Chancery Finds Expert Valuations Are Inadmissible as Hearsay Evidence

The Delaware Court of Chancery issued an important evidentiary ruling in Zohar II 2005-1 Ltd. v. FSAR Holdings, finding that expert valuation reports were inadmissible as hearsay.

By Francis G.X. Pileggi and Alexandra Rogin | October 25, 2017

The expert valuation reports at issue were considered hearsay within hearsay under Delaware Rule of Evidence 805. Importantly, these reports contained expert opinions, which are commonly relied upon by parties. The court noted that when expert opinion is not subject to cross examination Delaware courts are inclined to enforce the general rule against admissibility of hearsay evidence.

The defendants had argued that the reports were admissible under: Rule 801 (d)(2)(E): They qualified as party-opponent admissions, including statements by a co-conspirator during the course and in furtherance of the conspiracy. Rule 803(6): The valuations were records of regularly conducted business activities. Rule 804(b)(3): The valuations contained
statements against interest. Rule 807: The catch-all residual hearsay exception.

The first argument failed because there was no evidence to establish a conspiracy. The court offered guidance in a footnote, explaining that the better argument would have been that the statements within the reports qualified as those made by “a person authorized by [the party] to make a statement concerning the subject” pursuant to Rule 801(d)(2)(C).

The second argument failed because the defendants did not offer any foundation to support their assertion. The court again advised that this flaw could have been avoided had the authors of the documents testified as to the preparation and maintenance of the valuations.

The third argument failed because the defendants did not offer any evidence in support of Rule 804’s prerequisite—that the declarants (the valuation experts) were unavailable for trial. Additionally, there was no evidence to support that at the time the reports were prepared, the experts’ statements were “so far contrary to [their] pecuniary or proprietary interests … that a reasonable person in the declarant’s position would not have made the statement.”

The fourth argument also failed. The court detailed the narrow construction of Rule 807 and acknowledged the risk of its invocation creating a snowball effect that could “swallow the hearsay rule.” Given the complex nature of the expert opinions, which had not been explained or tested through “usual tools available to trial courts as they ferret out evidence in search of the truth,” the expert valuation reports were inadmissible.

The court noted that the defendants might be able to cure their deficiencies at trial, if, for example, proper foundation evidence were presented. Additionally, the valuation reports might still be admissible, not for their truth, but, for example, as impeachment evidence under Rule 607. Spreadsheets of supporting financial data could also be admissible if defendants were first able to lay a proper foundation.
For practitioners who may be many years removed from the bar examination, this ruling highlights the court’s interpretation of multiple key rules regarding hearsay and the admissibility of evidence. Notable for its application to expert opinions and reports, the court also provides guidance on how to make the case for admissibility in accordance with the hearsay exceptions.

Francis G.X. Pileggi is the member-in-charge of the Delaware office of Eckert Seamans Cherin & Mellott. Alexandra Rogin is an associate with the firm. Both practice in the firm’s corporate and commercial litigation group.