

Daubert and Financial Experts: Standards and Tips for Ensuring Testimony is Admissible

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INTRODUCTION

The 1993 Supreme Court decision in *Daubert v. Merrell Dow* created a new standard for the admissibility of expert testimony. The standard was rooted in Rule 702 of the Federal Rules of Evidence and replaced the one set seventy years earlier in *Frye v. United States*. In 1999, *Kumho Tire Co. v. Carmichael* confirmed that the *Daubert* standard should be used not only for scientific witnesses, but for all experts, including financial experts.

In the sixteen years since *Daubert*, and especially in the ten since *Kumho*, several factors have emerged that can often determine whether the testimony of a financial expert should be admitted at trial. These factors test the reliability and relevance of an expert's testimony. Although financial experts are subject to the same general factors as other experts, each field of expertise has nuances with which experts and attorneys should be familiar.

This article discusses general standards for admissibility under Rule 702 and *Daubert*, the application of those standards to financial experts, and tips ensuring their testimony is admissible.

FRYE v. UNITED STATES

In 1923, *Frye v. United States*¹ established admission of expert testimony based on its “general acceptance in the particular field in which it belongs.”² Having been convicted of second-degree murder, James Alphonzo Frye appealed his case to the District of Columbia Court of Appeals.³ Frye claimed the lie detection evidence used to convict him should have been found inadmissible, as it did not “have such a scientific recognition among psychological and physiological authorities as would justify the courts in admitting expert testimony, deduced from experiments thus far made.”⁴

In affirming the appeal, the *Frye* Court established the doctrine of “general acceptance”:

*Just when a scientific principle or discovery crosses the line between the experimental and demonstrable stages is difficult to define. Somewhere in this twilight zone the evidential force of the principle must be recognized, and while courts will go a long way in admitting expert testimony deduced from a well recognized scientific principle or discovery, the thing from which the deduction is made must be sufficiently established to have gained general acceptance in the particular field in which it belongs.*⁵

ORIGINAL FEDERAL RULE OF EVIDENCE 702

Federal Rule of Evidence 702 eventually supplanted the *Frye* standard, but that change took many years. In 1965, a committee formed under Supreme Court Chief Justice Earl Warren began work on formulating rules of evidence for the federal courts.⁶ After considerable debate and several delays, the Federal Rules of Evidence were passed into law in 1975.⁷ Rule 702 governed admission of expert testimony, but did not mention the *Frye* “general acceptance” test,⁸ leaving the door open for *Frye*’s replacement.

¹ 293 F. 1013 (D.C.Cir. 1923).

² *Id.* at 1014.

³ *Id.* at 1013.

⁴ *Id.* at 1014.

⁵ *Id.*

⁶ Paul R. Rice & Neals-Erik William Delker, A Short History of Too Little Consequence, 191 F.R.D. 678, 683-84 (2000).

⁷ *Id.*

⁸ Rule 702, “Testimony by Experts,” as originally promulgated, provided as follows:

If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise.

DAUBERT v. MERRELL DOW

In 1993, the Supreme Court decision *Daubert v. Merrell Dow Pharmaceuticals, Inc.*⁹, brought landmark change to the standard for admitting expert testimony. Two babies, Jason Daubert and Eric Schuller, were born with serious birth defects which, the plaintiffs alleged, had been caused by their mothers' ingestion of the drug Bendectin.¹⁰ The plaintiffs brought the case relying on expert testimony using "'in vitro' (test tube) and 'in vivo' (live) animal studies that found a link between Bendectin and malformations; pharmacological studies of the chemical structure of Bendectin that purported to show similarities between the structure of the drug and that of other substances known to cause birth defects, and the 'reanalysis' of previously published epidemiological (human statistical) studies."¹¹

Defendant Merrell Dow moved for summary judgment, claiming the plaintiffs' expert testimony was inadmissible.¹² The district court granted summary judgment, saying evidence was only admissible if based on a principle that is "sufficiently established to have general acceptance in the field to which it belongs."¹³ On appeal, the Ninth Circuit affirmed the district court's ruling, citing *Frye*.¹⁴

The Supreme Court granted certiorari¹⁵ and relied upon the Federal Rules of Evidence to overturn the Ninth Circuit's decision. The Court held "[t]he Federal Rules of Evidence, not *Frye*, provide the standard for admitting expert scientific testimony in a federal trial."¹⁶ In his majority opinion, Justice Blackmun wrote:

*The merits of the Frye test have been much debated, and scholarship on its proper scope and application is legion. Petitioners' primary attack, however, is not on the content but on the continuing authority of the rule. They contend that the Frye test was superseded by the adoption of the Federal Rules of Evidence. We agree.*¹⁷

Daubert established a new standard for the admissibility of expert testimony, which focused broadly on the two characteristics of reliability and relevance:

"General acceptance" is not a necessary precondition to the admissibility of scientific evidence under the Federal Rules of Evidence, but the Rules of Evidence – especially Rule 702 – do assign to the trial judge the task of ensuring that an expert's testimony both rests on a reliable foundation and is relevant to the task at hand.

⁹ 509 U.S. 579 (1993).

¹⁰ *Id.* at 582.

¹¹ *Id.* at 583.

¹² *Id.* at 582.

¹³ *Id.* at 583.

¹⁴ *Id.* at 584.

¹⁵ *Id.* at 585.

¹⁶ *Id.* at 586.

¹⁷ *Id.* at 587-8 (citations omitted).

*Pertinent evidence based on scientifically valid principles will satisfy those demands.*¹⁸

The *Daubert* standard for reliability was based on Rule 702 of the Federal Rules of Evidence. The Supreme Court held that the reliability standard is established by Rule 702's requirement that an expert's testimony pertain to "scientific ... knowledge," since the adjective "scientific" implies a grounding in science's methods and procedures, while the word "knowledge" connotes a body of known facts or of ideas inferred from such facts or accepted as true on good grounds.¹⁹

KUMHO TIRE v. CARMICHAEL

The 1999 case of *Kumho Tire Co. v. Carmichael*²⁰ laid to rest any doubts concerning *Daubert*'s universal employment as the standard for admissibility of expert testimony in non-scientific as well as scientific cases. The plaintiff brought a product liability suit against Kumho Tire, alleging that his car crash was caused by defendant's allegedly defective tire.²¹ The plaintiff relied upon a tire failure analysis expert for defect and causation testimony.²² The district court excluded the expert's testimony, citing *Daubert*'s standard for admissibility.²³ Carmichael appealed the decision before the Eleventh Circuit Court of Appeals, which reversed the ruling, claiming the district court had abused its discretion in applying *Daubert* to a non-scientific expert.²⁴ The United States Supreme Court, on certiorari, however, reverted to the initial ruling, finding that *Daubert*'s "gatekeeping obligation," requiring an inquiry into both relevance and reliability, applied not only to "scientific" testimony, but to all expert testimony.²⁵

Although *Kumho* dealt specifically with an engineering expert, the breadth of the Supreme Court's language established a precedent for experts in all fields, including financial experts that set the precedent necessary for financial experts to be judged by the *Daubert* standard. The two decisions, taken together, have established a rigorous, well-defined standard to replace the previous doctrine of "general acceptance" which had prevailed for seven decades since the *Frye* decision.

Although the *Kumho* decision was certainly the pivotal event in the application of the *Daubert* standard to financial expert testimony, the use of *Daubert* to exclude financial experts was not unprecedented:

¹⁸ *Id.* at 597.

¹⁹ *Id.* at 590-91.

²⁰ 526 U.S. 137 (1999).

²¹ *Id.* at 143.

²² *Id.* at 142.

²³ *Id.* at 146-7.

²⁴ *Id.* at 147.

²⁵ *Id.* at 148-9.

*Even prior to the holding in Kumho Tire, the Daubert standards had been applied by several judges to exclude the expert testimony of economists, and these courts had often held that such testimony was unreliable because of the poor methodology employed, particularly if the expert failed to consider other possible variables in the economic analysis, or if the testimony would not aid the jury in its determination.*²⁶

AMENDED RULE OF EVIDENCE 702

Shortly after the *Kumho* decision, the Federal Rules of Evidence were amended to conform to the *Daubert* and *Kumho* standards. The new Rule 702, “Testimony by Experts,” states:

*If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise, if (1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts of the case.*²⁷

Because the Rule only identifies broad areas of review, case law provides the primary guidance for district courts to determine the factors for review in exercising their gatekeeping role.

BURDEN OF PROVING EXPERT TESTIMONY ADMISSIBILITY

The starting point for analyzing the admissibility of any expert testimony is the burden of proof. The proponent of expert testimony bears the burden, under Rule 104(a) of the Federal Rules of Evidence, of proving admissibility by a preponderance of evidence.²⁸ The record should contain an adequate explanation of the expert’s methodology and basis of the testimony.²⁹ If the proponent fails to establish such a record, the testimony may be excluded.³⁰

²⁶ Cecil C. Kuhne, Excluding Testimony of Financial Experts in Federal Litigation: How Far Do the *Daubert* Standards Extend?, 18 St. John’s J. Legal Comment. 525, 535 (2004).

²⁷ Fed. R. Evid. 702.

²⁸ *Daubert*, 509 U.S. at 593.

²⁹ *Elcock v. Kmart Corp.*, 233 F.3d 734, 747 (3d Cir. 2000).

³⁰ *Hamilton v. Emerson Electric Co.*, 133 F.Supp.2d 360, 372 (M.D. Pa. 2001).

FINANCIAL EXPERT’S QUALIFICATIONS AND TESTIMONY MUST FIT THE ISSUES

A financial expert must initially establish that his or her area of expertise fits the testimony being provided and that testimony is relevant to the facts at hand. Courts determine fit by assessing whether the testimony “will aid the jury in resolving a factual dispute.”³¹ The assessment of fit is, in essence, a heightened relevance review that requires a showing of more than bare relevance.³²

The mere fact that an expert is qualified in one area does not necessarily mean their expertise is relevant to related areas. Indeed, “there are many different kinds of experts, and many different kinds of expertise.”³³ If a financial expert does not have the necessary expertise in a specific area, their testimony does not fit and, therefore, is not admissible.³⁴ Thus, in *M.S. Distributing Co. v. Web Records, Inc.*,³⁵ the court held the testimony of a company’s chairperson on lost sales was excludable, in part, because her experience was dated, the business had changed while she was out of it, and her experience in rock ‘n roll did not transfer to hip-hop, country, or comedy.³⁶

Courts should, nevertheless, permit the testimony of an expert with general financial knowledge that is properly applicable to a specific area.³⁷ Thus, in *Cooper Tire and Rubber Co. v. Farese*,³⁸ the court held that an accountant who did not have specialized expertise in the tire industry was not precluded from providing expert testimony concerning a business’s market capitalization reduction.³⁹ If the facts of a case require testimony that goes beyond an expert’s education and experience, it is prudent to rely on another expert and make clear that the opinions offered on these issues are not the expert’s own formulation.

³¹ *Daubert*, 509 U.S. at 591.

³² *In re Paoli Railroad Yard PCB Litigation*, 35 F.3d 717, 745 (3d Cir. 1994), cert. denied, *General Electric Co. v. Ingram*, 513 U.S. 1190 (1995).

³³ *Kumho*, 526 U.S. at 150.

³⁴ *LifeWise Master Funding v. Telebank*, 374 F.3d 917, 928-929 (10th Cir. 2004) (company’s CEO not qualified to testify concerning lost future profits because he was not an economist, statistician, academic, and had no training in regression analysis); *Chemipal Ltd. v. Slim-Fast Nutritional Foods International, Inc.*, 350 F. Supp. 2d 582, 584 (D. Del. 2004) (court excluded damage expert because he had no experience with slimming products and could not relate his knowledge of the sales growth of beer, chocolate, and cosmetics to slimming products); *Pfizer Inc. v. Advanced Monobloc Corp.*, 1999 WL 743927, at *4-5 (Del. Super. Sept. 2, 1999) (using *Daubert* analysis) (excluding testimony of professor who was clearly qualified to testify concerning marketing issues, but not the specific questions in the case).

³⁵ 2003 WL 21087961 (N.D. Ill. May 13, 2003).

³⁶ *Id.* at *10 n.4.

³⁷ *Loeffel Steel Prods., Inc. v. Delta Brands, Inc.*, 387 F. Supp. 2d 794, 801-02 (N.D. Ill. 2005); *TC Systems Inc. v. Town of Colonie*, 213 F. Supp. 2d 171, N.D.N.Y. 2002)

³⁸ 2008 WL 5188235, No. 3:02CV210 (N.D. Miss. Dec. 9, 2008).

³⁹ *Id.* at *3.

The fit also must exist between the expert testimony and the facts of the matter at hand.⁴⁰ The Supreme Court, in *Daubert*, relied upon Federal Rule of Evidence 401 to define relevance between testimony and facts:

*“Relevant evidence” is defined as that which has “any tendency to make the existence of any fact that is of consequence to the determination of the action more probable or less probable than it would be without the evidence.”*⁴¹

If expertise and relevance are proven, the testimony may be admitted provided it is reliable⁴².

THE DAUBERT RELIABILITY STANDARD

Daubert offered four non-exclusive factors that courts may use to judge the reliability of expert testimony: general acceptance of the theory, testing, peer review, and error rate. The Supreme Court did not hold these four factors were either universal or unflinching, stating:

*The inquiry envisioned by Rule 702 is, we emphasize, a flexible one. Its overarching subject is the scientific validity and thus the evidentiary relevance and reliability-of the principles that underlie a proposed submission. The focus, of course, must be solely on principles and methodology, not on the conclusions that they generate.*⁴³

Since the *Daubert* ruling was handed down, these four factors have been important in determining admissibility of expert testimony and courts have subsequently established other factors. Not every factor must be satisfied for admission of a financial expert’s testimony.⁴⁴ The court must decide which factors it will rely upon to determine admissibility.

Below is a discussion of each factor and its implications for financial experts. Although the factors potentially apply to all experts, the specific issues dealt with by financial experts create unique circumstances that, if not closely attended, may lead to an expert’s exclusion. Included is a discussion of many of these issues, but it should be noted that the discussion is by no means all inclusive.

⁴⁰ *Daubert*, 509 U.S. at 591.

⁴¹ *Id.* at 587 (quoting Fed. R. Evid. 401).

⁴² *Cary Oil Co., Inc. v. MG Refining & Marketing, Inc.*, No. 99 Civ. 1725, 2003 WL 1878246, at *2-3 (S.D.N.Y. April 11, 2003) (economist’s testimony admissible because it fit the facts of case). See also *Rider v. Sandoz Pharmaceuticals Corp.*, 295 F.3d 1194, 1202 (11th Cir. 2002); *Rogers v. Ford Motor Co.*, 952 F.Supp. 606, 616 (N.D. Ind. 1997).

⁴³ 509 U.S. at 594.

⁴⁴ *Mata v. Lowe’s Home Centers, Inc.*, SA- 04-CA0691, 2006 WL 5159392, at *3 (W.D. Tex. Feb.9, 2006).

GENERAL ACCEPTANCE

Although *Daubert* overturned *Frye*'s "general acceptance" standard, the Supreme Court maintained that acceptability by the scientific community remained a valuable, if not omnipotent, aspect of a court's admissibility decision. Justice Blackmun's decision states:

"[G]eneral acceptance" can yet have a bearing on the inquiry...Widespread acceptance can be an important factor in ruling particular evidence admissible, and "a known technique which has been able to attract only minimal support within the community, . . . may properly be viewed with skepticism."⁴⁵

Daubert's main clash with *Frye* regarded newer, more groundbreaking methodology. Although *Frye* had specifically required "general acceptance," *Daubert* allowed, in some cases, for analysis "too particular, too new, or of too limited interest to be published."⁴⁶ The opinion agreed with *Frye*, however, in its skepticism of techniques which, though well-known, had attracted "only minimal support within the community."⁴⁷

The general acceptance standard appears to be the most important *Daubert* factor for financial experts. Expert financial testimony is often admitted after it is established that the testimony is based upon an accepted methodology used by other financial experts or professionals.⁴⁸ Expert financial testimony not based on an accepted methodology will most likely be excluded.⁴⁹ A financial expert should, therefore, be well versed in explaining their methodology's support in the relevant community.

TESTING

Daubert held "a key question to be answered in determining whether a theory or technique is scientific knowledge that will assist the trier of fact will be whether it can be (and has been) tested."⁵⁰ The Supreme Court stressed the ability of scientific testimony to be falsifiable and to have undergone testing to determine its validity.⁵¹

⁴⁵ 509 U.S. at 594.

⁴⁶ *Id.* at 593.

⁴⁷ *Id.* at 595 (quoting *United States v. Downing*, 753 F.2d, 1224, 1237 (3d Cir. 1986)).

⁴⁸ *Conwood Co., L.P. v. U.S. Tobacco Co.*, 290 F.3d 768, 793 (6th Cir. 2002) (admitting testimony based on regression analyses, a yardstick test, and a before-and-after test because all three methods are generally accepted methods for calculating antitrust damages); *McIntosh v. Monsanto Co.*, 462 F.Supp.2d 1025, 1033 (E.D. Mo. 2006) (noting an expert's methodology that created a hypothetical "but for" market free from the alleged market restraints was standard in antitrust cases).

⁴⁹ *LifeWise Master Funding v. Telebank*, 374 F.3d 917, 929 (10th Cir. 2004); if *Gallagher v Southern Source Packaging, LLC*, 568 F. Supp.2d 624, 634 (E.D.N.C. 2008); *Sunlight Saunas, Inc. v. Sundance Sauna, Inc.*, 427 F. Supp. 2d 1022, 1030-31 (D. Kan. 2006).

⁵⁰ 509 U.S. at 593.

⁵¹ *Id.* at 594.

In other fields, such as engineering, testing is the most important *Daubert* factor, but it appears less important for expert financial analysis because testing for an individual case is rare. Most experts rely upon recognized research done by others to create their analysis. “If expert testimony is not based on independent research, the party proffering it must come forward with other objective, verifiable evidence that the testimony is based on scientifically valid principles.”⁵² A three-part diagnostic assessment for determining whether an expert’s theory has been adequately tested has been suggested:

- “Is the expert’s theory capable of being tested? If so, has it been tested?”
- “Has the expert performed his own testing? If not, why not?”
- “If a theory has been tested by others, and they have come to contrary conclusions, how does the expert explain his own lack of testing?”⁵³

A financial expert should be prepared to answer these questions.

Testing has been an important factor for financial experts in some cases.⁵⁴ For example, in *Zenith Electronics Corp. v. WH-TV Broadcasting Corp.*,⁵⁵ an expert was tendered to testify concerning the growth of plaintiff’s cable television business and market share in San Juan, Puerto Rico absent an alleged breach of contract and fraud.⁵⁶ The court rejected his claim that the market was “unique” making experience elsewhere irrelevant for conducting a regression analysis.⁵⁷ Citing his lack of testing and other factors, the court found that his reliance on his expertise alone to support his opinions precluded his testimony.⁵⁸ Likewise, in *Cochrane v. Schneider National Carriers, Inc.*,⁵⁹ the court refused to allow an economist to testify concerning the value of lost instruction, guidance, counsel, and training, because the theory was admittedly “theoretical” and had not been tested or a potential error rate shown.⁶⁰

PEER REVIEW

Daubert did not establish peer review as a necessary precursor for admissibility, but discussed its value because “submission to the scrutiny of the scientific community is a component of ‘good

⁵² Mary Oppendahl, James Neudecker and Michael Brown, Alternatives to Cross-Examination: a “How To” Guide for Excluding the Opposition’s Expert’s Testimony under the Federal Rules: Practical Applications of *Daubert v. Merrell Dow*, Practising Law Institute, *Litigation and Administrative Practice Course Handbook Series*, PLI Order Number 7383, May/June 2005, 329.

⁵³ *Id.* at 335 (formatting added).

⁵⁴ *Saia v. Sears Roebuck and Co., Inc.*, 47 F. Supp. 2d 141, 146 (D. Mass. 1999) (“willingness-to-pay” model for hedonic damages inadmissible because not testable).

⁵⁵ 395 F.3d 416 (7th Cir. 2005).

⁵⁶ *Id.* at 418.

⁵⁷ *Id.* at 419-20.

⁵⁸ *Id.*

⁵⁹ 980 Supp. 374 (D. Kan. 1997).

⁶⁰ *Id.* at 380.

science,’ in part because it increases the likelihood that substantive flaws in methodology will be detected.”⁶¹ Thus, in *Apollo Group Inc. Securities Litigation*,⁶² the court admitted an economics expert’s testimony, noting that “the basic regression model he ... [used was] subjected to peer review and publication.”⁶³ Likewise, in *Hayes v. Wal-Mart Stores, Inc.*,⁶⁴ the court, noting that an expert economist’s theory was not peer-reviewed as a factor, excluded his testimony that a punitive damages award of a retailer’s total yearly dividend would not cause it irreparable financial harm.⁶⁵

Experts may subject their work to the approval of specific peers and then testify to the existence and contents of those conversations. Commonly, however, a financial expert’s methodologies (but not conclusions for a particular case) may have been reviewed by the community of their peers:

*The testifying expert may offer proof that the research and analysis supporting the proffered conclusions have been subjected to normal scientific scrutiny through peer review and publication, or, where such evidence is unavailable, he must explain precisely how he went about reaching his conclusions and point to some objective source to show that he has followed the scientific method as it is practiced by at least a recognized minority of scientists in his field.*⁶⁶

ERROR RATES

The Supreme Court in *Daubert* stated that known error rates could be considered in assessing reliability:

*“Additionally, in the case of a particular scientific technique, the court ordinarily should consider the known or potential rate of error, see, e.g., United States v. Smith, 869 F.2d 348, 353-354 (7th Cir. 1989) (surveying studies of the error rate of spectrographic voice identification technique), and the existence and maintenance of standards controlling the technique’s operation.”*⁶⁷

Because a financial expert’s methodology may not have a calculable error rate, courts have admitted such testimony, noting that it “does not have a known rate of error.”⁶⁸ In many instances where a court

⁶¹ 509 U.S. at 593.

⁶² 527 F. Supp.2d 957 (D. Ariz. 2007).

⁶³ *Id.* at 964.

⁶⁴ 294 F.Supp.2d 1249 (E.D. Okla. 2003).

⁶⁵ *Id.* at 1250-1251.

⁶⁶ Opendahl, *supra* note 48, at 329.

⁶⁷ 509 U.S. at 594.

⁶⁸ *Hammes v. Yamaha Motor Corp. USA*, 2006 WL 1195907, No. 03-6456, at * 9 (D. Minn. May 4, 2006)

has criticized the lack of an error rate, it also noted several other infirmities in the testimony when refusing admission.⁶⁹

OTHER FACTORS NOT IDENTIFIED IN *DAUBERT*

Consistent with *Kumho*'s holding that the *Daubert* test is flexible, the lower courts have discussed many other factors in determining whether to allow an expert's testimony, including those listed below. Some of these factors were more important, in many instances, than the original four *Daubert* factors in determining admissibility.

VALID DATA AND INFORMATION

Rule 702 requires that an expert's opinion must be based on sufficient facts and data. In response to this general proposition, courts have stated that an expert's method must be based on "sufficiently reliable facts."⁷⁰ Courts will determine whether *Daubert* challenges to financial expert's facts and data go to weight or admissibility.⁷¹

Courts have, therefore, excluded testimony when an expert failed to verify data provided by their client.⁷² In *United Phosphorus, Ltd. v. Midland Fumigant, Inc.*,⁷³ an economist relied on the deposition testimony of his client's president to determine that the product in question was of such uniform quality that consumers did not distinguish among brands.⁷⁴ The court excluded his testimony, accepting the opposing expert's contention that "it is not acceptable methodology for an economist to rely on deposition testimony of an interested party where objective evidence and analysis exists[sic]."⁷⁵ Likewise, in *TK-7 Corp. v. Estate of Barbouti*,⁷⁶ the court upheld a directed verdict where the only damage evidence was from an expert who relied on a marketing study, which contain unexplained and unsupported assertions.⁷⁷

⁶⁹ *Burton v. Wyeth-Ayerst Lab. Div.*, 513 F. Supp. 708, 717 (N.D. Tex. 2007); *Cochrane v. Schneider Nat. Carriers, Inc.*, 980 F.Supp. 374, 379-380 (D. Kan., 1997).

⁷⁰ *Alexander v. Smith & Nephew, P.L.C.*, 98 F.Supp.2d 1310, 1316 (N.D. Okla. 2000) ("[a]t a minimum, [the expert] should describe the method he used in reaching, and the data supporting, his determination. The Court cannot rely on an expert's mere assurance that the methodology and data are reliable").

⁷¹ *Margulies v. McCleary, Inc.*, 447 F.3d 1115, 1121 (8th Cir. 2006).

⁷² *ID Security Sys. Canada, Inc. v. Checkpoint Sys, Inc.*, 249 F. 2d 622, 695-96 (E.D. Pa. 2003).

⁷³ 173 F.R.D. 675 (D. Kan. 1997).

⁷⁴ *Id.* at 685.

⁷⁵ *Id.*

⁷⁶ 993 F. 2d 722 (10th Cir. 1993)

⁷⁷ *Id.* at 732-34.

Other courts, however, have held that similar failures went only to the weight of the testimony.⁷⁸ And, some opponents ask too much of experts. For example, the court in *Platypus Wear, Inc. v. Clarke Modet & Co.*,⁷⁹ held that an expert's failure to verify the accuracy of his client's sales forecasts and income ledgers was not a grounds for exclusion. It found that "an expert witness is not a private investigator hired to investigate the accuracy of each report or document he used in creating his report," but is only required under Fed. R. Evid. 703 to rely upon documents reasonably relied upon by experts in their field.⁸⁰

VALID AND COMPLETE ASSUMPTIONS

Ideally, a financial expert will have reasonably complete information. Incomplete or disputed information, however, sometimes requires an expert to make certain assumptions in the analysis of damages. The law is clear that an expert may rely upon assumptions to support an opinion on financial issues.⁸¹ It is important these assumptions be well-articulated and shown to be valid based on the facts that *are* available.

If significant assumptions are contrary to or not supported by the evidence, the expert's testimony will often, be found inadmissible.⁸² A few examples of faulty assumptions that caused exclusion are that the plaintiff had a 10% share of the pantyhose market in Lithuania,⁸³ a direct-mail company would penetrate into 49 marketing zones,⁸⁴ and the plaintiff's premium womans' shave gel would have achieved the same market coverage as its mens' shave gel.⁸⁵ If, on the other hand, the assumptions are fairly disputed, the challenge merely goes to the weight of the evidence and the proper remedy is cross-examination.⁸⁶

⁷⁸ *PRS Benefits, LP v. Cent. Leasing Mgmt. Inc.*, No. 3:03-CV-1183-B, 2004 U.S. Dist LEXIS 24135, at *4-6 (N.D. Tex. Nov. 29, 2004); *In re Tasch, Inc.*, 1999 WL 596261, No. 97-15901 at *3 (E.D. La. Aug. 5, 1999).

⁷⁹ 2008 WL 4533914, No. 06-20976 (S.D. Fla. Oct. 7, 2008).

⁸⁰ *Id.* at *5.

⁸¹ *International Adhesive Coating Co., Inc. v. Bolton Emerson International, Inc.*, 851 F.2d 540, 545 (1st Cir. 1988); *Sigur v. Emerson Process Management*, No. 05-1323, 2007 WL 1893632, at *5 (M.D. La. April 25, 2007).

⁸² *Fashion Boutique of Short Hills, Inc. v. Fendi USA, Inc.*, 75 F.Supp. 235 (S.D.N.Y. 1999) (plaintiff did not provide adequate evidence supporting expert's assumption of causation and expert testimony was, therefore, inadmissible); *MapInfo Corp. v. Spatial Re-Engineering Consultants*, No. 02-CV-1008, 2006 WL2811816, at*5 (N.D.N.Y. Sept. 28, 2006).

⁸³ *Lithuanian Commerce Corp. v. Sara Lee Hosiery*, 179 F.R.D. 450, 461 (D.N.J. 1998).

⁸⁴ *Target Mkt. Publ'g. v. ADVCO, Inc.*, 136 F.3d 1139, 1140 (7th Cir. 1998).

⁸⁵ *Pfizer*, 1999 WL 743927, at *5.

⁸⁶ *Synergistics, Inc. v. Hurst*, 477 F.3d 949, 955-6 (8th Cir. 2007) (testimony admissible despite a disputed factual assumption because the objection could be raised on cross-examination); *Minnesota Supply Co. v. Raymond Corp.*, 472 F.3d 524, 544 (8th Cir. 2006) (same).

ALTERNATE CAUSES AND CONTRARY EVIDENCE

A failure to rule out reasonable alternate causes of alleged damage or contrary evidence can be cited as a basis for excluding expert testimony. Thus, in *Blue Dane Simmental Corp. v. American Simmental Assoc.*,⁸⁷ the court upheld the exclusion of an economist's testimony despite his relying on a common before-and-after model for his analysis.⁸⁸ His failure to consider evidence that could have affected his conclusion made his testimony unreliable.⁸⁹

Generally, experts are required to rule out only reasonably likely causes.⁹⁰ Some courts have held that the opponent of admission has the burden of raising alternate causes.⁹¹ Other courts have not explicitly saddled the opponent with that burden.⁹² Nevertheless, as a practical matter, the opponent to admission must raise alternate causes, or their existence is likely to be overlooked.

Even if an expert uses a recognized methodology, their testimony will probably be excluded if they fail to take into account reasonable alternate causes.⁹³ For example, in *Children's Broadcasting Corp. v. Walt Disney Co.*,⁹⁴ a financial expert's testimony, which relied upon a generally accepted methodology (discounted cash flow), was inadmissible because he failed to take into account that the alleged damage could have been caused by legitimate conduct.⁹⁵ Likewise, in *Craftsman Limousine, Inc. v. Ford Motor Company*,⁹⁶ the court upheld the exclusion of an admittedly qualified economics expert because he assumed a conspiracy lowered plaintiff's business growth, but did not take into account other factors, including the emergence of two direct competitors, that could also have lowered growth.⁹⁷

Experts must, therefore, take into account important differences and market factors other than those related to the cause of action that may have affected a party's circumstances. A financial expert of any kind must be able to identify known information that disputes his or her conclusions and be prepared to explain why they are not sufficient to nullify the analysis. An expert's failure to account for facts

⁸⁷ 178 F.3d 1035 (8th Cir. 1999).

⁸⁸ *Id.* at 1041-2.

⁸⁹ *Id.*

⁹⁰ *Lauzon v. Senco Products*, *supra*, 270 F.3d at 693 (the requirement to rule out alternate causes "cannot be carried to a quixotic extreme"); *Westberry v. Gislaved Gummi AB*, 178 F.3d 257, 266 (4th Cir. 1999) ("expert's causation conclusion should not be excluded because he or she has failed to rule out every possible alternate cause").

⁹¹ *Paoli Railroad Yard PCB Litigation*, 35 F.3d at 76

⁹² *Turner v. Iowa Fire Equipment Co.*, 229 F.3d 1202, 1208 (8th Cir. 2000); *Claar v. Burlington Northern Railroad Co.*, 29 F.3d 499, 502 (9th Cir. 1994).

⁹³ *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039, 1056-57 (8th Cir. 2000) (experts' testimony inadmissible because his financial model did not take into account contrary causes, including market events not related to alleged anticompetitive conduct); *Mallettier v. Dooney & Bourke, Inc.*, 525 F. Supp. 558, 668-9 (S.D.N.Y. 2007) (testimony concerning regression analysis excluded because expert did not provide explanation that obvious were considered, analyzed, and ruled out).

⁹⁴ 245 F.3d 1008, 1019 (8th Cir. 2001).

⁹⁵ *Id.* at 1019.

⁹⁶ 363 F.3d 761 (8th Cir. 2004).

⁹⁷ *Id.* at 777.

that are clearly in contradiction to the opinion, or an inability to refute them when presented, undermine the merit of the analysis and may ultimately prove to be grounds for exclusion.

In some cases involving multiple defendants or multiple causes of action, financial experts should be careful to allocate damages to the appropriate defendant or cause. This point is also important as a practical matter. Separating causes or defendants from one another means the dismissal of a cause at summary judgment or the removal of a defendant through settlement will not completely undermine a financial expert's assessment of damages.

RESEARCH CONDUCTED SOLELY FOR LITIGATION

Not surprisingly, courts will apply greater scrutiny to an expert opinion that was developed solely for litigation purposes.⁹⁸ Thus, in *United Phosphorus, Ltd. v. Midland Fumigant, Inc.*, the court excluded an economist's testimony noting that he was president and shareholder of an economics and statistics firm that provided 90% of its services to the legal profession.⁹⁹ The court held that opinions "developed expressly for the purpose of testifying weighs against a finding that his opinions are 'derived by the scientific method.'"¹⁰⁰ Faced with the opposite situation, the court in *Apollo Group Inc. Securities Litigation*,¹⁰¹ permitted an economist to testify noting his "prelitigation research in econometrics."¹⁰²

RELATION OF TESTIMONY TO EXPERT'S NON-LITIGATION WORK

Courts have examined whether the expert "is being as careful as he would be in his regular professional work outside his paid litigation consulting."¹⁰³ What this entails is considering whether the expert has used "the same level of intellectual rigor" in his or her non-litigation work.¹⁰⁴ Thus, the court in *Sheehan v. Daily Racing Form, Inc.*¹⁰⁵ excluded an expert statistician's testimony who found that the birth dates of terminated employees statistically showed age discrimination using standard statistical methods.¹⁰⁶ The statistician, however, failed "to make any adjustment for variables bearing on the decision whether to discharge or retain a person ... [which indicated] a failure to exercise the

⁹⁸ See *Daubert v. Merrill Dow Pharmaceuticals, Inc.*, 43 F.3d 1311, 1317 (9th Cir. 1995).

⁹⁹ 173 F.R.D at 679.

¹⁰⁰ *Id.* at 686 (quoting *Daubert*, 43 F.3d at 1317).

¹⁰¹ 527 F. Supp. 2d 957 (D. Ariz. 2007).

¹⁰² *Id.* at 963.

¹⁰³ *Sheehan v. Daily Racing Form, Inc.*, 104 F.3d 940, 942 (7th Cir.), *cert. denied*, 521 U.S. 1104 (1997).

¹⁰⁴ *Kumho*, 526 U.S. at 152.

¹⁰⁵ 104 F.3d 942 7th Cir. (1997).

¹⁰⁶ *Id.* at 942.

degree of care that a statistician would use in his scientific work, outside of the context of litigation.”¹⁰⁷

CHANGES IN OPINIONS

When an expert changes their opinion, a suspicion will arise that the expert was either not thorough or altering their opinion to avoid challenges in litigation. Courts occasionally have relied on changes to determine that an expert’s testimony was not reliable.¹⁰⁸ Of course, if an expert can demonstrate that the change was caused by evidence that was unavailable at the time the opinion was rendered, it should have no impact on admissibility.¹⁰⁹

It goes without saying that experts are responsible for minimizing the potential for error by preparing thorough opinions and revising them for quality and completeness. If errors, nevertheless, occur they should be promptly recognized and corrected by the expert. Submission of a written opinion or of testimony that is plagued by errors can undermine an expert’s credibility. Although the appearance of carelessness or lack of expertise may be problematic, the possibility of exclusion on the basis of mistaken testimony is of more serious concern to a financial expert.

ANALYTICAL GAP BETWEEN EXPERT’S OPINION AND UNDERLYING DATA

In *General Electric v. Joiner*,¹¹⁰ the Supreme Court permitted a final overarching review of expert opinions in addition to reviewing the foregoing methodological factors. A court may determine that an opinion derived from valid data is unreliable because the analytical gap between the opinion and the data is too great.¹¹¹ *Joiner* further held that trial court expert admissions are reviewed on an abuse of discretion standard.¹¹² In the previously cited *Blue Dane Simmental Corp. v. American Simmental Assoc.*,¹¹³ the court, relying on *Joiner*’s admonition concerning analytic gaps between data and

¹⁰⁷ *Id.*

¹⁰⁸ *Daubert*, 43 F.3d at 1322 (“Any such tailoring of the experts’ conclusions would, at this stage of proceedings, fatally undermine any attempt to show that these findings were ‘derived by the scientific method.’”); *Comer v. American Electric Power*, 63 F. Supp.2d 927, 935 (N.D. Ind. 1999) (“an expert must be able to point to some reliable scientific or factual basis to support any significant change in his specialized testimony”); *In re: TMI Litigation Cases Consolidated II*, 922 F. Supp. 997, 1015 (M.D. Pa. 1996) (“A purportedly scientific opinion that constantly changes merely to avoid critique can hardly be said he based upon ‘good grounds.’”).

¹⁰⁹ *Cf. Brennan’s Inc. v. Dickie Brennan & Co., Inc.*, 376 F.3d 356, 374 (5th Cir. 2004) (change in lost profits, reducing it to half the size in expert’s initial report was based upon more accurate data for a supplemental report and this difference did not affect reliability because the same methodology was used in both reports).

¹¹⁰ 522 U.S. 136 (1997).

¹¹¹ *Id.* at 146.

¹¹² *Id.*

¹¹³ 178 F.3d at 1041-2.

opinions, excluded the expert's testimony.¹¹⁴ In contrast, the court in *Hynix Semiconductor Inc. v. Rambus Inc.*,¹¹⁵ noted an economist's analytic gaps in determining a market's economic substitutes, but refused to exclude him under *Joiner* because of the complexity and significance of the issue.¹¹⁶ There is no bright line test for exclusion under *Joiner*. Thus, if a judge is convinced that testimony is unreliable for any reason, he or she will have the power to exclude it and appellate review will be limited.

CONCLUSION

Standards of reliability and relevance have been the primary factors in determining expert admissibility since the *Daubert* decision in 1993 and have been applied to scientific and non-scientific experts, including financial experts, at least since the *Kumho* decision in 1999. The Supreme Court in *Daubert* was careful to state that its factors were non-exclusive and flexible. It is, therefore, important to carefully review the relevant standards and facts in each case and deal with financial experts' testimony accordingly.

¹¹⁴ *Id.*

¹¹⁵ CV-00-20905, 2008 WL 73689 (N.D. Cal. Jan. 5, 2008).

¹¹⁶ *Id.* at *11.

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