Personal Injury Damages

Income v. Earning Capacity
Labour v. Capital

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Personal Injury Damages

Loss of Earning Capacity - Employees

Loss of Earning Capacity

- Employed
- Self-Employed
- Case Law

Employee

- Plaintiff may not be currently suffering a direct loss (at date of trial or mediation)
- Earning same or more than prior to accident
  - Accommodating employer
  - Change jobs
  - Promotion
  - Working longer hours
- Potentially no past loss
- Future Loss of Competitive Advantage / Loss of Earning Capacity

Employed - Loss of Competitive Advantage

- Causes of potential future losses of income:
  - Longer periods of unemployment
  - Early retirement
  - May limit job options
  - Limit promotion opportunities
  - Working longer hours for same work output
  - May be forced to reduce to part-time work

Employed - Loss of Competitive Advantage – How to Quantify

- Difficult to quantify
  - Unknown if or when changes will occur
  - Based on hypothetical scenarios
- Early retirement can be quantified
- Comparative statistics on earnings and unemployment
  - Disability in Canada: A 2006 Profile (Employment and Social Development Canada – Government of Canada)
  - Participation and Activity Limitation Survey (PALS) 2006 (Statistics Canada)
  - Government Census data and Labour Force Surveys

Employed – Example - Background

- Salaried employee
- Off for a couple of months and then returns to work
- Continues to work in pre-loss job with accommodation from employer
- Has been able to use vacation and sick days to cover any missed time
- Due to annual pay increases, Plaintiff is now making more than at date of loss

Example – Loss of Earning Capacity

- Potential reasons for future loss of earning capacity:
  - If terminated (or employer closes/downsizes), will have more difficulty finding a new job
  - May not be able to work in certain jobs - new employer may not be accommodating and/or job may require physical tasks the Plaintiff cannot perform
  - Injuries may get worse over time, resulting in forced early retirement or reduction to part-time work
  - May not be able to obtain promotions due to work performance or physical limitations
  - Working longer hours to complete the same amount of work

Personal Injury Damages

Loss of Earning Capacity – The Self-Employed

Self-Employed

- Business earning income greater than prior to accident
  - Use of replacement worker
  - Increased demand for the business’ product/service
  - Plaintiff working longer hours
- Business had minimal income prior to accident

Self-Employed – Loss of Earning Capacity

- Could have grown more than actual
- Delayed loss of income
- Loss due to extra time required for tasks
- Value of labour greater than business earnings (both pre- and post-loss)
- Replacement labour cost

Self-Employed – Example - Background

- Self-employed flooring installer
- Started the business the year prior to the accident
- Business earned minimal income prior to the accident
- Plaintiff continued to work, but mostly in supervisory and management functions
- Had to increase use of subcontractors to perform physical work he previously performed himself
- Business had greater income in years after the accident

Example – Loss of Earning Capacity

- Reasons for future loss of earning capacity:
  - Plaintiff is not able to return to the nature and level of work performed prior to the accident
  - Not able to perform the physical work and has had to hire people to do this
  - Plaintiff is less marketable and his career choices have narrowed
  - Ability to earn a livelihood has been compromised
  - Suffered a loss of competitive advantage in the marketplace
  - Replacement labour cost

Loss of Earning Capacity - Tips

- Focus on the facts specific to the case
  - Courts tend to reject scenarios that are not based on actual circumstances of the case
- Prepare multiple scenarios where possible

Personal Injury Damages – The Factors of Production

The Case

- Jordan Ramsey owns a full service restaurant, Heaven’s Kitchen.

- She started the restaurant when she was 22 years old. It has been around for 20 years, and its results have been very stable the past few years.

- She was injured in a car crash; doctors fear she will never be able to work again.

The Case

Income Statement				**Balance sheet**			
Revenue		$ 1,000,000		**Assets**			
				Inventory		$ 30,000	
COGS		300,000		PPE		470,000	
Labour		300,000					
Other Costs		200,000		Total Assets		$ 500,000	
EBITDA		$ 200,000		Liabilities - AP		$ 20,000	
				Equity		$ 480,000	
		Owner does not take salary; she manages the restaurant full-time					

The Issue – Measuring the Loss

- Personal injury damages are normally discounted at a risk-free rate
  - E.g. Ontario Rules of Civil Procedure 53.09

(1) The discount rate to be used in determining the amount of an award in respect of future pecuniary damages, to the extent that it reflects the difference between estimated investment and price inflation rates, is,

(a) for the 15-year period that follows the start of the trial, the greater of,

(i) the average of the value for the last Wednesday in each month of the real rate of interest on long-term Government of Canada real return bonds (Series V80691347, formerly Series V121808 and Series B113911), as published on the Bank of Canada's website for the period starting on March 1 and ending on August 31 in the year before the year in which the trial begins, less ½ per cent and rounded to the nearest 1/10 per cent, and

(ii) zero; and

(b) for any later period covered by the award, 2.5 per cent per year for each year in that period. O. Reg. 488/99, s. 2; O. Reg. 263/03, s. 4 (1); O. Reg. 231/13, s. 9 (1); O. Reg. 383/23, s. 1 (1).

The Issue – Measuring the loss

- Some experts would do as follows:
  - Annual income available to owner: $200,000
  - PV factor for female aged 42 until age 67 – 20.8x
  - Therefore, loss is equal to:

Income to Owner			
Income to Owner		$ 200,000	
Multiple		20.84	
Loss of Income to Owner		$ 4,168,478	**A**

Loss of BV			
Income before Owner		$ 200,000	
FMV of Owner Labour		- 50,000	
Normalized EBITDA		$ 150,000	
EBITDA Multiple		4.5	
Value		$ 675,000	
Discount to V-Date		0.62	
PV of Loss of BV		$ 419,923	**B**

The Problem

- Profits from a closely held corporation are a function of:
  - Return on tangible assets
    - Do these still retain their value? Can they be sold?
  - Return on intangible assets
    - Trademarks, patents
    - Personal goodwill
  - Return on labour
    - Based on statistical data
    - Based on replacement worker

- Only the last of these three is risk-free

A Better Approach

- Total pre-owner income of $200,000 might be said to consist of:
  - Return on tangible assets (assume normal return of 8% based on pre-tax cost of debt) - $38,500
  - Return on labour (based on average wage for restaurant manager) - $40,000
  - Excess returns - $121,500
- Query – what is causing the excess returns? What is the impact of the MVA?
  - Location?
  - Décor?
  - Menu items?
  - Reputation of Jordan Ramsay?

A Better Approach

- If the excess returns are all due to factors unimpacted by the accident, Jordan can simply hire a replacement worker to replace her labour:
  - Loss of income = $45,000 x 20.85 = $937,000
  - Loss of BV = $0
- If the excess returns are due to Jordan's skill as a restaurant manager, then:
  - Loss of income = $161,500 x 20.84 = $3.4M
    - Or is it? Query whether return on personal goodwill should be discounted at risk-free rate.
  - Loss of BV = $0 (since the restaurant can still hire a replacement manager for $45k)
- In some cases, bringing in a replacement manager may lead to negative returns to the restaurant.

Thank you

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