downer EDI Limited [2014] VSC 357

WHAT YOU NEED TO KNOW

- In *Camping Warehouse Australia Pty Limited v Downer EDI Limited* [2014] VSC 357, the Supreme Court of Victoria refused to strike out a statement of claim for failing to expressly plead reliance upon misleading or deceptive statements which allegedly caused the plaintiff's loss.
- The Court held that given the differences in judicial opinion as to whether proof of reliance is necessary, it could not be said that the case as pleaded was hopeless and bound to fail. Causation requires detailed consideration of context, which was undesirable to embark upon in an application to strike out.

Background

The defendant, Downer EDI Limited, entered into a public-private partnership with the New South Wales State Government to design and deliver the so-called "Waratah" passenger trains and a maintenance facility for the Sydney commuter rail network (the **Waratah train project**).

The defendant, which was listed on the ASX, announced on 1 June 2010 that:

- its previous estimates for the time and costs in delivering the Waratah train project was incorrect;
- its prior estimate that the Waratah train would be 80% based on the Millennium train (which the defendant had previously manufactured) was incorrect;
- it had, and would continue to experience cost overruns; and
- its financial performance and position would be affected by the cost overruns

(together, the **Waratah matters**).

Prior to 1 June 2010, the defendant had made certain announcements declaring that the Waratah train project would be delivered on budget and as scheduled, and that it was expecting net profit after tax growth of 5% for the 2010 financial year. Cost overruns and delays in the delivery of the project occurred, which allegedly impacted on the defendant's financial performance.

The proceeding

The plaintiff brought a class action on behalf of certain shareholders. The plaintiff alleged that the defendant knew of the Waratah matters prior to its announcement on 1 June 2010. The plaintiff alleged that the defendant's failure to disclose those matters to the market upon becoming aware of them constituted a breach of the defendant's continuous disclosure obligations. It further alleged that a reasonable person would have expected the Waratah matters to be disclosed to the market, and the defendant's failure to correct its prior statements constituted conduct that was misleading or deceptive, or was likely to mislead or deceive, in contravention of section 1041H of the Corporations Act.

The plaintiff submitted that the misrepresentations and failures to disclose caused the price of the defendant's shares to be inflated. It alleged that it acquired the shares when they were overpriced, and it had subsequently suffered loss because of their reduced value.

Reliance not necessarily Basic

The defendant sought to strike out the plaintiff's statement of claim on the basis that the plaintiff had failed to plead that it had relied on the alleged misrepresentations. Sifris J held that it was "far from clear" that the plaintiff's statement of claim should be struck out.

The plaintiff submitted that individual shareholders are not required to prove that particular representations were made to them, or that they "relied" upon them. The plaintiffs cited *P Dawson Nominees Pty Ltd v Multiplex Ltd* [2007] FCA 1061 (*Multiplex*) in which Finkelstein J referred to the rebuttable presumption of reliance in "fraud on the market" securities cases in the United States. In *Multiplex*, Finkelstein J noted that a securities market is open and efficient when all material information regarding the company is publicly available. His Honour cited *Basic Inc. v Levison*, 485 US 224 (1988) in which the Supreme Court of the United States held that plaintiffs in a securities class action are entitled to a presumption of reliance on particular misleading statements where the market is "efficient". In "fraud on the market" cases in the United States, the defendant bears the burden of rebutting the presumption of reliance because of a presumed reliance by investors upon the integrity of the market price of securities. The plaintiff submitted that a cause of action based on the breach of a continuous disclosure obligation does not depend on whether the plaintiff relied upon the alleged misrepresentations.

The defendant submitted that reliance was necessary because it constitutes proof of the causal link between the defendant's alleged conduct and the plaintiff's loss.

Sifris J referred to the authorities that considered the provisions of the Corporations Act that allow recovery for loss or damage for certain breaches of the Act. His Honour noted that different language is used in relation to the causal link between the conduct and the loss suffered. His Honour considered at [59] that the provisions differ in the language and statutory meaning, and the matters that "underpin or evidence the causation required are matters of some complexity that require comprehensive and detailed analysis", which would be undesirable to embark upon in a strike out application. His Honour also stated at [46] that the "authorities are not entirely clear and extrapolating principles to cover situations and legislation not entirely analogous is not something that should be done on a strike out application." His Honour concluded that a court should only strike out a claim where it is plainly hopeless and bound to fail, and the plaintiff's claim was clearly not one of them.

Implications

The US "fraud on the market" doctrine has not yet been the subject of any judicial decision in Australia (apart from the observations made by Finkelstein J in *Multiplex*), because Australian courts have not been called upon to decide a shareholder class action despite their prevalence. The Supreme Court of the United States recently affirmed the "fraud on the market" doctrine (and therefore the presumption of reliance) in *Halliburton Co. et al v Erica P. John Fund, Inc*. (see our *Dispute Resolution Update* on the *Halliburton* decision here).

The ongoing uncertainty regarding whether proof of reliance is necessary continues to be exploited by class action plaintiffs, and is a cause of concern in corporate decision making.

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