Economic experts

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1 Introduction

The title of this session is "Economic experts: How necessary are they?" I have been asked to address the role of the economic expert in the original decision-making process and how this might differ from the role of the expert in Part IV competition matters. I have been asked also to comment on the use of experts in merits and proceedings for judicial review of decisions by regulators.

The result is a paper that is both comparative and personal. It is comparative because it tries to compare the roles of the economic expert in these different forums: the ACCC, the Competition Tribunal, in trials before the courts and in proceedings for judicial review.

The paper is personal because I am not a lawyer. The paper is the personal view of someone who has experienced these different roles within the constraints of the institutions and rules created by lawyers.

The paper is ordered around three themes. In the first, I reflect on the obligations and duties that an economist must bear in each of the different forums. In the second, I deal with the ways in which the substantial material one presents differs among these forums. In the final section, I deal with the form of one's presentation – and how that must vary among these forums.

2 Obligations and duties

2.1 Obligation to the court

The obligations on an expert appearing before a court or tribunal are clear. – the obligations are those of the Practice Direction of the Chief Justice of the Federal Court in his *Guidelines for Expert Witnesses in Proceedings in the Federal Court of Australia* [1] or, if a jurisdiction has its own Guidelines, they will be very similar to those of the Federal Court.

These rules state the expert's duty plainly:

1. An expert witness has an overriding duty to assist the Court on matters relevant to the expert's area of expertise.
2. An expert witness is not an advocate for a party even when giving testimony that is necessarily evaluative rather than inferential.

[1] The current version is dated 5 May 2008.

3. An expert witness's paramount duty is to the Court and not to the person retaining the expert.

The expert's paramount duty to the court might be thought to be similar to the duties of an advocate. In *Giannarelli v Wraith* Mason CJ stated:

"The peculiar feature of counsel's responsibility is that he owes a duty to the court as well as to his client. His duty to his client is subject to his overriding duty to the court. In the performance of that overriding duty there is a strong element of public interest."[2]

Although the language of Mason CJ in *Giannarelli v Wraith* refers to an overriding duty to the court, the language is quite different from that of the Practice Direction. An economist's interpretation of the difference might be framed in terms of objectives and constraints. The advocate has (and should have) a duty to his/her client; and this is acknowledged in expositions of the topic. This duty is constrained by his/her duty to the court. That is, maximising the interests of the client is subject to a constraint that the advocate must be honest and must not mislead the court; and they must present evidence that is "necessary, relevant, admissible and probative". As Pagone J recently stated in a seminar paper: "What the advocate must do is not simply to propound the client's case, but to do so in a way that helps the decision-maker to achieve the correct outcome."[3]

The expert economist cannot maximise the interests of the client subject to overriding duty to the court. The Practice Direction does not allow this. One's objective must be different: one's duty is to maximise the help that one can give to the Court – subject to the instructions one is given by the instructing lawyer.

2.2 How to manage the lawyer?

If one is giving evidence before a court or tribunal, one is generally retained by a law firm rather than by the lawyer's client. In general, lawyers are familiar with the obligations of experts and respect those obligations. However, this is not universally the case. Occasionally, one comes across lawyers who are tempted to pressure one to do things that may be contrary to the Practice Note.

In my experience, there is a very simple solution to this problem. Simply say to the lawyer in a pleasant non-threatening voice: "I really do not think that I could do that consistent with the Practice Direction of the Chief Justice." In my experience, that is sufficient to get the lawyer off your back. The lawyer is sure to respond: "You misunderstand me completely; I would never suggest that you do anything that would be contrary to the Practice Direction of the Chief Justice."

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[2] (1988) 165 CLR 543 at 556.

[3] G T Pagone, "The advocate's duty to the court in adversarial proceedings", Victorian Bar Ethics Seminar, 23 July 2008, p 3.

The Practice Direction of the Chief Justice is not a weapon to be used lightly. The better approach is to avoid confrontations altogether. In my experience, this can best be done by keeping the lawyer informed from the beginning as to one's results and opinions.

When I was younger, I was more inclined to allow misunderstandings to develop between myself and lawyers who had retained me for the purposes of litigation. These misunderstandings arose because I failed to keep them informed as to the developments in my work or thinking. These days, I try to deal with this by asking, when I am briefed initially, for some basic documents about the nature of the dispute. I then say that, if I can be retained for one day's work, I can read the documents and write a one page reaction – or, if it is preferred, I can attend a conference and give my reaction orally so that there is no record of my involvement in the matter.

I have found that this procedure protects me – and it protects the lawyer, who will not wish to proceed with me if I am unlikely ultimately to be able to support the case he/she wishes to present.

Even if one is able to assure the lawyer at the outset that one is sympathetic to the case he/she wishes to put, one may find that one's views change during the course of preparation for the hearing. In my experience, this problem arises most starkly when one undertakes empirical work: one does not know what the data will show when one starts out; and the data may well yield results that do not favour the interests of the lawyer's client.

In these cases, I try to follow the same precept as in non-empirical work; I try to keep the lawyer informed as soon as I get any preliminary results. If the results seem to be contrary to the interests of the lawyer's client, the lawyer can quickly end the engagement. This will mean that I will not have to give evidence; and I will not have to disclose to the court the material that I have discovered.

2.3 Obligations to the regulator

If an economist is retained by a business to put a submission to a regulator there are many different forms that this retainer might take. One may:

- write a report that will be handed to the regulator;
- undertake some piece of work that will be incorporated into a submission from the business – but which will not be separately identified although the regulator will know that the economist has been involved; or
- help with the drafting of the report while the participation of the consultant economist is not revealed to the regulator.

I am happy to undertake work in any of these three ways; but in my experience it is best to reach agreement early on which role one is to play.

If one's participation in the submission is not going to be revealed to the regulator, one does not have to worry about the effect of the work on one's reputation with the regulator. However, if one is to be identified with the work – either through direct attribution or because one is to be identified in a general way with the whole submission, one has to be concerned about one's reputation. One always hopes that one's interaction with the regulator is a repeat game. One's ability to make it a repeat game will depend on one's reputation with the regulator: clients will not hire you if they think that you are regarded with suspicion by the regulator. This means that an economist has an obligation to his/her employer or, if he/she is self-employed, to his/her future income. One can best discharge this obligation by operating in accordance with the precepts of the Chief Justice's Practice Direction. One should do this not because one is obliged to by the Chief Justice but because one has regard for one's future income.

In my experience, one is more likely to come under a bit of pressure from a lawyer or a corporate client if one is making a report for a regulator than if one is preparing evidence for a court. If one is preparing a report for a regulator, the lawyer will not feel constrained by the Practice Direction; and the client will be less likely to be reminded by the lawyer of the need for the expert to be independent. Furthermore, if one is subject to pressure, one cannot defend oneself by referring to the Practice Direction.

One tactic that I have found useful in such circumstances is to tackle the lawyer/client with the following two-pronged strategy. First, point out that the argument that it suggested that you should put makes no sense in terms of economics. Secondly, point out that there are some very well informed economists on the staff of the regulator and that it may do the client's case a great deal of harm if they put the regulator offside by proposing arguments that are economic nonsense. In my experience, this two-pronged strategy gets the lawyer/client to back off.

3 Substance of contribution

The substance of our contribution as economists is the logic of economics and econometrics. We have nothing else to offer. This is true, whether one is presenting before a regulator, a tribunal or a court.

But the economics must be presented within the framework of the law. This lesson needs to be learnt by most of the newly minted economics graduates who come to work in our firm. They are well-trained and eager to apply their tools of economic reasoning to solve the problems of the world; and this is wonderful to observe. However, if their work is to find its way into reports for a court or a

regulator it must fit within the framework of the law – because this framework constrains the courts and the regulators.

Maureen Brunt always stressed this to her students. In her collected papers, she added a section of closing reflections that deals with the relationship between law and economics in the study of antitrust. She wrote:

"As to the issue of 'dominance', if either partner is to be regarded as dominant it must be the law. As I wrote in the essay on 'Antitrust in the Courts', the source of the law's power lies in the controlling statute, the court's formulation of rules of liability, its control over practice and procedure, and perhaps most fundamentally its monopoly of enforcement and the implementation of sanctions and remedies. The nub is that antitrust is court-centered."[4]

If economists are experts in the logic of economics and econometrics, what is the role (if any) of economic evidence in proceedings for judicial review of decisions by regulators?

The answer to this question is primarily a matter for the lawyers. An interesting paper by Geoff Airo-Farulla[5] explores the meaning of the requirement of the courts for rationality in decision-making by administrators. The paper takes off from the observation that the courts have increasingly used the term 'rationality' when referring to the standards of good administrative decision-making when reviewed by the courts.

It quotes a decision by French J in *TCN Channel Nine Pty Ltd v Australian Broadcasting Tribunal:*

"[T]here is a pervasive requirement for rationality in the exercise of statutory powers based upon findings of fact and the application of legal principle to those facts …A serious failure of rationality in the decision making process may stigmatise the resultant decision as so unreasonable that it is beyond power. Alternatively, lack of rationality may be reflected in a failure to take into account relevant factors or the taking into account of irrelevant factors. Each of these heads of review seems to collapse into the one requirement namely that administrative decision in the exercise of statutory power should be rationally based."[6]

If irrationality is to be equated with Wednesbury unreasonableness as a standard for judicial review, it would seem that an expert economist would be an ideal person to give evidence in proceedings for judicial review of a decision by an

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[4] Maureen Brunt, *Economic Essays on Australian and New Zealand Competition Law,* Kluwer Law International, 2003, p 366.

[5] Geoff Airo-Farulla, "Rationality and Judicial Review of Administrative Action", *Melbourne University Law Review,* vol 23, 2000, pp 1-32.

[6] (1992) 28 ALD 829, 861, quoted by Airo-Farulla at p 3.

economic regulator. The expert would not evaluate the ultimate decision of the regulator. Rather he/she would evaluate the economic logic on which the decision was based. The role of the economic expert would be somewhat like that of a University Professor marking the term paper of an economics student. Whether the paper passes or fails depends on whether the paper shows a basic understanding of economic logic. If the paper does not show such a basic understanding, it should fail.

The courts do not seem to adopt this approach to the admissibility of expert economic evidence in judicial review cases – particularly when there is a dispute as to the admissibility of that evidence. My first experience of this was the *Seven Cable Television Case.*[7] Foxtel applied for judicial review of a declaration decision of the ACCC. I was retained by solicitors for Foxtel to give my opinion of the process of reasoning in the ACCC's decision. My opinion was not favourable. I wrote a detailed examiner's report pointing to the numerous mistakes of economic logic in the report. This was filed with the Court; and I was called to give evidence. The ACCC argued strenuously for some hours before the Court that it should not read my evidence. Eventually, Wilcox J agreed with the ACCC and I returned to Melbourne having been denied the opportunity to give my evidence.[8] The decision of Wilcox J to reject my evidence at trial was upheld on appeal (per Beaumont, Moore and Gyles JJ).

In contrast to the approach of the ACCC, the Reserve Bank of Australia (RBA) did not fight the admissibility of expert economic evidence in the applications for judicial review of its decisions to designate credit cards and EFTPOS.[9] In both cases, the RBA retained first-class experts and there was a vigorous debate in the court between experts on highly-technical matters over whether the RBA had shown a basic understanding of economic logic in the reasons it gave for these decisions.

In both cases, the judges expressed important reservations about the relevance of much of the expert evidence. Weinberg J's decision in the EFTPOS case acknowledges that some expert evidence was relevant. However, he made it clear that he found much of it unhelpful:

"42. In ordinary circumstances, an application for judicial review, whether under the *ADJR Act* or at common law, is based essentially on the reasons for decision given by the decision maker. It is an unusual feature of this proceeding that each

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[7] *Telstra Corporation Ltd v Seven Cable Television Pty Ltd* [2000] FCA 1160.

[8] This is not the only time my evidence has been found to be inadmissible. The other occasion was the Arnotts case (*TPC v. Arnotts Limited* (unexpurgated version) (1990) ATPR 41-062) when the ACCC again devoted substantial effort to prevent the court from taking my evidence into account.

[9] See *Visa International service Association v Reserve Bank of Australia* [2003] FCA 2003, and *Australian Retailers Association v Reserve Bank of Australia* [2005] FCA 1707 (28 November 2005).

side led a prodigious body of evidence in support of its case. In the *Visa* case a similar approach was taken.

43. It may be accepted that the very nature of the applicants' challenge to the Decision warranted the reception of some such evidence. For example, their contention that the RBA misconstrued the terms "efficient" and "competitive" in *s 8* of the *PSR Act* opened the door to expert economic opinion regarding the meaning of these words, as technical terms of art. Regrettably, the expert evidence was not merely exceedingly detailed, but also highly contentious. Each of the experts was cross-examined at considerable length."

As I understand, the Australian courts have traditionally shown a strong reluctance to condemn as unreasonable the logic of economic regulators. If these decisions are challenged for judicial review, the regulator will adopt one of the two tactics noted above. It will either fight to prevent the evidence being admitted or it will engage its own experts to neutralise the experts retained by the applicants. If the second approach is adopted, the court will be faced with a vigorous debate among experts – one group of which is arguing that the logic of the regulator was hopeless and the other arguing that it was not hopeless. In such circumstances, a court is unlikely to find the economic evidence particularly helpful.

4 Form of presentation

No matter what the forum, the job of the expert is to help the authority to see the truth. But reasonable, well-informed economists may well have different opinions as to where the truth lies. This means that the expert must try to persuade the regulator, tribunal or court to see things the way he/she does. This is acknowledged in the Practice Direction:

"An expert witness does not compromise objectivity by defending, forcefully if necessary, an opinion based on the expert's specialised knowledge which is genuinely held but may do so if the expert is, for example, unwilling to give consideration to alternative factual premises or is unwilling, where appropriate, to acknowledge recognised differences of opinion or approach between experts in the relevant discipline."

Any person who hopes to persuade an authority (regulator, tribunal or judge) to share his/her way of seeing things, must use forms of presentation that the authority finds congenial. Judges are not economists and many are not familiar with mathematical modes of reasoning.[10] Its reliance on mathematical reasoning

[10] There are some notable exceptions. A brilliant performance by a judge in mastering highly technical economic reasoning is the decision by French J in *Australian Gas Light Company v ACCC (no 3)* [2003] FCA 1525.

was one of the reasons why Weinberg J elected to reject the evidence of Professor Farrell in the EFTPOS case:

"If I am wrong in holding that Professor Farrell's evidence was insufficiently relevant to warrant admissibility, I would nonetheless exclude that evidence in the exercise of my discretion. I would do so pursuant to s 135 of the *Evidence Act*, on the basis that, read as a whole, it is confusing. Having attempted, I believe assiduously, to understand the gist of Professor Farrell's evidence, as set out in his various reports, I regret to say that I cannot make a great deal of sense of considerable parts of that evidence.

Two illustrations of the difficulty in comprehending Professor Farrell's evidence will suffice. Under the heading "Strict Allocative Efficiency", at 5 of "Technical Appendix A", Professor Farrell observes:

"For strict allocative efficiency, the cardholder should choose payment system A over B if and only if:

$$b^{A}_{ch} - b^{B}_{ch} \geq \left(RC^{A}_{issuer} + RC^{A}_{acquirer} + RC^{A}_{merchant}\right) - \left(RC^{B}_{issuer} + RC^{B}_{acquirer} + RC^{B}_{merchant}\right)$$

where b^{1}_{ch} represents marginal net cardholders benefits, RC represents marginal resource cost."

I have only the vaguest notion of what this means."[11]

Even if one can find a suitable form in which to present one's argument to the authority, one is still faced with the issue as to how best to expose any flaws there may be in the reasoning by economists retained by the other side. In the case of a regulator, this should not be a problem: the regulator should have the skills in-house to expose any weaknesses in the economic reasoning – whether from economists on the 'other side' or from one's own documents.

In formal proceedings, reports by experts are normally made available to both sides and they can draw the attention of the regulator to any defects. This is not generally the case in applications for informal clearance of mergers before the ACCC – where any submissions and expert reports are normally treated by the ACCC as confidential. As I understand, the reason for this is to encourage parties to participate in the informal process. The obvious disadvantage is that an expert is not always in a position to expose weaknesses in arguments being put by other experts – because one does not know what is being put.

The Tribunal and the Federal Court have developed the hot-tub procedure. One of the merits of this procedure is that experts can more readily expose weaknesses in each other's arguments than can the traditional procedure of cross-examination by counsel. The principal problem with cross-examination by

[11] *Visa International service Association v Reserve Bank of Australia* [2003] FCA 2003, paras 480-482.

counsel is that they are not economists. This means that they are unlikely to be confident in challenging an expert on technical matters.

In my experience, direct questioning of one expert by another can overcome this problem quite readily. It means that counsel loses control of the proceedings; but it does help expose weaknesses quite rapidly. A formal version of this was tried by the Tribunal in the EFTPOS authorisation appeal.[12] Heerey J invited the economists to cross-examine each other in turn. Economist A went first. Economist B could ask questions (uninterrupted) of economist A. Then economist C could ask questions – and so on. Then it was the turn of economist B to face questions, first from A, then from C, then from D and so on.

This whole procedure was over within a couple of hours and I thought it was remarkably successful in exposing differences between experts and defects in the reasoning of experts. Counsel was not excluded from the process completely. They were allowed to conduct their cross-examinations in the usual manner.

[12] Re EFTPOS Interchange Fees Agreement (2004) ATPR 41-999.