A newsletter from NIFA
APPROVED EXPERT FINANCIAL WITNESSES

NIFA NEWS

ISSUE 20

NIFA IS PLEASED TO WELCOME A NEW MEMBER
Norman Cowan • Wilder Coe • Stevenage

In this issue:

NIFA CREDIT CRUNCH SQUEEZES MULTIPLIERS

NIFA MEMBERS HAVE SEEN A SIGNIFICANT REDUCTION IN MULTIPLIERS APPLIED TO EARNINGS IN CORPORATE TRANSACTIONS THIS YEAR AND WARN THAT BUSINESS VALUATIONS IN DIVORCE AND OTHER LITIGATION PROCEEDINGS ARE LIKELY TO BE CORRESPONDINGLY DEPRESSED.

The credit crunch has severely limited the availability of funding for corporate "Deals" which has, in turn, reduced the price that purchasers are willing or able to pay.

At the moment, the BDO Stoy Hayward's Private Company Price Index for the first quarter of 2008 indicates that, on average, private companies are being sold for 13.2 times their historic after tax profits. We view this figure with a degree of caution. The statistic is based on undisclosed transactions and exceeds the comparable FT index for quoted companies.

In our experience, even substantial and profitable owner managed business are struggling to achieve sale prices based on multipliers of even as much as half this figure unless there are exceptional circumstances or special buyers.

Buyers may be keen to buy and sellers may be keen to sell but, in the absence of bank debt to fund new investments, even the most alluring deals can founder. In the current climate, those advising litigants, especially those in ancillary relief proceedings, on the subject of business valuations, should manage their clients' expectations carefully to avoid any unwelcome surprises.

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MALCOLM FORBES OF FORBES MAGAZINE ONCE FAMOUSLY SAID, "RETIREMENT KILLS MORE PEOPLE THAN HARD WORK EVER DID". BUT SOMEHOW WE DOUBT THAT THE GOVERNMENT'S PLANS TO INCREASE THE STATE RETIREMENT AGE ARE MOTIVATED MERELY BY A WISH TO INCREASE LONGEVITY IN THE POPULATION.

In any event, the changes to state retirement age are easily overlooked but they can have a significant effect on the quantum claims for damages for loss of earnings.

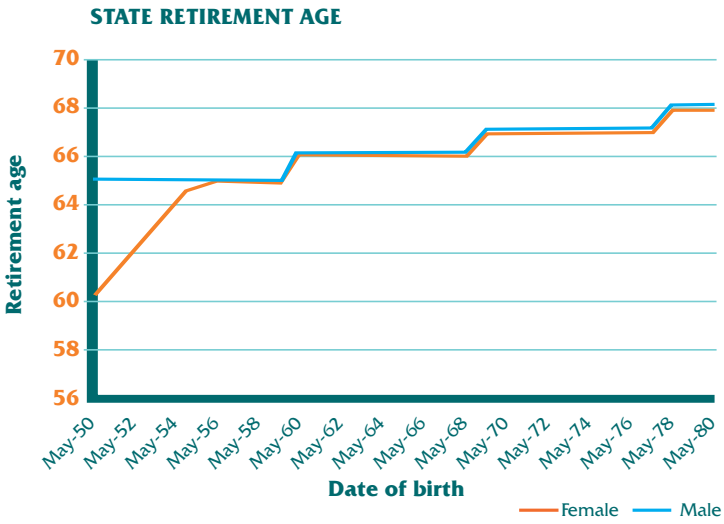
The State Pension age is currently 65 for men and 60 for women born on or before 5 April 1950. The State Pension age for women will increase gradually from 2010, so that by 2020 it will be 65.

The increase in the State Pension age will not affect women born on or before 5 April 1950. Women born between 6 April 1950 and 5 April 1955 (inclusive) will have a State Pension age between 60 and 65. Women born on or after 6 April 1955 and before 6 April 1959 will have a State Pension age of 65.

The state pension age for both men and women is to increase from 65 to 68 between 2024 and 2046, with each change phased in over two consecutive years in each decade. The first increase, from 65 to 66, will be phased in between April 2024 and April 2026; the second, from 66 to 67, will be phased in between April 2034 and April 2036; and the third, from 67 to 68, between April 2044 and April 2046.

The position can be illustrated graphically.

The Ogden tables do not lend themselves easily to the calculation of loss of earnings to or pension from most of these different ages so care needs to be taken to ensure that claimants do not lose out.



INTERESTING TIMES

Last year the House of Lords erased a "*Blot on English common law jurisprudence*" by ruling that compound interest can be payable on damages.

Almost all litigation solicitors are likely to be affected by the ruling in Sempra Metals v Commissioners for the Inland Revenue ([2007] UKHL, 34, [2007] 3 WLR 534). Failing to be aware of the implications could lead to "Easy Wins" being missed, Part 36 offers being miscalculated or, in extreme cases, even leave lawyers open to claims for negligence.

The Sempra case itself involved a claim for restitution. As recently as 1996, the House of Lords had upheld the principle that regardless of equity, compound interest could not be awarded in such cases[1]. However, in Sempra, Lord Nicholls pulled no punches, saying, "*The common law should sanction injustice no longer. The House should recognise the remnant of the restrictive common law exemption for what it is: the unprincipled remnant of an unprincipled rule*".

The effect of the ruling goes much further than restitution claims. It seems that **if it can be adequately pleaded and proved, compound interest can be claimed in every common law claim**.

In many cases it is likely to be open to argument as to what might have been the claimant's true commercial cost of borrowing or what his or her missed investment opportunities.

Interestingly, the poorest claimants are likely to have the highest claims for interest. It is easy to envisage cases in which individuals are suing for, say, breach of contract, having paid for the disputed good or services on a credit card that charged them interest at an APR of 20%-30% or more. In those circumstances, the claim for interest could even exceed the claim for the principal sum.

Happily for forensic accountants, compound interest computations; marginal borrowing costs; and quantification of claims for lost investment opportunity are all grist to the mill for us. Of course, no matter how compelling, in these types of case, accountancy evidence is unlikely to be sufficient on its own. Issues of remoteness and mitigation will inevitably be raised but they, happily, are matters for the lawyers.

[1] Westdeutsche Landesbank Girozentrale v Islington Borough Council [1996] AC 669

LATEST NEWS ON COMMERCIAL AGENCIES

THE COURTS HAVE RECENTLY LOOKED AGAIN AT THE QUESTION OF COMPENSATION PAYABLE ON THE TERMINATION OF COMMERCIAL AGENCIES.

In our previous newsletter we reported on the decision in the House of Lords case of Lonsdale. Further guidance has now been given in the case of Nigel Fryer v Ian Frith Hardware Limited [2008] EWHC 767 (Ch).

In that case the judge followed the ruling in Lonsdale and gave further helpful guidance. In particular he confirmed that a deduction must be made for the notional salary of the commercial agent in the calculation of his net profit.

What was not addressed and is critical to any calculation of compensation is the argument that the choice of multiplier should take into account the existence of the statutory compensation regime. In other words, an hypothetical potential purchaser will pay much more for an agency if he knows that there is a good chance of getting his capital investment back at some time in the future, when the agency terminates.

Suppose, for example, that, by acquiring an agency, the purchaser could expect to augment his earnings by £10,000 per annum over and above a reward for his labour at market rates. It could then be argued that it is entirely reasonable to think he might be willing to pay as much as, say, £100,000 for the chance to increase his earnings in this way but only as long as he were confident of being paid compensation of £100,000 when it terminated at some time in the future. The income in the meantime would be simply a return on a relatively safe investment.

The analogy to this would be the situation faced by a senior associate in a law firm. He may well be willing to stump up £100k to become a partner. By so doing he "unlocks" the prospect of higher future earnings but can also be relatively confident that he will get his £100k back when he retires.

The contrary view is that this approach overvalues the agency because it does not truly reflect its commercial risk. That risk, however, is mitigated by the existence of the statutory compensation regime. The argument then becomes circular.

In the writer's opinion it therefore seems sensible that those acting for claimants seek high multipliers and leave it to the defendants to argue that this is not appropriate.

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CONFISCATION ORDERS DON'T BRING OUT THE BEST IN THE BILL

PERHAPS IT IS THE FACT THAT CHIEF CONSTABLES GET TO KEEP A PROPORTION OF ANY FUNDS RECOVERED UNDER THE CRIMINAL CONFISCATION REGIME FOR THEIR RESPECTIVE POLICE FORCES THAT MAKES SOME MEMBERS OF THE CONSTABULARY PARTICULARLY ZEALOUS IN THE RECOVERY OF THE PROCEEDS OF CRIME.

We are certainly seeing a dramatic increase in the number of forensic accounting instructions related to confiscation orders.

However, we recently heard of a case in which the accused admitted to possession of class A drugs under caution during a taped interview at the police station. In effect he said it was a "fair cop". However the arresting officer then engaged the accused in what seemed to him to be casual conversation, albeit that the tape was still running.

Being off his guard, the defendant volunteered the fact that he had been a drug addict for the past 15 years and used heroin, cocaine and marijuana on a daily basis. On the basis of this evidence an application was made for a confiscation order for £65,700 being the "Benefit" of an estimated £30 a day habit for 365 days a year for the previous six years. The burden of proof then fell to the defendant to prove he had a legitimate source of income with which to meet these estimated expenses!

DISCUSSIONS WITH SINGLE JOINT EXPERTS

Childs v Vernon; Vernon v Butler [2007] EWCA Civ 305

The Court of Appeal has provided a useful reminder of the principles governing conferences with single joint experts. The court held that is was 'wholly improper' for one party to have a discussion with a joint expert in the absence of the other party. The court did concede that it might be possible if the absent party gave its consent, but emphasised that this consent must be fully informed'. In the court's view, an unrepresented party (as was the case here), could not give fully informed consent without knowing its rights.

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