

Article Information

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Shareholder Class Actions in Australia: Uncertainty for the future of market-based causation

In the third decision delivered in a shareholder class action in Australia,^[1] Iluka Resources Limited (ASX: ILU), (Iluka) succeeded in its defence of a lawsuit^[2] which failed to prove that the shareholders' direct reliance on Iluka's conduct caused their losses. However, the decision in favour of Iluka notably lacked any significant consideration of the second causation argument typically pleaded in shareholder class actions - market-based causation.

Background of the matter

Iluka is a large mining company and global supplier of mineral sand products. On 9 July 2012, Iluka revised its sales guidance for its products, resulting in a 25% drop in share price. The shareholders alleged that Iluka's sales guidance leading up to its announcement:

1. was misleading or deceptive; and
2. breached their continuous disclosure obligations.

The lead applicant purported that reliance on the sales guidance impacted their decision to purchase shares in the company (direct reliance). It is not clear to the authors if the lead applicant or shareholders pleaded that the market as a whole was impacted by the sales guidance (market-based causation).

The Federal Court of Australia (FCA) rejected both claims on the basis that the representations alleged were not actually made, and were merely statements/guidance about Iluka's expectations and were not guarantees or predictions/forecasts of future performance.

The FCA also found that the lead applicant relied on various external stock reports rather than statements made by Iluka, causing the direct reliance case to fail.

Direct reliance and market-based causation

Direct reliance in a shareholder class action requires the claimant to prove they *actually relied* on the contravening conduct (i.e. statements) when deciding to acquire shares in the defendant company, and that the subsequent decrease in share price was directly related to the contravening conduct, resulting in loss to the shareholder.

Market-based causation is based on establishing that the price that the defendant's shares traded on the market was inflated by the contravening conduct, such that the claimant *prima facie* suffered loss by paying an increased price for the shares.

The Court has accepted this proposition,^[3] however, also suggested that it may still be necessary for individual shareholders to give evidence that, *but for* the contravention by an entity, they would not have purchased the shares (or not at the price paid) in order to establish loss.^[4]

Causation and loss in Iluka

Because the Court found that no representations were made (and therefore they were not capable of being relied upon, either directly or by the market), the judgment was relatively quiet in relation to causation. While there is reference to the failed direct reliance case, in so far as it was held that the lead applicant did not rely on the sales guidance issued by Iluka when deciding to purchase the shares, unusually the judgment is completely silent on market-based causation. In previous cases where market-based causation has been alleged by the plaintiff, the *but for* test has been discussed by the FCA in the context of considering misleading or deceptive conduct claims. For example, the alleged contraventions in *Myer* and *Re HIH* were assessed by considering whether the alleged loss would not have occurred *but for* the contraventions.^[5]

The High Court in Australia has offered an alternative approach in cases of proving factual causation of misleading and deceptive conduct generally – the ‘a factor’ test.^[6] The *a factor* test is satisfied if the misleading or deceptive conduct was a *factor* in the occurrence of the plaintiff’s loss, or in other words materially contributed to the plaintiff’s loss.

In Iluka, this test for market-based causation would be satisfied if the alleged contraventions *materially contributed* to the shareholders’ loss, rather than the more stringent test of whether the contraventions were *necessary* for the loss.

The *a factor* test, if adopted, arguably offers a more appropriate test for market-based causation in cases of misleading or deceptive conduct. Firstly, it is more reliable and intuitive.^[7] For example, the *but for* test requires counterfactual speculation as to how a market would have responded *but for* a particular event. This can be a difficult exercise for a plaintiff to speculate and quantify the loss. The *a factor* test shifts the requirements from necessity to contribution and is not as easily defeated by a claim that it was not the only factor relevant to the plaintiff’s loss.

Secondly, the test also avoids duplicative causation, as market-based causation often involves multiple factors that could have affected share prices.^[8] The court does not need to assess each separate factor and consider its relative relevance to the causal loss overall, as is required when assessing the causal conduct following the *but for* test.

Finally, the *a factor* test promotes the deterrence of all misleading or deceptive conduct by providing a broad opportunity for the conduct to be considered misleading or deceptive, regardless of whether it was necessary for the loss.^[9]

Conclusion

By failing to address market-based causation, the Iluka decision has created uncertainty around what causal test the court would be willing to accept for shareholders to succeed with a market-based causation claim. It is only a matter of time before there is a substantial decision on this point, however, until this occurs, the law on market-based causation remains unsettled.

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[1] Following *Crowley v Worley Limited* [2020] FCA 1522 and *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Ltd* [2019] FCA 1747.

[2] *Bonham v Iluka Resources Ltd* [2022] FCA 71.

[3] *In the matter of HIH Insurance Limited (In Liquidation)* [2016] NSWSC 482; *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Ltd* [2019] FCA 1747.

[4] *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Ltd* [2019] FCA 1747, [1671].

[5] *In the matter of HIH Insurance Limited (In Liquidation)* [2016] NSWSC 482; *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Ltd* [2019] FCA 1747.

[6] *Henville v Walker* [2001] HCA 52, [61] and [106].

[7] Henry Cooney, *Factual causation in cases of market-based causation* (2021) 27 *Torts Law Journal* 51.

[8] *Ibid.*

[9] *Ibid.*