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NIIFA OGDEN SIX - A NEW APPROACH

The sixth edition of the Ogden Tables was published in May last year and is likely to have a significant impact on personal injury and clinical negligence claims.

DISCOUNTS FOR CONTINGENCIES OTHER THAN MORTALITY

The most important changes relate to the discounts that apply to contingencies other than mortality. In previous editions the factors affecting the level of discount were the occupation of the claimants, their geographical location and the level of expected future economic activity. The sixth edition reflects the results of research by City, London and Cardiff universities which suggests that the relevant factors are the claimants' levels of education and whether or not, at the time of injury, they were employed or disabled.

The new guidance also recommends a new method of calculation which is intended to replace some of the perceived vagaries of so called "Smith and Manchester Awards." These awards were intended to compensate claimants for the weakening of their competitive position in the open labour market.

In most cases, if the new approach is adopted, then the discounts for contingencies other than mortality will take into account the matters for which the Smith and Manchester Awards were intended to compensate. However, in the writer's opinion, there may still be rare occasions in which Smith and Manchester Awards should still be claimed.

Importantly, there will be both winners and losers under the new approach. Claimants with no residual earning capacity are likely to be worse off because the discounts for contingencies other than mortality are likely to be higher than those applied previously. On the other hand, the winners are likely to be those with some residual earning capacity and even those whose earnings have fallen by little, if anything. This can be illustrated by way of example set out in the box below.

| Facts | | New approach | |
|---|-----------------------------------|--|-----------------------------------|
| Man aged 30 at date of trial | | Net salary before accident | £35,000 |
| Retirement age 65 | | Ogden multiplier for loss of earnings to age 65 for a man aged 30 at date of trial at a discount of 2.5% (taken from table 9 of the sixth edition) | 22.78 |
| No educational qualifications | | Less adjustment for contingencies other than mortality (from Table A for employed able bodied males with no qualifications) | 0.89 |
| Traditional approach | | Adjusted multiplier | $0.89 \times 22.78 = 20.27$ |
| Net salary before accident | £35,000 | Product of multiplier and multiplicand for pre accident earnings | $20.27 \times £35,000 = £709,450$ |
| Net salary after accident | (£10,000) | Net salary after accident | £10,000 |
| Annual loss of earnings | £25,000 | Ogden multiplier for loss of earnings to age 65 for a man aged 30 at date of trial at a discount of 2.5% (taken from table 9 of the sixth edition) | 22.78 |
| Ogden multiplier for loss of earnings to age 65 for a man aged 30 at date trial at a discount of 2.5% (taken from table 9 of the fifth edition) | 22.81 | Less adjustment for contingencies other than mortality (from Table B for employed disabled males with no qualifications) | 0.40 |
| Less adjustment for contingencies other than mortality (from Table A for medium economic activity) | 0.97 | Adjusted multiplier | $0.40 \times 22.78 = 9.11$ |
| Adjusted multiplier | $0.97 \times 22.81 = 22.13$ | Product of multiplier and multiplicand for pre accident earnings | $9.11 \times £10,000 = (£91,100)$ |
| Future loss | $22.13 \times £25,000 = £553,250$ | Total claim | £618,350 |
| Add Smith and Manchester award for weakening of the claimant's competitive position in the open labour market Say | £20,000 | | |
| Total claim | £573,250 | | |

Claim under old approach: £573,250 Claim under new approach: £618,350 Additional claim: £45,100 Increase in claim 8%

MULTIPLIERS IN FATAL ACCIDENT DEPENDENCY CLAIMS

The sixth edition also recognises the fact that the courts have been reluctant to follow the Ogden Committee's recommended methodology in fatal accident cases. Instead, they have used the House of Lords' decision in *Cookson v Knowles* as authority that multipliers should be established from the date of death rather than the date of trial. This can give rise to absurd conclusions which result from the tables being used in an inappropriate way.

New guidance sets out how fatal accident dependency claims should be calculated so as to accord with the *Cookson* and *Knowles* approach but in a way which avoids the problems encountered in the past.

In essence a multiplier is established in respect of the deceased from the date of death from which is deducted the period between the date of death and the date of trial. The multiplier for the dependant is calculated from the date of trial and the calculation of losses based on the lower of the two, in the usual way.

CONCLUSION

In summary, the sixth edition of the Ogden Tables is likely to have a very substantial impact on the calculation of claims.

The Courts are not obliged to follow the guidance set out in the tables but, in the writer's opinion, it would be difficult to justify not doing so, especially because they are not only based on the latest and best statistical information available but have the backing of the government's own actuary.

COMPENSATION FOR TERMINATION OF COMMERCIAL AGENCIES

The recent House of Lords' decision in *Lonsdale v Howard and Hallam Limited* has provided important new guidance on the calculation of compensation payable to commercial agents on the termination of their agencies.

Commercial agents are protected by The Commercial Agents (Council Directive) Regulations 1993 which derive from French jurisprudence which regards a commercial agent as having a right to share in the goodwill of the principal's business which he has helped to create.

The implication is that agent and principal will have co-operated in building up the principal's business, the principal by providing a good product and the agent by his skill and effort in selling it. Consequently, if the agency is terminated and the principal retains the goodwill, the agent ought to be entitled to compensation.

The *Lonsdale* judgement makes it clear that the compensation payable to an agent, on the termination of his agency, should reflect the commercial value that a hypothetical purchaser would have been willing to pay to acquire the right to continue earning commissions by, effectively, stepping into the shoes of the agent whose agency has been terminated.

In France, there is a ready market for commercial agencies and they typically change hands for a figure equal to two years' gross commissions. However no such market exists in the UK.

The force of the *Lonsdale* judgement has made it clear that the application of a rule of thumb (such as that which exists in France) should not be applied to English cases. Instead a formal valuation of the agency is required. Consequently, solicitors advising commercial agents facing termination of their agencies are likely to be criticised if they do not advise their clients to consider obtaining a forensic accountant's independent professional valuation to support any claim for compensation. In the writer's opinion agencies should normally be valued by calculating the likely future income stream of which the agent has been deprived and to apply to this an appropriate multiplier.

The multiplier should reflect:-

- **The commercial strength of the principal;**
- **The terms of the agency;**
- **The existence of the statutory compensation regime; and**
- **The effect on the principal of the future activity of the agent whose agency has been terminated where he too represents competitors of the principal.**

Oddly it was decided in Lonsdale that, in the case of an agent who has more than one agency, his expenses should be fairly attributed to each. The argument that the marginal costs for a particular agency might be very small was rejected. This is difficult to reconcile with the principles of commerciality which lie behind the judgment. The value of an agency to a hypothetical purchaser will be the profit he can generate from it. If he can undertake the agency at no additional cost, then one might have thought that the value of the agency to him would be calculated by deducting only the additional costs of undertaking it rather than an element of the cost that he was already incurring undertaking his existing agencies.

No commercial agent can have only one agency. If he were to do so, then the Inland Revenue would be likely to argue that he was not, in reality, an agent but was, in effect, an employee of the principal. Similarly, most agents with multiple agencies will specialise in complimentary products such that they can visit the same customers and attend the same exhibitions and marketing events whilst promoting many or all of the products they represent.

The option of considering only the marginal cost is no longer open and all the costs of the agent should be reasonably apportioned between his agencies. However, the Lonsdale judgement is silent on what those costs might be. Of particular importance is whether or not they should include the value of the agent's own time.

In summary, therefore, any commercial agent seeking compensation for the termination of his agency, is likely to have to follow the Lonsdale ruling. He will, in even the smallest cases, be likely to have to seek accountancy advice in what is an area now even more fraught with difficulty and ambiguity than previously.

WHEN BENEFIT IS NOT BENEFICIAL

It has recently been reported that the Assets Recovery Agency, which is soon to be abolished, has cost far more to administer than it has managed to collect by confiscating the proceeds of crime. It was launched on a wave of optimism and expected to ensure that criminals would, as a matter of course, face confiscation of their ill gotten gains.

The writer has mentioned in previous articles the fact that the confiscation legislation appears to be somewhat draconian. However, this has never been clearer than in the case of an accountant recently investigated for providing false mortgage references.

In essence, he would falsely certify that an individual was earning more than was in fact the case so as to enable him or her to obtain a mortgage. He charged a few hundred pounds for each mortgage reference letter. However, under the confiscation legislation, the definition of "benefit" is such that if, for example, he charged £500 for a letter that enabled an individual fraudulently to obtain a mortgage of £200,000, then the benefit would be calculated as £200,500. It is this amount that would be sought from him by way of confiscation!

For more information about Confiscation Proceedings including the latest case reports, the writer (as a contributor!) can recommend a useful online resource at www.wikicrimeline.co.uk.

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CREDIT CRUNCH

Most profitable companies are valued using the earnings basis, whereby a multiple is applied to the future maintainable profits of the company. Such multiples are commonly referred to as Price Earnings (P/E) ratios or capitalisation factors.

The recent 'credit crunch', has had severe implications for many organisations, most notably Northern Rock. It has also had an impact upon the P/E ratios of both quoted and privately owned companies.

One of the benchmarks often used by expert accountants when arriving at the appropriate P/E ratio, is the Private Companies Price Index published by BDO Stoy Hayward. During the course of 2004 to late 2006, the Index showed a steady rise in the multiples being applied in the sale of privately owned companies. However, as the markets have been squeezed, so too have the funds available to potential purchasers of these businesses. Therefore, as the demand for privately owned businesses has fallen, it would appear so have the P/E ratios being applied to them.

We have amended a number of their valuation reports recently to reflect both these factors, in order to give the Courts the most up to date picture of the likely value of shares within a privately owned company. These factors will have implications in both matrimonial proceedings and shareholder disputes, together with other areas of litigation that require the valuation of a shareholding.

These factors should not be overlooked as they may have a significant impact upon value.

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