WHEN DOES 'FRAUD ON THE MARKET' INDUCE A RIGHT TO DAMAGES?

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Sections 1041E and 1041H of the Corporations Act 2001 *(Cth) give investors a right to trade in a market that is free of false statements. Section 1041I of the* Corporations Act 2001 *(Cth) gives investors compensation for loss or damage caused 'by' conduct that breaches ss 1041E to 1041H. However, the courts' current approach to determining when loss is caused 'by' breaches of ss 1041E or 1041H is unclear and does not quadrate with the nature of false statements. This paper examines the interpretation of 'by' to determine the appropriate causal nexus between breach of ss 1041E and 1041H, and compensation under s 1041I.*

I INTRODUCTION

Corporate managers and traders have an incentive to make false or misleading statements that alter share prices. Corporate managers may make false statements to increase profits or to make financial positions appear artificially high.[1] Traders may make false statements that alter share prices in order to induce trading opportunities.[2] However, the courts have not defined precisely how and when shareholders can obtain compensation for damage suffered due to these false statements. This article analyses shareholders' access to compensation and proposes an appropriate causal nexus between breach of false information provisions in the *Corporations Act 2001* (Cth) and compensation. Section 1041I of the *Corporations Act 2001* (Cth) provides compensation for false or misleading statements.[3] Sections 1041E and 1041H impose an obligation not to make false or misleading statements. Section 1041F imposes similar obligations, but in the limited, and not presently relevant, context of 'inducing persons to deal' in financial products. Section 1041I imposes liability for loss or damage caused 'by' the misstatement.

The primary right is a right to trade in a market without breach of ss 1041E and 1041H.[4] The secondary right is a right to a remedy if another person breaches

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1 See, eg, *James Hardie Industries NV v ASIC* [2009] NSWCA 18 (Unreported, Giles, McColl and Macfarlan JJA, 18 February 2009).

2 See, eg, Australian Securities and Investments Commission ('ASIC'), *AD09-48 ASIC Bans Broker for Spreading Misleading Information* (2009) ASIC <http://www.asic.gov.au/asic/asic.nsf/byheadline/AD09-48+ASIC+bans+broker+for+spreading+misleading+information?openDocument> at 23 December 2009.

3 Section 1041G of the *Corporations Act 2001* (Cth) is beyond the scope of this discussion.

4 James Edelman and Steven Elliott, 'Money Remedies against Trustees' (2004) 18 *Trust Law International* 116, 116-17; Steven Elliott, 'Remoteness Criteria in Equity' (2002) 65 *Modern Law Review* 588, 590; Steven Elliott and Charles Mitchell, 'Remedies for Dishonest Assistance' (2004) 67 *Modern Law Review* 16, 24-5; Charles Rickett, 'Equitable Compensation: Towards a Blueprint?' (2003) 25 *Sydney Law Review* 31.

ss 1041E or 1041H. A court order for compensation replicates this secondary right.[5] The word 'by' in s 1041I connects the primary right with the secondary right. This article considers the connection between the primary right and the secondary right. At general law, this connection comprises four key concepts denoted 'connecting principles': causation, remoteness, contributing fault, and mitigation. All four principles address the question: 'Is the breach connected to the loss?' This is a separate inquiry from the extent of the loss.[6] Further, while some *obiter dicta* on other statutes indicates that the connection only contains causation,[7] there is no unified analysis of ss 1041E, 1041H and 1041I. Thus, further analysis of all the connecting principles is necessary.

The word 'by' is capable of a range of meanings depending upon the breach and the nature of the underlying duty. Thus, the word 'by' is vague.[8] Statutory interpretation resolves this vagueness by adopting the purposive approach.[9] According to this approach, an interpretation is valid only if it is consistent with the legislature's objectively evinced intentions[10] as indicated through the text, purpose, and context of the legislation.[11] Statutory interpretation determines the meaning of the connecting principles. However, the courts' current approach to the connecting principles does not quadrate with either the intentions of the legislature or the nature of market manipulation. This article posits an alternative that is consistent with investors' right to trade in a market free of manipulation. The article proceeds as follows. Part II discusses how misstatements influence stock prices and values. Part III outlines the purpose of compensation. Parts IV to VII analyse causation, remoteness, contributing fault, and mitigation respectively.

II HOW DO MISSTATEMENTS WORK?

An interpretation of ss 1041E and 1041I must begin with the ordinary meaning of the provisions.[12] Thus, analysis of s 1041E must begin with an understanding of how false statements work. Shares have two important values: the share price (p)

5 Rafal Zakrzewski, *Remedies Reclassified* (2005) 17-18; Peter Birks, 'Rights, Wrongs and Remedies' (2000) 20 *Oxford Journal of Legal Studies* 1, 15-16.

6 See especially Michael Tilbury, Michael Noone and Bruce Kercher, *Remedies* (4th ed, 2004). See also Zakrzewski, above n 5.

7 See *Trade Practices Act 1974* (Cth) ss 52, 82; *Johnston v McGrath* (2005) 195 FLR 101, 108 [37] (Gzell J) citing *Munchies Management Pty Ltd v Belperio* (1988) 58 FCR 274, 286-7.

8 Randal Graham, 'A Unified Theory of Statutory Interpretation' (2002) 23 *Statute Law Review* 91, 118.

9 Philip Frickey, 'Structuring Purposive Statutory Interpretation: An American Perspective' (2006) 80 *Australian Law Journal* 849, 856-7 analysing *Acts Interpretation Act 1901* (Cth) ss 15AA, 15AB. See also *Cooper Brookes (Wollongong) Pty Ltd v Commissioner of Taxation* (1981) 147 CLR 297.

10 *Inland Revenue Commissioners v Ayrshire Employers Mutual Insurance Association Ltd* [1946] 1 All ER 637, 641; *Cooper Brookes (Wollongong) Pty Ltd v Commissioner of Taxation* (1981) 147 CLR 297; *Kingston v Keprose Pty Ltd* (1987) 11 NSWLR 404.

11 Michael Zander, *The Lawmaking Process* (1980) 57; *R (Daly) v Secretary of State for the Home Department* [2001] 2 AC 532, 548 (Steyn LJ); *Theophanous v Herald & Weekly Times Ltd* (1994) 182 CLR 104, 196; William Eskridge and Philip Frickey, 'Statutory Interpretation as Practical Reasoning' (1990) 42 *Stanford Law Review* 321, 341-2.

12 See, eg, *McKinnon v Secretary, Department of Treasury* (2006) 228 CLR 423, 441 [48] (Hayne J, considering the definition of 'reasonable grounds'); *Kingston v Keprose Pty Ltd* (1987) 11 NSWLR 404, 423 (McHugh JA); *Bropho v Western Australia* (1990) 171 CLR 1, 20.

and the intrinsic value (v). The price is the amount that investors pay for the stock. The intrinsic value is the amount that the stock is worth. Ordinarily, if the market is somewhat efficient, the price should equal the intrinsic value on average. Shares hold these values at two important times: (a) the misstatement-date (*time 1*), and (b) the reveal-date (*time 2*). Denote the price and value at *time 1* as p_1 and v_1, and the price and value at *time 2* as p_2 and v_2. Figure 1 depicts this situation.

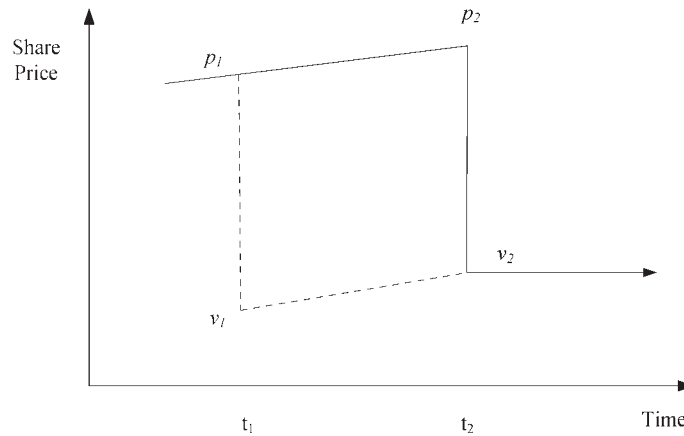

Figure 1

False statements affect the share price as follows. If the market is efficient, the share price equals the intrinsic value on average.[13] However, if a misstatement either disguises bad news, or conveys false good news, then the price will exceed the intrinsic value. Three implications for litigation are notable. First, the plaintiff sustains a loss only if he or she purchases after the misstatement-date. This is because the plaintiff can sustain a loss from the misstatement only if it causes him or her to pay too much. If the plaintiff purchased before the misstatement, then the misstatement could not have caused him or her to pay too much since the misstatement did not exist yet at the time of purchase. Second, the loss arises on the purchase-date (assuming it is after the misstatement-date). On the misstatement-date, the price exceeds the intrinsic value ($p_1 > v_1$) and the plaintiff sustains a loss equal to $p_1 - v_1$. This loss is unrealised. It is the difference between the share price and the intrinsic value.[14] On the reveal-date, the market has all information, and the price at *time 2* equals the intrinsic value at *time 2* ($p_2 = v_2$). Thus, while the plaintiff sustains a loss on the purchase-date, he or she only realises it on

13 Charles Lee, James Myers and Bhaskaran Swaminathan, 'What Is the Intrinsic Value of the Dow?' (1999) 54 *Journal of Finance* 1693.

14 See Bradford Cornell and R Gregory Morgan, 'Using Finance Theory to Measure Damages in Fraud on the Market Cases' (1990) 37 *UCLA Law Review* 883; David Tabak, 'Risk Disclosures and Damages Measurement in Securities Fraud Cases' (2006) 21 *Securities Reform Act Litigation Reporter* 6.

the reveal-date.[15] Third, the defendant cannot be responsible for general market movements. Due to general market movements, the price and the intrinsic value can change over time. Thus, the intrinsic value at the reveal-date (v_2) may not equal the intrinsic value at the misstatement-date (v_1). However, if the loss arises at *time 1*, then the defendant is not responsible for the change between v_1 and v_2. Instead, the defendant is only responsible for the difference between the price at the time of the misstatement (p_1) and the value at the time of the misstatement (v_1).

III WHAT IS THE PURPOSE OF COMPENSATION?

If legislation uses vague or unclear language, then the courts often adopt purposive statutory interpretation.[16] The overriding purpose of ss 1041E and 1041H is to ensure that investors have confidence in the integrity of financial markets.[17] The sections accomplish this in three ways. First, s 1041I places the plaintiff into the position that he or she would occupy if the defendant did not make the misstatement. This quadrates with the purpose of awarding compensation for common law and equitable wrongs.[18] Awarding compensation promotes confidence in financial markets by allowing investors to reverse any undue losses. Second, ss 1041E and 1041H aim to protect people from wrongful conduct.[19] In the context of ss 1041E and 1041H, wrongful conduct is conduct that prevents market prices reflecting genuine supply and demand.[20] This occurs by holding wrongdoers liable for the plaintiff's losses and by allowing plaintiffs to avoid unfair losses. This protection ensures confidence in financial markets. Third, ss 1041E and 1041H appear to promote compliance with the law, in a similar way to fiduciary duties. To see this, consider the purposes behind ss 1041E, 1041H, and fiduciary duties. The unifying policy behind fiduciary duties is strict loyalty.[21]

15 See especially *Sons of Gwalia Ltd v Margaretic* (2007) 231 CLR 160; Sharon Christensen and Stephen Lumb, 'Ascertaining When Loss Is First Suffered by Misleading Conduct: Relevance of Contingencies, Future Predictions and Concealment' (2005) 13 *Trade Practices Law Journal* 149, 151.

16 See, eg, *Air-India v Wiggins* [1980] 1 WLR 815, 820-2 (Lord Scarman); *Astor v Perry* [1935] AC 398, 416; *Capcount Trading v Evans (Inspector of Taxes)* [1993] 2 All ER 125; *The Halcyon the Great* [1975] 1 WLR 515, 520; *Bank Officials' Association (SA) v Savings Bank of South Australia* (1923) 32 CLR 276 (Starke J).

17 Paul Latimer, 'Securities Regulation Laws: What Are They Trying to Achieve?' in Gordon Walker and Brent Fisse (eds), *Securities Regulation in Australia and New Zealand* (1994) 167; *R v Lloyd* (1996) 19 ACSR 528 (Ipp, Malcolm and Murray JJ); Merritt Fox, 'After Dura: Causation in Fraud-on-the-Market Actions' (2006) 31 *Journal of Corporation Law* 829, 833; Vivien Goldwasser, 'Regulating Manipulation in Securities Markets: Historical Perspectives and Policy Rationales' (1999) 5 *Australian Journal of Legal History* 149.

18 *Wilson v Wilson's Tile Works Pty Ltd* (1960) 104 CLR 328; *Bird v Commonwealth* (1988) 165 CLR 1; *J Odlin Shopfitting International Pty Ltd v Kaljanac* (1993) 29 NSWLR 632.

19 See eg, *Day and Dent Constructions Pty Ltd (in liq) v North Australian Properties Pty Ltd* (1982) 150 CLR 85; *Magic Australia Pty Ltd v Caltex Oil (Australia) Pty Ltd* (1988) 19 FCR 389; *Devenish v Jewel Food Stores Pty Ltd* (1991) 172 CLR 32; *McAusland v Deputy Commissioner of Taxation* (1993) 47 FCR 369.

20 *R v Lloyd* (1996) 19 ACSR 528; *Basic, Inc v Levinson*, 485 US 224 (1988).

21 *Bristol and West Building Society v Mothew* [1998] Ch 1, 18; *Pilmer v Duke Group Ltd (in liq)* (2001) 207 CLR 165; Andrew Lynch, 'Equitable Compensation for Breach of Fiduciary Duty: Causation and Contribution – The High Court Dodges a Fusion Fallacy in *Pilmer*' (2001) 21 *Australian Bar Review* 173, 187.

Fiduciary duties variously promote this by enforcing relationships of trust and confidence,[22] standards of honesty and propriety,[23] and reasonable expectation that the fiduciary will act in the beneficiary's interests.[24] Consider the conduct underlying ss 1041E and 1041H. These sections pertain to a situation where a person has information that can influence share prices. Potential shareholders *trust* that that person will not *dishonestly* hide that information from them. That is, potential shareholders have a reasonable expectation that the person will not artificially inflate the share price by hiding value-relevant information. Thus, ss 1041E and 1041H appear to address a similar situation to fiduciary duties.

Prohibition of false statements has three purposes: compensation, protection and compliance. These purposes influence the interpretation of the *Corporations Act 2001* (Cth). Thus, the issue is the appropriate approach to causation, remoteness, contributing fault and mitigation.

IV CAUSATION

The defendant is liable under s 1041I only if the breach of s 1041E or s 1041H causes the plaintiff's loss. Causation establishes whether the defendant's action produced the loss. The nature of false statements determines the appropriate causal nexus between breach and loss.[25] It has been established in Part II above that the defendant can be liable only if the plaintiff purchases after the misstatement. However, this misstatement causes the loss only if it causes the shareholder/plaintiff to pay too much. That is, because of the statement, the plaintiff pays p_1 when he or she should pay v_1.[26] This situation induces three issues: first, how do the courts currently approach causation; second, what alternative approaches to causation are available; and third, what is the appropriate approach to causation?

22 *Farrington v Rowe McBride and Partners* [1985] 1 NZLR 83, 94 (McMullin J); *Hospital Products Ltd v United States Surgical Co* (1984) 156 CLR 41, 96; *United Dominions Co Ltd v Brian Pty Ltd* (1985) 157 CLR 1, 11-12 (Mason, Brennan and Deane JJ).

23 *Hospital Products Ltd v United States Surgical Co* (1984) 156 CLR 41, 96-7; *Pavan v Ratnam* (1996) 23 ACSR 214, 224 (Beazley JA).

24 *Commonwealth Bank of Australia v Smith* (1991) 102 ALR 453, 476 (Davies, Sheppard and Gummow JJ).

25 *ASIC v Adler* (2002) 168 FLR 253, 417 [749]-[750] (Santow J); *Fico v O'Leary* [2004] WASC 215 (Unreported, Heenan J, 11 October 2004) 168-72; *Canson Enterprises Ltd v Boughton & Co* (1991) 85 CLR 129, 155 (McLachlin J); *O'Halloran v R T Thomas & Family Pty Ltd* (1998) 45 NSWLR 262, 272-3, 277; *Beach Petroleum NL v Kennedy* (1999) 48 NSWLR 1, 90 [430] (Spigelman CJ, Sheller and French JJ); Joachim Dietrich and Thomas Middleton, 'Statutory Remedies and Equitable Remedies' (2006) 28 *Australian Bar Review* 136, 158-9; Lusina Ho, 'Attributing Losses to a Breach of Fiduciary Duty' (1998) 12 *Trust Law International* 66, 69-70.

26 See *Trade Practices Act 1974* (Cth) ss 52, 82; *Johnston v McGrath* (2005) 195 FLR 101, 108 (Gzell J). For academic opinion in the United States see Merritt Fox, 'Demystifying Causation in Fraud-on-the-Market Actions' (2005) 60 *Business Lawyer* 507; Fox, 'After Dura: Causation in Fraud-on-the-Market Actions', above n 17.

A *What Is the Current Approach?*

The current approach appears to follow the *Trade Practices Act 1974* (Cth) ('*TPA*') s 82. The courts have not definitively interpreted ss 1041E and 1041H. However, three key principles are identifiable. First, the *TPA* s 82 jurisprudence is relevant to the interpretation of ss 1041E and 1041H. Second, in this context, this means that the plaintiff must prove that the misstatement has affected the share price. The current approach states that principles of common sense dictate if the misstatement influenced the price. Third, the plaintiff need not prove that he or she relied on the misstatement.

The first key principle is that *TPA* s 82 jurisprudence guides the interpretation of ss 1041E and 1041H. Mansfield J in *Gughlielman v Trescowthick*[27] tacitly recognised this by basing his Honour's interpretation of the analogous s 12GF of the *Australian Securities and Investments Commission Act 2001* (Cth) ('*ASICA*') on *TPA* s 82 jurisprudence.[28] In *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd*[29] Giles J explicitly recognised this by endorsing *TPA* s 82 jurisprudence vis-à-vis the predecessors of ss 1041E and 1041I in the *Corporations Act 1989* (Cth) ss 995 and 1005.[30]

Second, in *Johnston v McGrath*[31] Gzell J held that a misstatement caused loss only if it altered the stock price.[32] The case involved misleadingly positive statements in press releases from HIH Insurance Limited ('HIH'). The plaintiff sued for contravention of s 52 of the *TPA*. The plaintiff argued that these statements had inflated the stock price and thus he sustained loss when the market realised HIH's true financial position. The Court held that the statements did not inflate the stock price and thus that causation did not obtain. By similar reasoning, causation can obtain vis-à-vis ss 1041E, 1041H, and 1041I only if the misstatement affects the stock price.

Common sense principles determine whether the misstatement has influenced the price. Mansfield J in *Gughlielman*[33] adopted a 'commonsense' test to similar provisions in s 12GF of the *ASICA*.[34] Mansfield J based this on *TPA* s 82 jurisprudence. Similarly, the Court in *ASIC v Vines*[35] and *ASIC v Loiterton*[36] affirmed that the analogous phrase 'as a result of' adopts its ordinary meaning.[37]

27 [2004] ATPR 41-995 ('*Gughlielman*').
28 Ibid [128].
29 (2008) 252 ALR 659 ('*Ingot*').
30 Ibid 665-70 [2]-[22].
31 (2005) 195 FLR 101.
32 Ibid 108.
33 [2004] ATPR 41-995.
34 Ibid [128].
35 (2006) 58 ACSR 298.
36 (2004) 50 ACSR 693 ('*Loiterton*').
37 Ibid 727 [85] (Bergin J).

The ordinary meaning is that causation 'is a matter of fact'.[38] Further, the New South Wales Court of Appeal held that the analogous provision in s 1317H of the *Corporations Act 2001* (Cth) should be given its 'ordinary meaning',[39] and this also means that causation is a 'matter of fact'.[40]

Third, the plaintiff need not prove that he or she directly relied on the false statement. *Ingot* indicates that the plaintiff can prove causation even if he or she did not rely on or know about the misstatement. *Ingot* concerned misstatements in a prospectus and marketing offer. The relevant issue was whether plaintiffs could recover compensation even if they could not prove that they relied on the prospectus in making their investments. The Court held that if the defendant intended the plaintiff to act in the way that he or she did, then the plaintiff need not prove direct reliance on the false statement.[41] Relevantly, if the defendant's false statement inflated the price, and the Court finds that the defendant intended the plaintiff to purchase shares, then the plaintiff need not prove reliance on the statement.

These three principles are persuasive but not determinative. Section 1041I of the *Corporations Act 2001* (Cth) should follow s 82 of the *TPA* only if the legislature objectively intended it.[42] Thus, if the policy underlying s 82 differs from the policy underlying the combination of ss 1041E and 1041I, different causal principles may apply. Section 82's policy is consumer protection. The policy underlying market misconduct provisions is protection of the integrity of the market. Therefore, the policies appear to differ. Thus, proper examination of causation is necessary.

Further, the Court in *Ingot* considered conduct of a different nature in a now superseded law. The Explanatory Memorandum for the *Corporations Act 1989* (Cth) evinces a clear intention that s 1005 should adopt *TPA* s 82 jurisprudence.[43] However, the Corporations Bill 2001 (Cth) does not mention ss 1041E, 1041H or 1041I, and there is no further explanation of the causal requirements for the superseded s 1005.[44] While not definitive, this different treatment may indicate that the legislature intended courts to interpret the new provisions differently from the old provisions. This motivates examination of the interpretation of ss 1041E, 1041H and 1041I.

38 *ASIC v Vines* (2006) 58 ACSR 298, 363 [246] (Austin J).

39 Ibid [245]-[246] (Austin J); *Adler v ASIC* (2003) 46 ACSR 504, 652-3 [708]-[709].

40 *Adler v ASIC* (2003) 46 ACSR 504, 653 [709].

41 *Ingot* (2008) 252 ALR 659, 669 [19] (Giles JA).

42 See *Ogden Industries Pty Ltd v Lucas* [1970] AC 113, 131 (Lord Upjohn for Lord Reid, Lord Hodson, Lord Upjohn, Lord Donovan and Lord Pearson); *Melbourne Co v Barry* (1922) 31 CLR 174, 183 et seq (Isaacs J); *Brennan v Comcare* (1994) 50 FCR 555, 572 (Gummow J); *McNamara v Consumer Trader and Tenancy Tribunal* (2005) 221 CLR 646, 661 (McHugh, Gummow and Heydon JJ).

43 Explanatory Memorandum, Corporations Bill 1989 (Cth) 733-4, <http://www.takeovers.gov.au/content/Resources/acts_bills_ems/downloads/Corporations_Bill_ExMem_1988_3c.pdf> at 21 December 2009.

44 Corporations Bill 2001 (Cth) Vol 3 <http://www.comlaw.gov.au/ComLaw/legislation/bills1.nsf/0/7BB29402F5D4F389CA257013000CC018/$file/CorpBill2001Vol3.pdf> at 21 December 2009.

B *What Are the Options?*

It is necessary to analyse which approach to causation quadrates with fundamental compensatory principles and the policy underlying ss 1041E, 1041H and 1041I. Analytically, causation can apply to both the purchase and the price-change (if any). This induces two key issues. First, when does the misstatement 'cause' the purchase? And, especially, must the plaintiff prove that he or she relied on the misstatement or will the courts presume that he or she did so? Second, when does the misstatement 'cause' the loss?

Compensation for breach of common law and equitable duties suggests three possible approaches to causation with regard to the purchase and the loss. However, different causal requirements may apply to (a) the purchase of securities, and (b) the loss resulting from the misstatement.

The first option is presumed causation. Under presumed causation, the court presumes that X caused Y. Here, the court would simply presume that because the defendant made a misstatement, the plaintiff purchased the stock and/or overpaid. Thus, the court automatically assumes that the misstatement caused p_1 to exceed v_1. This is similar to the approach to equitable compensation for breach of fiduciary duty in *Brickenden v London Loan & Savings Co.*[45]

The second option is bare 'but for' causation. This approach holds that X caused Y if Y would not have occurred 'but for' X. Here, the plaintiff would have to prove that (a) he or she would not have purchased but for the misstatement, or (b) the share price would have been lower but for the misstatement. This typically requires that the plaintiff prove[46] that the breach (ie, the misstatement) was 'a cause' of the loss.[47] This resembles common law causation for deceit.[48]

The third option is qualitative causation which resembles the approach at common law to negligence.[49] At its least rigorous, this approach holds that common sense determines whether X causes Y.[50] At its most rigorous, this approach requires that the plaintiff prove that (a) the misstatement was 'a cause' of the purchase (or price-inflation), and (b) the purchase (or price-inflation) was not primarily due to a supervening event. Unlike 'but for' causation, qualitative causation requires that the misstatement be more than a necessary condition for the loss;[51] it must be

45 [1934] 3 DLR 465.

46 *A S James Pty Ltd v Duncan* [1970] VR 705, 724; *Duyvelshaff v Cathcart & Ritchie Ltd* (1973) 1 ALR 125; *Imperial Chemical Industries of Australia and New Zealand Ltd v Murphy* (1973) 47 ALJR 122.

47 *Duyvelshaff v Cathcart & Ritchie Ltd* (1973) 1 ALR 125; *Alexander v Cambridge Credit Co Ltd* (1987) 9 NSWLR 310, 350 (McHugh JA); *Bicknell v Australian Telecommunications Commission* (1993) 10 WAR 373; *Rosenberg v Percival* (2001) 205 CLR 434.

48 *Field v Shoalhaven Transport Pty Ltd* [1970] 3 NSWR 96; *Edgington v Fitzmaurice* (1885) 29 Ch D 459; *Gould v Vaggelas* (1985) 157 CLR 215, 238-9 (Wilson J); *Demetrios v Gikas Dry Cleaning Industries Pty Ltd* (1991) 22 NSWLR 561.

49 Michael O'Meara, 'Causation, Remoteness and Equitable Compensation' (2005) 26 *Australian Bar Review* 51, 53.

50 See *National Insurance Co of New Zealand Ltd v Espagne* (1961) 105 CLR 569, 591 (Windeyer J).

51 Ibid; *March v E & M H Stramare Pty Ltd* (1991) 171 CLR 506, 509 (Mason CJ).

both necessary and sufficient to cause the loss. If there are multiple 'sufficient' causes, then the facts of the case,[52] 'commonsense',[53] and the policy underlying the duty[54] determine whether the defendant has 'caused' the loss.

C *What Is the Appropriate Approach Vis-à-vis the Purchase?*

Purchase-causation should adopt the presumed causation approach: courts presume the misstatement caused the plaintiff to purchase the stock. While this approach lacks explicit Australian authority,[55] it has significant support in the United States.[56] Further, it quadrates with the conclusion in *Ingot* that the plaintiff need not show he or she directly relied on the misstatement. This article contends that presumed causation is appropriate since it agrees with the purpose of ss 1041E and 1041I.

'But for' causation and qualitative causation are inconsistent with compensatory purpose of s 1041I. Logically, a misstatement causes a transaction only if the plaintiff knows of the misstatement and relies on it.[57] In efficient stock markets, misstatements inflate the stock price even if the particular plaintiff was unaware

52 See, eg, *Livingstone v Halvorsen* (1978) 53 ALJR 50 (a torts case: causation of damage and liability of drivers of vehicles); *TNT Management Pty Ltd v Brooks* (1979) 53 ALJR 267 (a torts case: sufficiency of proof of negligence in the context of the road accident); *West v Government Insurance Office (NSW)* (1981) 148 CLR 62 (a torts case: inferences drawn from proved facts in an action for negligence arising out of a collision between motor vehicles); *Nominal Defendant v Puglisi* (1984) 58 ALJR 474 (a torts case: circumstantial evidence of negligent driving).

53 *Kocis v SE Dickens Pty Ltd* [1998] 3 VR 408 (a torts case: duty of care of a supermarket to conduct inspection of floors; each case will turn on its own facts); *State Electricity Commission (Vic) v Gay* [1951] VLR 104, 106 (a torts case) ('*Gay's Case*'); *Fitzgerald v Penn* (1954) 91 CLR 268, 277 (Dixon CJ, Fullagar and Kitto JJ); *Curmi v McLennan* [1994] 1 VR 513, 525-6 (Gobbo J); *Medlin v State Government Insurance Commission* (1995) 182 CLR 1, 6 (Deane, Dawson, Toohey and Gaudron JJ): 'For the purposes of the law of negligence, the question whether the requisite causal connexion exists between a particular breach of duty and particular loss or damage is essentially one of fact to be resolved, on the probabilities, as a matter of commonsense and experience'.

54 See references to policy in *March v E & M H Stramare Pty Ltd* (1991) 171 CLR 506.

55 Michael Duffy, 'Fraud on the Market: Judicial Approaches to Causation and Loss from Securities Nondisclosure in the United States, Canada and Australia' (2005) 29 *Melbourne University Law Review* 621; Alexander Loke, 'The Investors' Protected Interest against Market Manipulation in the United Kingdom, Australia and Singapore' (2007) 21 *Australian Journal of Corporate Law* 22. See tentative *obiter* support in: *Johnston v McGrath* [2007] NSWCA 231 (Unreported, Giles JA, Young CJ in Eq and Handley AJA, 4 September 2007); *P Dawson Nominees Pty Ltd v Multiplex Ltd* (2007) 242 ALR 111; *Cultus Petroleum NL v OMV Australia Pty Ltd* (1999) 32 ACSR 1; *Dorajay Pty Ltd v Aristocrat Leisure Ltd* (2005) 147 FCR 394; *Stanilite Pacific Ltd (in liq) v Seaton* (2005) 55 ACSR 460.

56 *Green v Occidental Petroleum Corp*, 541 F 2d 1335 (9th Cir, 1976); *Harris v Union Electric Co*, 787 F 2d 355 (8th Cir, 1986); *Peil v Speiser*, 806 F 2d 1154 (3rd Cir, 1986); *Flamm v Eberstadt*, 814 F 2d 1169 (7th Cir, 1987); *Basic Inc v Levinson*, 485 US 224 (1988); *Re Convergent Technologies Securities Litigation*, 721 F Supp 1131 (ND Cal, 1988); *Re Apple Computer Securities Litigation*, 886 F 2d 1109 (9th Cir, 1989); *Robbins v Koger Properties Inc*, 116 F 3d 1441 (11th Cir, 1997); *Dura Pharmaceuticals Inc v Broudo*, 544 US 336 (2005); *Re Dura Pharmaceuticals Inc Securities Litigation*, 548 F Supp 2d 1126 (SD Cal, 2006); Fox, 'After Dura: Causation in Fraud-on-the-Market Actions', above n 17.

57 See, eg, *Gipps v Gipps* [1978] 1 NSWLR 454; *Holmes v Jones* (1907) 4 CLR 1692; *Gould v Vaggelas* (1985) 157 CLR 215; Fox, 'After Dura: Causation in Fraud-on-the-Market Actions', above n 17.

of them.[58] Therefore, persons can sustain loss even if they are unaware of the misstatement. If they are unaware of it, they cannot prove they relied upon it. Therefore, 'but for' causation and qualitative causation would deny compensation to those persons.

Qualitative causation leads to an anomaly. Many investors would buy stock even if they knew that the statement was false;[59] however, they would simply pay less for it. If they would buy it anyway, they cannot prove qualitative causation even if they sustained a loss.[60] Therefore, qualitative causation precludes compensation even if the misstatement inflated the price. This is anomalous and undermines the compensatory purpose behind ss 1041H and 1041E.

Presumed causation appears to best support proscriptive purposes of ss 1041H and 1041E. Consider the use of presumed causation in cases of breach of fiduciary duty. In the context of proscriptive fiduciary duties, courts have held that a stricter causation test promotes a policy of strict loyalty.[61] Thus, a stricter test for breach of s 1041E will promote its proscriptive purpose. Presumed causation is stricter than 'but for' causation or qualitative causation since it does not require the plaintiff to prove reliance. Therefore, it is likely that presumed causation supports s 1041E's proscriptive purpose.

Legislators are unlikely to intend the courts to adopt an interpretation that is either unclear[62] or impracticable.[63] While 'but for' causation, qualitative causation and presumed causation all have clear meanings, proving each plaintiff's actual subjective awareness is impracticable.[64] As 'but for' causation and qualitative causation, but not presumed causation, require this, these two approaches are impracticable. Thus, this article contends that the legislature intended to adopt presumed causation vis-à-vis purchase-causation. This approach is clear, practicable, and quadrates with the nature of market manipulation.

D *What Is the Appropriate Approach Vis-à-vis the Price Change?*

Qualitative causation is the most appropriate approach vis-à-vis the price change. This is because it best coheres with general compensatory principles

58 *Basic Inc v Levinson*, 485 US 224 (1988); Cornell and Morgan, above n 14; Baruch Lev and Meiring de Villiers, 'Stock Price Crashes and 10b-5 Damages: A Legal, Economic and Policy Analysis' (1994) 47 *Stanford Law Review* 7; Douglas Smith, 'Fraud on the Market: Short Sellers' Reliance on Market Price Integrity' (2005) 47 *William and Mary Law Review* 1003; Zachary Starr, 'Fraud on the Market and the Substantive Theory of Class Action' (1991) 65 *St John's Law Review* 441; Lynn Stout, 'The Mechanism of Market Inefficiency: An Introduction to New Finance' (2003) 28 *Journal of Corporate Law* 636.

59 *Semerenko v Cendant Corp*, 223 F 3d 165 (3rd Cir, 2000); Fox, 'Demystifying Causation in Fraud-on-the-Market Actions', above n 26; Fox, 'After Dura: Causation in Fraud-on-the-Market Actions', above n 17.

60 *Holmes v Jones* (1907) 4 CLR 1692; *Semerenko v Cendant Corp*, 223 F 3d 165 (3rd Cir, 2000).

61 *Maguire v Makaronis* (1997) 188 CLR 449; O'Meara, above n 49; Rickett, above n 4. See also *Pilmer v Duke Group Ltd (in liq)* (2001) 207 CLR 165.

62 *Blue Metal Industries Ltd v Dilley* (1969) 117 CLR 651; *Cooper Brookes (Wollongong) Pty Ltd v Federal Commissioner of Taxation* (1981) 147 CLR 297; *Al-Kateb v Godwin* (2004) 219 CLR 562, 577 (regarding the fundamental principles of interpretation); *R v Lavender* (2005) 222 CLR 67.

63 *R v Camphill Deputy Governor* [1985] QB 735; *Sheffield Council v Yorkshire Water Ltd* [1991] 1 WLR 58; *Blue Metal Industries Ltd v Dilley* (1969) 117 CLR 651; *Mills v Meeking* (1990) 169 CLR 214; *Collector of Customs v Agfa-Gevaert Ltd* (1996) 186 CLR 389; *R v Lavender* (2005) 222 CLR 67.

64 *Everist v McEvedy* [1996] 3 NZLR 348; Fox, 'Demystifying Causation in Fraud-on-the-Market Actions', above n 26; Fox, 'After Dura: Causation in Fraud-on-the-Market Actions', above n 17.

and the policy principles underlying ss 1041E, 1041H and 1041I. Preliminarily, all approaches to causation agree with the statement in *Ingot* that even if the plaintiff were unaware of the misstatement, he or she can recover damages if the misstatement 'by its very nature, causes the plaintiff's loss'.[65] That is, causation arises even if the plaintiff was unaware of the false statement. Thus, the answer to the first issue is that the plaintiff should not have to prove that he or she relied on the false statement. The answer to the second issue is that the plaintiff should have to prove that the misstatement caused loss.

It is unlikely that the legislature intended to displace fundamental compensatory principles[66] or impose unjust consequences.[67] Relevantly, it is unlikely that the legislature intended to turn the defendant into an insurer for all the plaintiff's losses, even if they were due to market movements completely unrelated to the misstatement. In *Johnston v McGrath* Gzell J recognised this by refusing to hold a defendant liable if his or her misstatement did not influence the stock price.[68] Further, imposing such unrelated losses is both unjust[69] and inconsistent with established compensatory principles.[70] Stock prices can decline for reasons unrelated to the misrepresentation.[71] These include general market movements.[72] If defendants are liable for unrelated market movements, then they insure plaintiffs for losses that arise through ordinary investing.[73] Plaintiffs would sustain these losses even if no misrepresentation existed. This analysis indicates that the defendant should not be liable for such losses.

Qualitative causation approach implicitly recognises this by requiring examination of all possible causes of the loss. By contrast, bare 'but for' causation or presumed causation would hold the defendant liable even if the loss was due to general market movements. This indicates that qualitative causation is the most appropriate approach. It also coheres with the academic[74] and judicial[75] opinion

65 *Ingot* (2008) 252 ALR 659, 667 [12] (Giles JA) citing *Digi-tech (Aust) Ltd v Brand* (2004) 62 IPR 184, 212 [155] (Sheller, Ipp and McColl JJA).

66 See *Hocking v Western Australian Bank* (1909) 9 CLR 738, 746 (Griffith CJ): 'It is a sound rule to be applied in the construction of all Acts altering the common law, that they are to be taken to alter it only so far as is necessary to give effect to the express provisions of the Act'.

67 See: references to limitations on power and the desire to restrict 'probable' 'excessive exercise' of power in *Federal Commissioner of Taxation v ANZ Banking Group Ltd* (1977) 143 CLR 499, 508-9 (Stephen J); *Mills v Meeking* (1990) 169 CLR 214, 242-4 (McHugh J).

68 *Johnston v McGrath* (2005) 195 FLR 101, 108 (Gzell J).

69 *Duke Group Ltd (in liq) v Pilmer* (1999) 73 SASR 64, 111-13 (overturned on appeal, but without doubting this point).

70 *Canson Enterprises Ltd v Boughton & Co* (1991) 85 CLR 129, 163 (McLachlin J); *O'Halloran v R T Thomas & Family Pty Ltd* (1998) 45 NSWLR 262; *Beach Petroleum NL v Kennedy* (1999) 48 NSWLR 1, 94 [449] (Spigelman CJ, Sheller and Stein JJA).

71 Recognised in *Dura Pharmaceuticals, Inc v Broudo*, 544 US 336 (2005) (Breyer J). See also Cornell and Morgan, above n 14; Lev and de Villiers, above n 58.

72 Zvi Bodie, Alex Kane and Alan Marcus, *Investments* (6th ed, 2005); Mark Grinblatt and Sheridan Titman, *Financial Markets and Corporate Strategy* (2nd ed, 2002).

73 See especially *Dura Pharmaceuticals, Inc v Broudo*, 544 US 336, 343, 345 (2005) (Breyer J); see also Cornell and Morgan, above n 14.

74 See, eg, Jerod Neas, 'Dura Duress: The Supreme Court Mandates a More Rigorous Pleading and Proof Requirement for Loss Causation under Rule 10b-5 Class Actions' (2007) 78 *University of Colorado Law Review* 347.

75 See especially Fox, 'After Dura: Causation in Fraud-on-the-Market Actions', above n 17; *Tricontinental Industries Ltd v PricewaterhouseCoopers LLP*, 475 F 3d 824 (7th Cir, 2007); *D E & J Ltd Partnership v Conaway*, 133 Fed Appx 994, 999-1000 (6th Cir, 2005).

in the United States. With respect to price change, only qualitative causation supports the policy underlying ss 1041E, 1041H and 1041I. First, compensation places plaintiffs into the position they would occupy if the breach had not occurred. As plaintiffs would sustain market-related losses even if no breach existed, liability for market losses does not promote compensation. Second, compensation for market losses may support deterrence and punitive goals. However, this would promote the policy underlying ss 1041E, 1041H and 1041I only if the sections are punitive. While proscriptive provisions, such as s 1041I, may appear to be punitive,[76] s 1041I is punitive only if the legislature intended it to be such.[77] The legislature is unlikely to intend ss 1041E, 1041H or 1041I to be punitive if there are other general penalty provisions in the *Corporations Act 2001* (Cth). Since the legislature achieves punishment through s 1311, it is unlikely that the aforementioned sections are punitive. Thus, only qualitative causation quadrates with the policy behind ss 1041E, 1041H and 1041I.

This analysis indicates that a structured qualitative approach to causation is preferable: the misstatement caused the loss only if the misstatement was a necessary and sufficient cause for the loss, and the loss is not properly attributable to some other supervening event.

V REMOTENESS

The defendant is liable only if the plaintiff's loss is not too remote. Remoteness inquiries determine if the defendant should be liable for losses of this type. Remoteness holds that the defendant is liable only if the nature of the loss is within the scope of liability.[78] This analysis precedes any analysis of the measure of the loss (which is a separate issue from the connection between loss and breach). Policy considerations determine the scope of liability[79] and include the nature of duty and the nature of the wrong.[80]

Three potential remoteness tests exist: the reasonable foreseeability,[81] the direct consequence,[82] and the contractual contemplation test. Reasonable foreseeability posits that loss is not too remote if it is a reasonably foreseeable consequence:

76 See, eg, *Rich v ASIC* (2004) 220 CLR 129; *ACCC v Dermalogica Pty Ltd* (2005) 215 ALR 482.

77 Dennis Pearce and Robert Geddes, *Statutory Interpretation in Australia* (6th ed, 2006) 284.

78 *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254 (Steyn LJ); John Cartwright, 'Remoteness of Damage in Contract and Tort: A Reconsideration' (1996) 55 *Cambridge Law Journal* 488; Jane Stapleton, 'Cause in Fact and the Scope of Liability for Consequences' (2003) 119 *Law Quarterly Review* 388, 411.

79 *Mayfair Ltd v Pears* [1987] 1 NZLR 459, 464, 466 (McMullin and Sommers JJ); Stapleton, above n 78, 411-12, 420-1, 425.

80 Cartwright, above n 78; Stapleton, above n 78, 420.

81 See generally Patrick Diaz and Rosemary Maxwell, 'Insider Trading and the Corporate Acquirer: Private Actions under Rule 10b-5 against Agents Who Trade on Misappropriated Information' (1988) 56 *George Washington Law Review* 600, 644-5.

82 See generally Elizabeth Sacksteder, 'Securities Regulation for a Changing Market: Option Trader Standing under Rule 10b-5' (1988) 97 *Yale Law Journal* 623, 628, 635-6.

this resembles remoteness for unintentional torts such as negligence.[83] The direct consequence test holds that loss is not too remote if it was either intentional or a direct consequence of the defendant's actions. This applies to intentional wrongs such as deceit,[84] trespass[85] and breach of fiduciary duty.[86] The contractual contemplation test holds that loss is not too remote if it is within the parties' contemplation.[87] It is within their contemplation if they have either actual knowledge of the special circumstances that generate the loss[88] or imputed knowledge of it as damage arising in the ordinary course of things.[89] Principles of statutory interpretation indicate that the direct consequence test is appropriate.

This article has argued that, for the purposes of s 1041E, the scope of the liability is limited to the direct consequences of the misstatement, and that, for the purposes of s 1041H, the loss must be reasonably foreseeable. For all practical purposes, this indicates that if the misstatement caused the plaintiff to overpay, then the loss is not too remote. That is, the plaintiff proves remoteness if the plaintiff proves causation. Thus, while remoteness is an important analytical and theoretical consideration, it is unlikely to limit damages in practice.

A *What Is the Current Approach?*

The current approach to remoteness is unclear. The courts have not directly analysed remoteness vis-à-vis s 1041I. The New South Wales Court of Appeal did indicate that common law and equitable principles could not guide the meaning of 'by' in s 1317H.[90] However, it is unclear if the same reasoning should apply to ss 1041H and 1041E. Thus, it is unclear if common law and equitable principles of remoteness can apply to ss 1041I and 1041E. This motivates further analysis of remoteness vis-à-vis ss 1041H and 1041E.

The reasoning vis-à-vis s 1317H is unhelpful. Justice Santow made two incompatible findings in *ASIC v Adler*.[91] First, Santow J held that analogous

83 *A-G v Geothermal Produce NZ Ltd* [1987] 2 NZLR 348; *Overseas Tankship (UK) Ltd v Morts Dock & Engineering Co Ltd* [1961] AC 388, 424-6 (Lord Simmonds); *Versic v Conners* [1969] 1 NSWR 481.

84 *Foster v Public Trustee* [1975] 1 NZLR 26, 29 (Cooke J); *Nicholls v Taylor* [1939] VLR 119; *South Australia v Johnson* (1982) 42 ALR 161, 169-70; *Gould v Vaggelas* (1985) 157 CLR 215, 266 (Dawson J).

85 *Mayfair Ltd v Pears* [1987] 1 NZLR 459; *Allan v New Mount Sinai Hospital* (1980) 109 DLR (3d) 634; *Cambridge Water Co v Eastern Counties Leather plc* [1994] 2 AC 264 (chemical solvent nuisance).

86 See especially Justice J D Heydon, 'Are the Duties of Company Directors to Exercise Care and Skill Fiduciary?' in Simone Degeling and James Edelman (eds), *Equity in Commercial Law* (2005) 190; *Hodgkinson v Simms* [1994] 3 SCR 377; *Swindle v Harrison* [1997] 4 All ER 705, 705 (Evans LJ); *Target Holdings Ltd v Redferns* [1996] AC 421, 438-9 (Lord Browne-Wilkinson); *Huff v Price* (1990) 76 DLR (4th) 138, 149; *Pilmer v Duke Group Ltd (in liq)* (2001) 207 CLR 165, 203 [93] et seq (Kirby J).

87 *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 529; *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653; *Alexander v Cambridge Credit Co Ltd* (1987) 9 NSWLR 310, 363-9.

88 *Koufos v C Czarnikow Ltd* [1969] 1 AC 350; *Robophone Facilities Ltd v Blank* [1966] 3 All ER 128, 143 (Diplock LJ).

89 *Koufos v C Czarnikow Ltd* [1969] 1 AC 350; *Hadley v Baxendale* (1854) 156 ER 145, 151 (Alderson B).

90 *Adler v ASIC* (2003) 46 ACSR 504, 652 [707].

91 (2002) 41 ACSR 72.

provisions in the *Corporations Act 2001* (Cth) s 1317H adopt the connecting principles that underlay equitable compensation for breach of fiduciary duty.[92] Second, Santow J held that even if the breach is 'a cause' of the loss, the defendant is liable only if they have 'actual knowledge' or 'reason to suspect' that the loss would occur.[93] These findings are inconsistent: in equity, the defendant is liable whether or not they had actual knowledge or reason to suspect the loss.[94] Instead, the second finding resembles remoteness in contract, where a defendant is not liable if the loss was not within their contemplation from either 'actual' or 'imputed' knowledge. Imputed knowledge includes losses that the defendant has reason to suspect as arising in the ordinary course of things. Bergin J in *Loiterton*[95] approved Santow J's approach, and indicated that if the loss arose 'in circumstances in which [the plaintiff] should have made further enquiry',[96] then the defendant had 'reason to suspect' that the loss would arise.[97]

The current approach is problematic. The notion of having 'reason to suspect' that the plaintiff would suffer the loss does not appear to be relevant to ss 1041E and 1041H. It is unclear when a defendant might have 'reason to suspect' that a false statement might cause a loss, as the notion has no established meaning and the courts did not define clear rules for its operation. This motivates examination of the appropriate approach to remoteness.

B *What Is the Appropriate Approach?*

The current approach to remoteness appears uncertain. Therefore, the issue is the appropriate approach to remoteness. Arguably, analogies to existing general law principles promote a direct consequence test. The argument is as follows: market manipulation, deceit,[98] breach of fiduciary duty[99] address intentional misrepresentations. Deceit and breach of fiduciary duty adopt the direct consequence test.[100] Therefore, market manipulation should follow the direct consequence test. However, this conclusion is valid only if the legislature

92 Ibid [748] (Santow J).

93 *ASIC v Adler* (2002) 42 ACSR 80, 124-5 [175]-[177] (Santow J).

94 See generally *Boardman v Phipps* [1967] 2 AC 46; *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134, 137 (Viscount Sankey), 144-5, 151 (Lord Russel).

95 (2004) 50 ACSR 693.

96 Ibid 733 [109] (Bergin J).

97 Ibid 731 [106] (Bergin J) citing *ASIC v Adler* (2002) 41 ACSR 72 [175] (Santow J).

98 Loke, above n 55. See also *Endresz v Whitehouse* [1998] 3 VR 461; *R v Aspinall* (1876) 2 QBD 48, 62 (Brett AJ); *United States v Brown*, 5 F Supp 81 (1933).

99 See, eg, *Re Bulmer; Ex parte Greaves* [1937] Ch 499; *Canson Enterprises Ltd v Boughton & Co* (1991) 61 BCLR (2d) 1; *Stewart v Layton* (1992) 111 ALR 687, 713 (breach of fiduciary duty by a solicitor).

100 On deceit see *South Australia v Johnson* (1982) 42 ALR 161, 170-1; *Gould v Vaggelas* (1985) 157 CLR 215, 266 (Dawson J). On breach of fiduciary duty see *Canson Enterprises Ltd v Boughton & Co* (1991) 61 BCLR (2d) 1. See also Derek Davies, 'Equitable Compensation: "Causation, Foreseeability and Remoteness"' in Donovan Waters (ed), *Equity, Fiduciaries and Trusts 1993* (1993) 297, 310-12; Heydon, above n 86.

objectively evinced an intention to adopt the direct consequence test.[101] This article argues that the text, purpose and context of ss 1041E and 1041I indicate that the legislature intended to adopt a direct consequence test vis-à-vis s 1041E and a reasonable foreseeability test vis-à-vis s 1041H.

The text of ss 1041E and 1041I supports the direct cause and reasonable foreseeability tests, respectively. Their context is the *Corporations Act 2001* (Cth) as a whole.[102] The legislature likely intended that (a) the words of the *Corporations Act 2001* (Cth) should work 'harmoniously' within each section,[103] and (b) the sections of the *Corporations Act 2001* (Cth) should work 'harmoniously' with each other.[104] Therefore, if the legislation uses different terms to deal with different matters, then the legislators likely intended to deal with the matters differently.[105]

The *Corporations Act 2001* (Cth) deals differently with intentional misrepresentations, proscribed in s 1041E and unintentional misrepresentations, proscribed in 1041H. The differences are that intentional breaches, but not unintentional breaches, have a mental fault element,[106] can involve criminal liability[107] and do not explicitly allow contributing fault.[108] Therefore, intentional misrepresentations (s 1041E) and unintentional misrepresentations (s 1041H) may have different remoteness tests. Further, in both common law and equity unintentional misrepresentations (equivalent to s 1041H) have different remoteness tests from intentional misrepresentations (equivalent to s 1041E).[109] This indicates that the legislature may have intended the direct consequence test for s 1041E and a reasonable foreseeability test for s 1041H. This contention draws further support from the purpose of ss 1041E, 1041H and 1041I.

The direct consequence test promotes s 1041E's proscriptive purpose. Section 1041E proscribes intentional misconduct and, thus, is proscriptive in nature. However, s 1041H pertains to unintentional misconduct and, thus, is less likely to be proscriptive. A defendant is less likely to breach his or her duties if it is easier

101 Implicit in *Murphy v Overton Investments* (2004) 216 CLR 388, 407; *Palgo Holdings v Gowans* (2005) 221 CLR 249, 281 [99] (Kirby J); *R v Lavender* (2005) 222 CLR 67, 103 [111] (Kirby J). See also *Knuller (Publishing, Printing & Promotions) Ltd v DPP* [1973] AC 435, 479.

102 *Re the Commercial Bank of Australia Ltd* (1893) 19 VLR 333; *Solution 6 Holdings Ltd v Industrial Relations Commission (NSW)* (2004) 60 NSWLR 558, 581 (Spigelman CJ); *Palgo Holdings v Gowans* (2005) 221 CLR 249, 264-5 [37] (Kirby J).

103 *R (Daly) v Secretary of State for the Home Department* [2001] 2 AC 532, 548 [28] (Lord Steyn); *Collector of Customs v Agfa-Gevaert* (1996) 186 CLR 389, 396-7.

104 *Colquhoun v Brooks* (1889) 14 App Cas 493, 506; *Mathews v Foggitt Jones Ltd* (1926) 37 CLR 455, 455 (Isaacs J); *Commissioner of Stamps (SA) v Telegraph Investment Co Pty Ltd* (1995) 184 CLR 453, 479: 'the provisions must be read together, "as one connected and combined statement of the will of Parliament"'(Brennan CJ, Dawson J and Toohey J); *Chikonga v Minister for Immigration and Multicultural Affairs* (1997) 47 ALD 49.

105 *R v Lavender* (2005) 222 CLR 67, 104 [114] (Kirby J); *Libke v R* (2007) 230 CLR 559, 592 [95] (Hayne J).

106 *Corporations Act 2001* (Cth) s 1041E(1)(c).

107 *Corporations Act 2001* (Cth) s 1311(1).

108 *Corporations Act 2001* (Cth) s 1041I(1B).

109 Cf the approach to negligence in *Overseas Tankship (UK) Ltd v Morts Dock & Engineering Co Ltd* [1961] AC 388, 424-6 (Viscount Simonds delivering judgment for the Court) to the approach to intentional torts such as deceit in *Gould v Vaggelas* (1985) 157 CLR 215, 266 (Dawson J).

to find him or her liable and, thus, if it is easier to establish that the loss is not too remote.[110] Establishing that the loss is not too remote is easier if the defendant is liable even if the loss is unforeseeable (ie, a direct consequence of the breach).[111] Therefore, the direct consequence test promotes s 1041E's proscriptive purpose.

Arguably, holding defendants liable for unforeseeable losses is unjust,[112] and legislators are unlikely to intend an unjust interpretation.[113] However, the better view is that it is more just to impose the risk of unforeseeable loss on a party if they are morally culpable.[114] Persons who make intentional or reckless misstatements are morally culpable.[115] Section 1041E explicitly pertains to intentional or reckless misrepresentations.[116] Therefore, if persons contravene s 1041E then they are morally culpable; and thus, it is more just to impose the risk of loss on them. Moral approbation is also consistent with s 1041E's proscriptive purpose.[117] Therefore, the direct consequence test best promotes s 1041E's proscriptive purpose. However, since s 1041H pertains to unintentional misconduct, the direct consequence test may not apply to it.

The direct consequence test promotes the compensatory purpose. In a commercial context, rules might best facilitate liquidated damages awards in general and compensation in particular, if the rules are clear, predictable and workable.[118] Therefore, it is unlikely that the legislature intended a remoteness test that is unpredictable, unclear or unworkable.[119] However, remoteness is predictable only if its nature is clear.[120] The reasonable foreseeability test is not clear; instead, the reasonable foreseeability test gives courts wide discretion to determine the scope of the liability[121] and the kinds of damage that are foreseeable. This discretion is predictable only if clear rules guide how courts exercise the discretion. However, no pre-existing legal rules exist to guide to a conclusion regarding whether a

110 Andrew Tettenborn, '*Hadley v Baxendale* Foreseeability: A Principle beyond Its Sell-by Date?' (2007) 23 *Journal of Contract Law* 120; Justice Andrew Tipping, 'Causation at Law and in Equity: Do We Have Fusion?' (2000) 7 *Canterbury Law Review* 443.

111 *Doyle v Olby (Ironmongers) Ltd* [1969] 2 QB 158; *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254, 279-81 (Lord Steyn).

112 See, eg, Justice Frank Easterbrook and Daniel Fischel, 'Optimal Damages in Securities Cases' (1985) 52 *University of Chicago Law Review* 611, 622-3; Lev and de Villiers, above n 58, 29-30.

113 *Ingham v Hie Lee* (1912) 15 CLR 267; *Public Transport Commission of New South Wales v J Murray-More (NSW) Pty Ltd* (1975) 132 CLR 336, 350.

114 *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254, 279-81. Argument raised in Elliott, above n 4, 589.

115 *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254, 279-81.

116 *Corporations Act 2001* (Cth) s 1041E(1)(c).

117 Andrew Burrows, *Remedies for Torts and Breach of Contract* (3rd ed, 2005) 408; *Kuddus v Chief Constable of Leicestershire Constabulary* [2002] 2 AC 122, 63-5 (Lord Nicholls); *Rookes v Barnard* [1964] AC 1129, 1226 (Lord Devlin).

118 Stapleton, above n 78, 422.

119 *Blue Metal Industries Ltd v Dilley* (1969) 117 CLR 651; *Cooper Brookes (Wollongong) Pty Ltd v Commissioner of Taxation (Cth)* (1981) 147 CLR 297, 320-1 (Mason and Wilson JJ).

120 Lionel Smith, 'Fusion and Tradition' in Simone Degeling and James Edelman (eds), *Equity in Commercial Law* (2005) 23.

121 Stapleton, above n 78, 417-18; Jane Stapleton, 'Occam's Razor Reveals an Orthodox Basis for *Chester v Ashfar*' (2006) 122 *Law Quarterly Review* 426.

loss is a reasonably foreseeable consequence of market misconduct.[122] Further, while deceit and breach of fiduciary duty are similar to market manipulation, they cannot guide the development of the reasonable forseeability test, since this test does not apply in cases of deceit or breach of fiduciary duty. And, the approach to negligence cannot guide the principles since negligence is an unintentional action whereas market manipulation (breach of s 1041E) is an intentional action.[123] Therefore, 'reasonable foreseeability' creates uncertainty, which the legislature is unlikely to intend.

The context of ss 1041E and 1041H supports the direct consequence test. The context includes the United States decisions on similar legislation. The United States cases tentatively indicate that, firstly, if the misstatement was *intentional* (as in s 1041E), then the defendant is liable for direct consequences of the misstatement even if the consequence is unforeseeable;[124] but, secondly, if the misstatement was *unintentional* (as in s 1041H), then the defendant is liable only if the loss was foreseeable.[125] Thus, the context of s 1041E and 1041H indicates that the sections should involve respectively the direct consequence test and the reasonable foreseeability test.

It is likely that with respect to market manipulation the legislature intends to adopt these tests for ss 1041E and 1041H. This has the following implications. First, if the defendant contravenes s 1041E, then he or she is liable for any losses that directly arise from the misstatement. Second, if the defendant contravenes s 1041H, then he or she is liable for a loss only if it is reasonably foreseeable. This allows general law concepts to guide the development of statutory compensation to produce the test of remoteness that is clear and quadrates with the nature of market manipulation.

VI CONTRIBUTING FAULT

Contributing fault ensures a connection between the loss and the breach. According to the principles of contributing fault, if the plaintiff is partially at fault for the loss or damage, compensation will be partially reduced. Contributing fault differs from causation.[126] Specifically, contributing fault depends upon policy considerations[127] and not principles of fact or law.[128] It also differs from analysis of the extent of damages. While contributing fault can influence the measure

122 See Gregory van Hoey, 'Liability for "Causing" Violations of the Federal Securities Laws: Defining the SEC's Next Counterattack in the Battle of Central Bank' (2002) 60 *Washington and Lee Law Review* 249, 302-4.

123 See Burrows, above n 117, 81-3; *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254, 279-81 (Lord Steyn).

124 Van Hoey, above n 122, 302-4.

125 See, eg, *R H Johnson & Co v SEC*, 198 F 2d 690, 696 (2nd Cir, 1952).

126 *Horkin v North Melbourne Football Club Social Club* [1983] VR 153, 165; *Alford v Magee* (1952) 85 CLR 437, 460-1.

127 *Horkin v North Melbourne Football Club Social Club* [1983] VR 153, 165.

128 *Podrebersek v Australian Iron & Steel Pty Ltd* (1985) 59 ALJR 492, 493-4.

of damages, it also determines the preliminary question of whether the breach connects with the loss.[129] Section 1041I(1B) explicitly allows contributing fault principles vis-à-vis s 1041H. However, the position vis-à-vis s 1041E remains unclear.

Contributing fault is relevant to causation in misstatement cases if it is consistent with the interpretation of the statute. While Gzell J indicated in *Johnston v McGrath* that contributing fault has a limited role in misstatement cases,[130] these statements were *obiter dicta*. Further, explicit allowance for contributing fault vis-à-vis s 1041H indicates a legislative intent for contributing fault vis-à-vis misstatements.

Three key approaches to contributing fault exist. First, contributing fault may be a complete defence that eliminates a right to compensation. This resembles contributory negligence at common law before apportionment legislation.[131] Thus, if the defendant caused the price inflation, but the plaintiff showed contributing fault (eg, by selling improvidently) then the plaintiff obtains no damages. Second, contributing fault may reduce compensation to the extent that is 'just and equitable' based upon the claimant's share of the responsibility for the damage. This resembles contributory negligence at common law after apportionment legislation.[132] Thus, if the plaintiff knew that the defendant inflated the price by $20, but the plaintiff only thought the inflation was $10, then the court would reduce the amount of damages by $10 per share. Third, courts may exercise a residual discretion to apportion liability. This resembles the approach to contributing fault in equity for breach of an equitable duty.[133] For practical purposes, this resembles the second option. However, it gives a theoretical possibility for the court to award no damages even if the plaintiff is only partially at fault.

The current position vis-à-vis s 1041I resembles the approach in equity. Thus, the courts held that while they can apportion liability under the *Corporations Act 2001* (Cth) s 1317S, the principles of contributing fault do not apply to compensation under s 1041I. However, it is unclear if this is appropriate in the context of market manipulation. This section contends that compensation should incorporate both principles of contributing fault and discretionary apportionment and, thus, incorporate both common law and equitable principles.

A *What Is the Current Approach?*

This article argues that current approach comprises three limbs. First, principles of contributing fault do not apply to market manipulation. Second, even if they did, contributing fault is an 'all or nothing' principle and courts are unlikely to

129 Implicit in *Johnston v McGrath* (2005) 195 FLR 101, 108 [35]-[36] (Gzell J).

130 Ibid 108 [33] (Gzell J).

131 *Butterfield v Forrester* (1809) 103 ER 926; *Joslyn v Berryman* (2003) 214 CLR 552, 559 [17] (McHugh J).

132 See, eg, *Law Reform (Miscellaneous Provisions) Act 1965* (NSW) s 9(1).

133 *Pilmer v Duke Group Ltd (in liq)* (2001) 207 CLR 165, 229-30 [169], 231 [173] (Kirby J).

apportion liability. Third, s 1041I(4) gives courts a *residual* discretion to apportion liability under s 1317S. However, it is unclear if this approach is appropriate for market manipulation.

Firstly, courts interpreted s 1041I as prohibiting principles of contributing fault in actions for breach of s 1041E.[134] *Dartberg*[135] indicated that contributing fault can apply only if the statute expressly allows it. The Court reasoned that s 1041I is similar to *TPA* s 82. Courts held that s 82 of the *TPA* incorporates contributing fault only if other provisions in the *TPA* expressly allow it.[136] Therefore, by analogy to s 82, contributing fault applies to s 1041I only if the legislation expressly allows it. Section 1041I(1B) expressly permits contributing fault in actions for breach of 1041H, but does not mention other provisions such as s 1041E.[137] Therefore, *Dartberg* indicates that contributory negligence applies to breaches of s 1041H, but not of s 1041E.

Secondly, even if contributing fault applied to s 1041E, it would be an 'all or nothing' defence. That is, if the plaintiff committed even a small act of contributory negligence, then they would receive no compensation. Santow J argued that *Corporations Act 2001* (Cth) s 1317H holds that courts must specify the amount of compensation; these words are strict and preclude apportionment. Thus, Santow J prohibited apportionment between concurrent wrongdoers in a primary proceeding for compensation.[138] Bergin J in *Loiterton* affirmed this in *obiter dicta*.[139] Therefore, even if contributing fault applies to breaches of s 1041E, courts would preclude apportionment of liability.

Thirdly, courts have a residual discretion to apportion liability. *Corporations Act 2001* (Cth) s 1317S gives courts discretion to relieve the defendant wholly or partly[140] from liability if they acted 'honestly'.[141] A person acts honestly only if they are 'without moral turpitude'.[142] The defendant bears the onus of positively proving honesty, and not mere absence of dishonesty.[143] *Loiterton* indicates that the extent of the defendant's liability depends upon their fault[144] and the causative potency of their actions.[145] Bergin J acknowledged these considerations are the same ones that determine if a court will apportion liability for contributory

134 *Dartberg Pty Ltd v Wealthcare Financial Planning Pty Ltd* (2007) 164 FCR 450, 453-6 [4]-[15] (Middleton J) ('*Dartberg*').

135 Ibid.

136 See especially *Henville v Walker* (2001) 206 CLR 459; Joachim Dietrich, 'The Decline of Contributory Negligence and Apportionment: Choosing the Black or White of All-or-Nothing over Many Shades of Grey?' (2003) 11 *Torts Law Journal* 51, 58.

137 *Australian Securities and Investments Commission Act 2001* (Cth) s 12GF(1B)(a); *Corporations Act 2001* (Cth) s 1041(1B)(a).

138 *ASIC v Adler* (2002) 42 ACSR 80, 112-14 [113]-[124] (Santow J).

139 *Loiterton* (2004) 50 ACSR 693, 733 [111] (Bergin J).

140 Ibid.

141 *Corporations Act 2001* (Cth) s 1317S(b)(i).

142 *ASIC v Adler* (2002) 42 ACSR 80, 123 [166] (Santow J).

143 Ibid 123 [166], [167], 124 [173] (Santow J).

144 *Loiterton* (2004) 50 ACSR 693, 733 [111] (Bergin J).

145 Ibid [112].

negligence.[146] Therefore, s 1317S enables discretionary apportionment. This resembles apportionment in equity.

The current approach to compensation precludes notions of contributing fault but allows courts to apportion liability under *Corporations Act 2001* (Cth) s 1317S. This resembles contributing fault in equity. However, courts achieved this by following *TPA* s 82. They did not analyse rigorously if the legislature intended contributory negligence to apply to market manipulation. Thus, the issue is if the courts' approach is principled.

B *What Is the Appropriate Approach?*

Compensation for market manipulation should incorporate principles of contributing fault only if the legislature intended it. The Court in *Dartberg* rejected contributing fault plea.[147] However, *Dartberg* did not explicitly analyse either the legislature's intentions or the nature of market manipulation. Thus, the issue is whether compensation for market manipulation incorporates principles of contributing fault. This article argues that contributing fault is consistent with the language, purpose and context of ss 1041E and 1041I.

Read in context, the language of ss 1041E, 1041H, 1041I(1B) is consistent with allocation of contributing fault. Section 1041I(1B) expressly allows contributing fault for breaches of s 1041H but does not mention s 1041E. Arguably, if the legislation considers ss 1041H and 1041E differently, it intends contributing fault to apply differently.[148] However, the better view is based on the fact that the legislature added s 1041I(1B) by amendment.[149] Before amendment, s 1041I did not preclude contributing fault for contravention of any provision. Section 1041I(1B) explicitly defines contributing fault vis-à-vis s 1041H. If the legislature intended to preclude contributing fault vis-à-vis any other breach, the amendment would have precluded it. That the amendment did not preclude contributing fault evinces an intention that contributing fault apply to breaches of s 1041E.

Extrinsic materials confirm this. The Explanatory Memorandum can weakly[150] indicate the legislation's policy.[151] Here, it indicates that s 1041I(1B) intends to mirror amendments to *TPA* s 82 that permit contributory negligence for contravention of *TPA* s 52.[152] However, s 52 applies to misleading and deceptive

146 Ibid.

147 *Dartberg* (2007) 164 FCR 450, 456 [18] (Middleton J).

148 *R v Lavender* (2005) 222 CLR 67, 104 [114] (Kirby J); *Libke v R* (2007) 230 CLR 559, 592 [95] (Hayne J).

149 *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (Cth) sch 3 ss 1-4.

150 *Singh v Commonwealth* (2004) 222 CLR 322, 363; Justice Michael Kirby, 'Towards a Grand Theory of Statutory Interpretation: The Case of Contracts and Statutes' (2003) 24 *Statute Law Review* 95, 98.

151 See, eg, *Assam Railways and Trading Co Ltd v IR Commissioners* [1935] AC 445; *Bitumen and Oil Refineries (Aust) Ltd v Commissioner for Government Transport* (1955) 92 CLR 200; *Palgo Holdings v Gowans* (2005) 221 CLR 249, 278-80 [88]-[92] (Kirby J).

152 Explanatory Memorandum, Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003 (Cth).

conduct. In the *Corporations Act 2001* (Cth), s 1041H, not s 1041E, applies to misleading and deceptive conduct. Thus, while the legislature clearly intended to remove contributing fault vis-à-vis s 1041H, it did not express a clear intention vis-à-vis s 1041E. This may evince an intention to retain principles of contributing fault for breaches of s 1041E.

This textual interpretation is persuasive. The amendment that inserted s 1041I(1B) attempts to balance the rights of defendants and plaintiffs.[153] It is true that, subjectively, legislators may not have intended contributing fault to apply to s 1041E. However, it is impossible to know the subjective beliefs of the legislature.[154] And, for interpretation, only the expressed beliefs, as objectively evinced in the language, purpose and context of the Act, are relevant.[155] Instead, compromises objectively operate like contracts. Courts uphold contracts only if courts implement the text.[156] Section 1041I's text does not expressly exclude contributing fault for contraventions of s 1041E. Therefore, contributing fault can apply to s 1041E. This interpretation also upholds the purpose of ss 1041E and 1041I.

Contributing fault promotes s 1041E's compensatory purpose. The premise behind contributing fault is that the plaintiff should obtain compensation only if the loss is within the reach or expectations of the primary duty.[157] Section 1041E imposes a primary duty to not intentionally mislead the market. This primary duty aims to allow investors to rely on the integrity of the market. If investors can rely on the integrity of market prices, then they need not care for their own interests by checking the accuracy of statements that influence the price.[158] However, this does not imply that defendants are liable even if the plaintiff demonstrates severe contributing fault.[159] If the loss arises because the plaintiff did not care for their own interests, then the defendant had no duty to protect them from the loss.[160] One example illustrates the point. If the investor invests knowing that the price is artificially inflated, then the misstatement does cause the loss. However, in this case the investor does not rely on the integrity of the market. If they do not rely on the integrity of the market, then it is not the purpose of s 1041E to compensate their loss, nor does s 1041E protect them from market manipulation

153 See, eg, Barbara McDonald, 'Proportionate Liability in Australia: The Devil in the Detail' (2005) 26 *Australian Bar Review* 29, 30.

154 Justice Frank Easterbrook, 'Statutes' Domain' (1983) 50 *University of Chicago Law Review* 533, 544-6; Peter Schanck, 'The Only Game in Town: An Introduction to Interpretive Theory, Statutory Construction and Legislative Histories' (1990) 38 *University of Kansas Law Review* 815.

155 *Stevens v Kabushiki Kaisha Sony Computer Entertainment* (2005) 224 CLR 193.

156 See eg, Easterbrook, above n 154; Justice Frank Easterbrook, 'The Role of Original Intent in Statutory Construction' (1988) 11 *Harvard Journal of Law and Public Policy* 59, 64. In Australia, see *Minister for Employment and Workplace Relations v Gribbles Radiology Pty Ltd* (2005) 222 CLR 194, 208 [21] (Gleeson CJ, Hayne, Callinan and Heydon JJ).

157 Rickett, above n 4, 34.

158 Theresa Gabaldon, 'Unclean Hands and Self-inflicted Wounds: The Significance of Plaintiff Conduct in Actions for Misrepresentation under Rule 10b-5' (1986) 71 *Minnesota Law Review* 317, 324-8.

159 Dietrich, above n 136, 8.

160 John Carter, Elisabeth Peden and Greg Tolhurst, *Contract Law in Australia* (5th ed, 2007) [35-29]; *Davies v Swan Motor Co (Swansea) Ltd* [1949] 2 KB 291, 308-9, 316, 324.

since they were aware of it. Thus, contributing fault is consistent with the purpose of s 1041E. Therefore, s 1041E should permit contributing fault.

Contributing fault does not weaken s 1041E's proscriptive purpose. Arguably, the operation of the principles of contributing fault weakens any deterrent effect the section might have.[161] However, this argument relies on the premise that the purpose of ss 1041E and 1041I is deterrence. This premise is faulty, since if the defendant contravenes s 1041E, then he or she becomes criminally liable under s 1311. The criminal penalties are a deterrent.[162] Therefore, contributing fault cannot weaken any proscriptive purpose inherent in the legislative provisions. The principles of contributing fault are consistent with s 1041I's text and quadrate with the nature of s 1041E. Therefore, contributing fault should apply. Further, s 1317S gives courts discretion to apportion liability between the plaintiff and the defendant. Therefore, compensation resembles a combination of common law contributing fault with equitable discretions.

VII MITIGATION

Mitigation ensures that the loss connects to the breach by barring recovery for avoidable losses. While mitigation, or lack thereof, can influence the measure of damages, it can also establish whether the breach properly relates to the loss.

Common law mitigation comprises three principles.[163] The nature of the underlying obligation, that is, compliance with ss 1041E and 1041H, determines if and how these principles apply.[164] First, loss is not compensable if the plaintiff could reasonably have avoided it.[165] This means that if the plaintiff knew of the misstatement, and could have sold the stock before the market realised (and the price decreased), then the plaintiff could have avoided the loss and should not receive compensation. Second, defendants are liable for reasonable costs of mitigation.[166] Here, this means that the defendant is liable for transaction costs. Third, if the plaintiff mitigates, then mitigation reduces the defendant's liability.[167] So if the misstatement inflates the price by $20 per share, but the plaintiff only suffers a loss of $10, then the defendant is only liable for $10 of damages. This article argues that only the third principle applies to damages for breach of ss 1041E and 1041H.

161 Gabaldon, above n 158.

162 *Harris v Digital Pulse* (2003) 197 ALR 626, 639 [171] (Mason P); *Lamb v Cotogno* (1987) 164 CLR 1; James Edelman, 'A "Fusion Fallacy" Fallacy' (2003) 119 *Law Quarterly Review* 375, 377.

163 Harvey McGregor, *McGregor on Damages* (2003) 216-17; Michael Bridge, 'Mitigation of Damages in Contract and the Meaning of Avoidable Loss' (1989) 105 *Law Quarterly Review* 398, 398.

164 See eg, McGregor, above n 163, 237-49.

165 *Automatic Fire Sprinklers Pty Ltd v Watson* (1946) 72 CLR 435, 451; *Wenham v Ella* (1972) 127 CLR 454, 460-1. For tort, see *Glavonjic v Foster* [1979] VR 536.

166 *British Westinghouse Electric & Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd* [1912] AC 673, 689-90 (Viscount Haldane LC, Lord Ashbourne, Lord MacNaghten and Lord Atkinson agreeing).

167 Ibid. See also *Jones v Fabbi (No 2)* (1974) 37 DLR (3d) 316.

Courts assumed that mitigation applies to the analogous s 12GF of the *ASICA*.[168] Thus, *ASIC v Australian Investors Forum Pty Ltd (No 3)*[169] indicated that if an investor could have avoided loss, then the loss was not recoverable.[170] However, the Court did not clearly premise this on principles of mitigation, did not define which of the three mitigation limbs apply to compensation, and did not stipulate the nature of those limbs. Further, the Court did not consider if principles of mitigation quadrate with the nature of market manipulation. Instead, this section argues that only limb three is appropriate.

Limb one (unreasonable failure to mitigate) cannot apply to ss 1041E and 1041H. Loss is not compensable if the plaintiff could have reasonably avoided it.[171] The plaintiff bears this duty to mitigate only if they know of the underlying breach.[172] Therefore, three reasons indicate that plaintiffs should not bear a duty to mitigate. First, if the plaintiff acquires inside information of the manipulation and trades on that information to mitigate their loss, then they commit a crime.[173] Committing a crime is not a reasonable act of mitigation.[174] Therefore, an insider's failure to sell is not a failure to mitigate. Second, if the plaintiff is not an insider, they know of the manipulation only if the whole market knows. If the whole market knows, then other investors will sell the stock and its price will fall. Thus, if they are not an insider, they have no opportunity to mitigate their loss. Third, selling shares after the fall is not a reasonable act of mitigation. The post-disclosure price is volatile.[175] If the stock price is volatile, then deciding whether or not to sell the stock is risky. Reasonable mitigation does not include taking risky actions.[176] Therefore, reasonable mitigation does not include selling the stock.

Limb two (costs of mitigation are recoverable) cannot apply. The only costs that investors incur are transaction costs. The plaintiff would eventually incur the costs of selling even if the defendant did not breach ss 1041E and 1041H. Also, a cost is not a cost of mitigation if the plaintiff would incur it anyway.[177] Therefore, transaction costs are not a cost of mitigation. Thus, this mitigation limb is inapposite.

Limb three (avoided losses are not compensable) does apply. The compensatory purpose of ss 1041E and 1041H supports limb three. Compensation under s 1041I

168 See, eg, *Motor Trade Finances Prestige Leasing Pty Ltd v Elderslie Finance Group Co Ltd* [2006] NSWSC 1348 (Unreported, White J, 8 December 2006) [244]-[251].

169 (2005) 56 ACSR 204.

170 Ibid 214 [64] (Palmer J).

171 *Hansen v Northern Land Council* [1999] NTSC 69, [32] (Unreported, Angel J, 12 July 1999); *Glavonjic v Foster* [1979] VR 536, 536 (Gobbo J). See also *Hoad v Scone Motors Pty Ltd* [1977] 1 NSWLR 88.

172 See a discussion on mitigation vis-à-vis fiduciary duties: Ho, above n 25, 75-6.

173 *Corporations Act 2001* (Cth) s 1043A.

174 The cases holding that plaintiff need not harm innocent persons or jeopardise commercial reputation are *Banco de Portugal v Waterlow and Sons Ltd* [1932] AC 452 and *Finlay v Kwik Hoo Tong* [1929] 1 KB 400 respectively.

175 Mark Mitchell and Jeffry Netter, 'The Role of Financial Economics in Securities Fraud Cases: Applications at the Securities Exchange Commission' (1994) 49 *Business Lawyer* 545.

176 See especially *Hoad v Scone Motors Pty Ltd* [1977] 1 NSWLR 88, 95 (Moffit P); *Jewelowski v Propp* [1944] KB 510.

177 See especially *McRae v Commonwealth* (1951) 84 CLR 377.

places the plaintiff in the position that they would occupy if they did not sustain the loss. But s 1041I does not promote over-compensation.[178] Thus, if the investor manages to avoid any loss and the court orders full compensation under s 1041I, then the court over-compensates the plaintiff. This does not achieve s 1041I's compensatory purpose. Thus, the issue is whether it is possible for the investor to avoid any loss.

If the defendant breaches ss 1041E or 1041H, then the plaintiff sustains a loss at the time of the purchase.[179] However, at this time the plaintiff simply has not realised the loss (eg, by selling the shares). The loss is the difference, at the time of the purchase, between (a) the current price that is due to the manipulation, and (b) the true value at which it would trade if there were no inflation.[180] Thus, if the investor (innocently) sells the shares before the market knows of the misstatement, then they avoid any loss.[181] Mitigation does apply to compensation under s 1041I for breach of ss 1041E and 1041H; however, only the third limb applies: avoided losses are not compensable.

VIII CONCLUSION

Investors have a primary right to trade in a market that is free of misstatements. Investors also have a secondary right to compensation for loss or damage that arises 'by' conduct that breaches that primary right. This paper analysed the meaning of 'by' and concluded that the current approach does not quadrate with either the nature of false statements or the intentions of the legislature. Instead, an approach that draws upon existing principles in common law and equity fits with investors' right to trade in a market free of misstatements.

178 *Henville v Walker* (2001) 206 CLR 459, 476 [44] (Gleeson CJ). See also *ASIC v Australian Investors Forum Pty Ltd (No 3)* (2005) 56 ACSR 204, 214 [64] (Palmer J); David Wright, 'Monetary Remedies under the *Trade Practices Act*' (2002) 22 *Australian Bar Review* 39.

179 See especially *Sons of Gwalia Ltd v Margaretic* (2007) 231 CLR 160; Sharon Christensen and Stephen Lumb, 'Ascertaining When Loss Is First Suffered by Misleading Conduct: Relevance of Contingencies, Future Predictions and Concealment' (2005) 13 *Trade Practices Law Journal* 149, 151.

180 See Cornell and Morgan, above n 14.

181 See especially ibid 886.