

Expert Evidence Under Review - Makita v Sprowles

Heydon JA's judgment in *Makita (Australia) Pty Ltd v Sprowles (2001) 52 NSWLR 705* ("Makita's case") considers what is required for an expert's report to be both admissible and persuasive.

The basic principle is that the Court must be able to arrive at an independent assessment of an expert's opinion and its value and this can only be done if the basis of the opinion is clearly explained by the expert. The following key points were raised by Heydon JA:

1. An expert gives an opinion based upon certain facts, thus the facts giving rise to the expert's opinion must be clearly set out.
2. The judge must then determine whether the facts accepted or assumed by the expert have been proved. Facts "observed" by the expert must be identified and admissibly proved by the expert. Facts which are assumed by the expert must be identified and proved in some other way. "If other admissible evidence establishes that the matters assumed are "sufficiently like" the matters established "to render the opinion of the expert of any value", even though they may not correspond "with complete precision", the opinion will be admissible and material".
3. It must be agreed or demonstrated that there is an area of specialised knowledge in which the witness has become an expert by reason of training, study or experience.
4. The opinion must be wholly or substantially based on the witness's expert knowledge applied to the relevant facts.
5. The expert must explain the intellectual basis of the conclusions reached. That is, how the field of specialised knowledge in which the witness is expert applies to the facts assumed or observed so as to produce the opinion propounded. It is possible for an expert to adopt statements made in scientific works as part of his or her testimony, but bare references to particular propositions carry no weight unless their basis is explained. The expert's duty is to furnish the judge with the necessary "scientific" criteria for independently testing the accuracy of the expert's conclusions.

Experts' Obligations

Heydon JA quoted the well known principles set out by Cresswell J in *National Justice Compania Naviera SA v Prudential Assurance Co Ltd ("the Ikarian Reefer") [1993] 2 Lloyd's Rep 68*, which have been influential in the formulation of court

guidelines to experts' obligations. These principles form the basis of the proposed new Family Law Rules regarding experts' obligations and the Federal Court of Australia's guideline for experts. They include:

- that an expert witness should provide independent assistance to the Court by way of an objective and unbiased opinion;
- an expert witness should state the facts or assumptions upon which his or her opinion is based;
- an expert witness should make it clear when a particular question or issue falls outside the expert's expertise;
- if an expert's opinion is not properly researched because the expert considers that insufficient data is available, then this must be stated with an indication that the opinion is no more than a provisional one;
- if an expert changes his or her opinion on a material matter having read the other side's expert's report, or for any other reason, such change of view should be communicated to the other side without delay and when appropriate to the Court; and
- where an expert's report refers to photographs, plans, calculations, analyses, measurements, survey reports, or other similar documents, these must be provided to the opposite party at the same time as the exchange of reports.

The Case

In *Makita v Sprowles* the New South Wales Court of Appeal unanimously overturned the original judgment in favour of the plaintiff by rejecting the were slippery and that she had fallen because of the slipperiness of the stairs, she was entitled to judgment in her favour.

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Expert Evidence Under Review - Makita v Sprowles (cont. from p1)

The plaintiff relied on the expert evidence of Professor Morton, a physicist who specialised in the investigation of slipping accidents. The defendant did not call any expert evidence. Professor Morton conducted a number of tests on the stairs and on the shoes the plaintiff was said to have been wearing at the time of the accident. On the basis of these tests he concluded that unless a person was wearing shoes "having a fairly high level of inherent grip" the stairs were sufficiently slippery to be dangerous even when dry and free of contamination.

Professor Morton's expert evidence was rejected largely on the basis that it conflicted with evidence that the plaintiff had walked on the stair over 500 times prior to the time that she fell (ie over a period of almost 2½ years) and that she had not had problems using the stairs previously. There was no evidence of any other persons having slipped on the stairs either before or after the accident. The plaintiff's supervisor gave evidence that he had never found the stairs slippery.

Both Powell JA and Heydon JA were critical of Professor Morton's failure to adequately explain the significance of the results of his tests and the basis of his ultimate finding. One particular shortcoming was Professor Morton's failure to explain why demonstrated adherence to the Australian Standard for the surface friction of floors was not, in his opinion, sufficient to establish that the stairs were safe.

Changes to the Family Law Rules - Impact on Experts

The Family Law Rules are currently being redrafted with the new rules to come into effect on 1 January 2004.

The revised rules can be expected to have a significant impact on experts briefed in Family Court matters and expands upon the present provisions regarding expert evidence contained in Order 30A of the Family Law Rules.

These changes, as they affect experts, follow from the discussion paper issued last year "The Changing Face of the Expert Witness".

The revised rules provide for much greater court supervision of the use of experts. They impose detailed obligations upon experts with some significant penalties for failure to comply.



Key features include:

- **Court Must Approve Calling of Expert**

The rules provide that a party may only rely on expert evidence with the Court's permission. The Court may also appoint an expert. An expert retained in a Family Court matter must be given instructions in writing and provide a written report which must then be served on the opposing party.

- **Conference of Experts**

If parties call their own experts to give evidence on the same question they must arrange for them to confer without the parties and their lawyers. At this conference, the experts must identify where they agree and disagree and the reason for any disagreement in dispute. They must also determine what action might be taken to resolve any outstanding issues.

- **The Expert's Duty**

The rules provide that an expert has a duty to help the Court with matters that are within the expert's knowledge and capability, which overrides the expert's obligations to the party instructing the expert or paying the expert's fees and expenses. This duty is stated to include a duty to:

- (a) take into account the primary goal of ensuring that each case is resolved in a just and timely manner at the lowest possible cost to the parties and the court;
- (b) to be independent, impartial,
- (c) to give an objective and unbiased opinion;
- (d) to conduct the expert's function in a timely way;
- (e) to avoid acting on instructions or a request to withhold or avoid agreement at a conference of experts;
- (f) to consider all material facts, including those that may detract from the expert's opinion;
- (g) to tell the Court when a particular issue falls outside the expert's expertise;
- (h) to produce a written report that complies with the rules.

The rules provide that an expert's report must:

- (a) include the written instructions given to the expert and any other document mentioned in the report; and
- (b) be verified by affidavit.
- (c) include a statement about the methodology used in the production of the report; and
- (d) state the facts supporting the expert's conclusions, including:
 - (i) the literature or other material used in making the report;
 - (ii) the relevant facts and assumptions on which the expert's opinions are based;
 - (iii) a clear statement about the facts in the report that are within the expert's knowledge.
 - (iv) a summary of the range of opinion;
 - (v) a summary of conclusions reached.

The affidavit verifying the expert's report must state: *"I have made all the inquiries that I believe are necessary and appropriate and to my knowledge there have not been any relevant matters omitted from this report. I believe that the facts within my knowledge that have been stated in this report are true. The opinions I have expressed in this report are truly held. I have read and understand the Family Court Practice Direction Guidelines for Experts and have complied with them. I have complied with the requirements of any relevant experts protocol, being I am independent of the parties and their lawyers. I understand my duty to the court and I have complied with it and will continue to do so. I understand that if I breach my obligations to the court, the sanctions the court may impose include an order that I pay costs and the court's findings be published"*.

The Practice Direction Guidelines for Experts referred to in the affidavit have not been yet been drafted.

- **Failure to Comply**

If an expert fails to comply with the obligations set out above, their report may be excluded from evidence or be given little weight. In addition the court might make an order that the expert meet the costs thrown away by reason of the expert's negligence, improper conduct, undue delay or failure to comply with the rules or guidelines. The court might also order that the expert must not charge for specified work or repay money already paid for that work.

- **Questions to Experts**

The rules enable a party to apply to the court for an order that an expert answer specific questions to clarify his or her report.

- **Obtaining Further Information to Complete Report**

The rules also permit applications to be made to the court for disclosure by an opposing party of information required to enable an expert to perform his or her role. This applies only to "financial cases" such as a property or maintenance disputes.

- **Single Expert**

If the court is satisfied that expert evidence is necessary on a particular issue and it is not appropriate for each party to appoint an expert for the issue; it may order the evidence to be given a single expert, either selected by agreement by the parties or selected by the court.

The parties must prepare a joint letter of instruction in such circumstances, and are equally liable to pay such an expert's reasonable fees and expenses incurred in preparing a report.

If a single expert has been appointed in relation to an issue, a party must not obtain a report or adduce evidence from another expert on the same issue without the permission of the court.

Executive Options

Executive stock options (“ESOs”) have been applied as a means of attracting, motivating and retaining senior employees, especially in companies in new technology industries. They align the interest of employees and shareholders by rewarding executives upon appreciation of share prices.

On 13 May 2003, the ASIC released guidelines on key considerations in valuing and disclosing options granted in their annual directors’ reports. These guidelines are effective for the financial year ended 30 June 2003 and apply to listed companies only.

Also, Accounting Proposal ED 108 was recently released by the Australian Accounting Standards Board. ED 108 proposes that a standard be operative for years beginning on or after 1 January 2004 and requires all share-based payments to be recognised in the financial statements and that the company record as an expense equity granted to employees.

ED 108 refers to six key factors that option valuation model should take into account:

- ★ the exercise price of the option
- ★ the life of the option
- ★ the current price of the underlying security / share
- ★ the expected volatility of the share price
- ★ the dividends expected on the shares
- ★ the risk-free interest rate for the life of the option.

The Black Scholes valuation formula is generally applied to traditional ESO’s. However, many recent ESO’s have idiosyncratic features that complex their valuation such as:

- ★ long periods to maturity, resulting in market prices being unavailable because similar exchange traded options do not exist.
- ★ performance hurdles (internal, peer or based on an index, etc),
- ★ non-marketability (ESOs are not tradeable prior to vesting),
- ★ forfeiture, if executive leaves prior to vesting date.

ED 108 states for the purpose of measuring the remuneration of an individual for disclosure in the directors’ report, it should be assumed that the individual director and executive officer will continue to provide service until vesting date, unless it is probable that the particular individual will cease at an earlier date.

ED 108 and ASIC’s draft guidelines mean ESOs accounting / disclosure value can differ significantly from their market value and may well be overstated. This has consequences for family law property settlements.

Munday Wilkinson recently prepared a valuation of a Banking executive’s share options for family law property settlement purposes. Many of the above issues required our consideration in that particular matter.

New Staff - New Strengths

Munday Wilkinson was the first dedicated Forensic Accounting practice in Melbourne and through your support we are pleased to announce the expansion of our staff to six. Our new staff are:

Paul Spence Associate Director

Paul was a Senior Manager with **Deloitte** and has over 14 years experience in Forensic Accounting having worked on numerous matters involving valuations, loss of profits and financial investigations. He also has significant Banking experience.

David Ferrier Associate Director

David was formally a Partner with Benjamin King & Money and a Senior Manager with **Sims Lockwood**. He combines experience in both professional firms and as a CFO in industry. He is well experienced in family law investigations and valuations, loss of profit assessments, due diligence matters and investigations.

Lauren Stanley

The pleasant voice you may now hear in our office is that of Lauren. Lauren is with us 3 days a week and provides the administration support necessary for a growing practice.

Farewell

Sadly for us, Willy Bagg has taken a senior role with business consultants, Business Strategies International, who provide financial consulting services and advice in relation to R&D and Export Market Development Grants. We wish him all the best with his new position.

Further Information

If you would like further information regarding this newsletter or our services, please contact us at:

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