‘EMPLOYMENT BENEFITS’ – DON’T MISS THE PERKS!

BY RICHARD FORMBY FCA MAE

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8 November 2007

Guildhall Chambers, Bristol

Warning:-
Please note that employment benefits are subject to complex tax treatments and tax liabilities can change depending on different circumstances, changes in tax rates and changes in tax legislation. Also, case law and best practice changes. The examples given in this handout are for illustrative purposes only – specialist advice should be sought in individual cases. In addition, certain aspects of these notes reflect the presenter’s views that may not accord with those of another forensic accountant.

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Loss of benefits

Traditional monthly 'net pay' has for many become just one part of remuneration for a significant proportion of the workforce. Employment benefits have become far less of a 'perk' and more of a commonplace part of a remuneration package.

When formulating a personal injury or fatal accident claim it is important to take time to review all aspects of a Claimant's (or Deceased's) remuneration package.

The obvious employment benefits are:-

- Company pension scheme
- Death-in-service cover
- Health Insurance
- Company car or van
- Fuel
- Parking

But now one comes across a much wider range of benefits:-

- Critical Illness/Income Insurance
- Mobile Phone
- Broadband internet @ home
- Computers @ home
- Cheap / soft loan
- Use of sports facilities
- Christmas gifts
- Performance awards

Also encountered, and worth watching for are:-

- Free/subsidised meals
- Child care facilities/vouchers
- Assistance with school fees (e.g. forces, civil service etc.)
- Free or cheap goods and services & deals with other companies

What is the loss?

The loss relating to an employment benefit is generally the cost to the Claimant of replacing the benefit less the costs to the Claimant/employee of the original benefit (the tax charge, if relevant, plus any contribution made by the employee).

What is the tax impact?

Certain benefits provided by an employer may not be taxable on the employee – presently, these include (a single) mobile telephone, parking facilities, broadband connection at home for business use, certain canteen and crèche facilities, pensions, 'soft' loans if less than £5,000 and in certain cases job related accommodation. Death-in-service cover as part of the company pension scheme is also a benefit that avoids tax (although is commonly dealt with as part of pension loss).

Other benefits are quantified and reported to HMRC via form P11D (or form P9D for 'lower paid staff').

Some benefits may be provided by the employer who enters into a PAYE Settlement Agreement with HMRC to pay the associated tax and NIC on behalf of the employee. This is commonly found with Christmas gifts and similar incentive awards paid in kind.

Please note the examples given below are for illustrative purposes only and the tax and NIC treatment of individual benefits can change depending on different circumstances. Specialist advice should be sought in individual cases.

The significance of the potential loss is always relative but they can 'mount-up' here are some illustrations:-

- **Mobile phone**
  There is, presently, no tax charge on the benefit of a mobile phone provided by an employer if certain conditions are met. The Claimant's loss equates to the cost of them providing a replacement phone.

  Example
  Cost to Claimant to replace – say £30 p.m.
  Cost to Claimant of original benefit – nil
  Annual loss = £30 X 12 months = £360 p.a.

- **Life cover**
  Usual to have between 3 and 4 times salary as a 'death-in-service' cover as part of company pension scheme arrangements. Such life cover is not presently a taxable benefit. The cost of replacement cover might be significant if the Claimant's health has been impaired by the accident.

  Example
  Cost to Claimant to replace £75,000 of cover – say £20 p.m.
  Cost to Claimant of original benefit – nil
  Annual loss = £20 X 12 months = £240 p.a.

- **Health Insurance**
  Typical health insurance (e.g. BUPA cover) for an employee aged 35 to 45 might cost an employer, via a group scheme and with reasonable excess, in the region of £300 per annum. Comparable cover taken outside of a group scheme will cost more. In addition, the cost may be increased yet further if there were accident related health impairment. The original benefit would have been shown on the employees P11D and subjected to tax at 22% or 40%. The employees would not have incurred NIC on the benefit.

Example
Assuming basic tax rate & no health issues
Cost to Claimant to replace – say £450 p.a.
Cost to Claimant of original benefit (the cost of the tax) = £300 @ 22% tax = £66
Annual loss = £450 - £66 = £384 p.a.

The company car

The annual loss to a Claimant who has lost the use of a company car as a consequence of an accident is:-

- The tax charge for the company car

  -vs-
- The cost of running a private car

The company car tax system is based on a percentage of the car's List Price graduated according to its $C0_2$ emissions. The range is 35% down to 15% of List Price. (There are certain categories of car that don't fit this system)

The cost of running a private car can be estimated from AA Motoring Costs (see Facts & Figures P/265 or the AA web site at www.theaa.com). They comprise annual standing costs and running costs per mile.

Example - Company Car
Claimant had the use of a Vauxhall Vectra Life 1.8i 16v
List Price - £16,300
CO_2 rating -173g/km.
The Claimant's marginal tax rate was 22% and they do 15,000 private miles a year.

Annual loss to Claimant is estimated at £4,120, based on:-

- **Tax charge was £753 p.a.** The 'benefit %' can be identified (from Fact & Figures P/270) as 21% giving a taxable benefit of £16,300 X 21% = £3,423 and resultant tax as £3,423 X 22% = £753.06

- **The cost of providing a private vehicle £4,873 p.a.** The standing charge for a comparable priced vehicle (Facts & Figures P/265) is £3,541. The running costs for the same vehicle are £1,332 (see table below) giving a total annual cost of £4,873.

Running costs For 15,000 private miles	Pence
Tyres	1.40
Service	3.98
Parts	1.70
Parking & Tolls	1.80
Total pence per mile	8.88
	times
Private mileage	15,000
Running cost of private mileage	£1,332

Fuel benefit

Where an employer provides a car and free fuel to an employee for private mileage then the taxable benefit needs to be calculated. To escape the fuel charge the employee must reimburse the whole of the cost of private fuel (a contribution towards the fuel cost does not result in a proportionate reduction).

The present car fuel benefit is set at £14,400 and the individual's benefit is calculated as the same percentage used to calculate the benefit of use of the car.

Example – Fuel Benefit

Using the example (above) of the Vauxhall Vectra, the 'benefit %' was 21% so the taxable benefit is £14,400 (the set amount) times 21% = £ 3,024.

The cost to the Claimant of the private fuel is the tax charge i.e. £3,024 X 22% = £665

The replacement cost to the Claimant of the free private fuel can be identified as estimated private mileage (say 15,000 miles) times fuel rate (say 12 pence per mile – per Facts & Figures P/265 plus allowance for fuel price increases) = £1,800

Resultant annual loss £1,135

Share Options

The issues involved with share option schemes are complex by their nature, a loss with a share option will be about lost opportunity. As a consequence it is probably appropriate to seek exert advice.

Presently there are four sets of provisions designed to give favourable tax treatment to schemes to acquire shares if the necessary conditions are satisfied, these 'approved schemes' are:-

- SAYE linked share option schemes
- Company share option plans
- Share incentive plans
- Enterprise management incentive share option schemes

Share options and incentive schemes are far more common in the workplace than they were and they don't just relate to managers and directors.

A quick internet search of 'staff share options' revealed:-

- Argos staff share in £13 million bonanza
- HBOS staff share in £210 million windfall
- M&S staff share in £40 million share scheme
- Tesco Staff share in £148 million payout

These were SAYE type schemes that must be available to all employees and so many of those benefiting were 'ordinary staff and workers'. Such schemes are reasonably common in larger, quoted, companies.

A Claimant who has participated in share save schemes and has had to cease or has lost their job and access to future schemes has the scope for a loss.

The key features of a typical SAYE linked scheme are:-

- Option to acquire shares after 3, 5 or 7 years but at 'today's' price
- Start saving monthly now – receive a tax-free bonus added to the savings
- If the share price in 3, 5 or 7 years time is higher than today's price – exercise the right to acquire the shares out of the monthly savings
- Sell any shares acquired or elect to hold and sell later
- If, after the expiry of 3 or 5 years, the share price is below option price – continue saving for further 2 years, receive another saving bonus and exercise option or eventually merely take the 'savings pot'

Benefits to forget?

There are some 'employment perks' that might not be worth claiming – for example:

- Employers may give employees lunch vouchers tax free up to the value of 15 pence per day
- Employees can benefit from a tax-free breakfast if they cycle to work on designated 'cycle to work' days
- Further good news for cyclists – they can claim 20p per mile tax free for business use of their bicycle

One to think about is 'family income cover'. This is where the employer provides insurance cover for an employee – this is to provide income in the event of their illness and inability to work. It's a benefit and it may be a lost benefit but it may be illogical to include it in a claim because the basis of the claim for lost earnings is that 'but for the accident' they would have been working and earning!

Pension Loss

What is a Pension scheme – it's a scheme designed to provide an income after retirement. This may be via the state, the employer or the individual. Approved pension schemes have tax free benefits, contributions and growth of funds, to encourage saving. But people can make informal arrangements – for example a buy-to-let investment taken out with the purpose of funding retirement.

In the context of this talk on Employment Benefits and Perks we are looking more at **Occupational Pension Schemes** of which there are two types of scheme – Defined Benefit or Defined Contribution.

The defined benefits schemes are also known as **Final Salary Schemes** because these are based on Pensionable Service and Final Pensionable Salary. We all know people in such scheme – e.g. Teachers, NHS workers, Civil Services, Local Government, and (now typically very) large private sector companies.

The defined contribution schemes are also known as **Money Purchase Schemes**. The scheme rules will set our how much the employer contributes to the scheme and the employee will have the option to vary their contributions.

Final Salary schemes are become harder to find. Many in the private sector are closed to new members, some are 'morphing' into money purchase schemes while others are varying the age from which a pension becomes payable – e.g. The Teachers Pension Fund changed its Normal Pension Age from 60 to 65 for those joining the scheme for the first time after 1 January 2007.

Money purchase schemes are becoming the norm – because employers cannot fund Final Salary Schemes. The employers are content to make their contribution for as long as the employee remains in service at which point the responsibility and financial obligation ends.

When acting for Claimants that enjoy/enjoyed membership of their employer's Final Salary Scheme it is wise to do a quick check (either via an internet search, the employer's HR dept. or via the pension scheme trustees) to see if there have been recent changes to the pension scheme, or if changes are afoot. Whist you need not adopt assumptions that will not benefit your client you will want to be up-to-date with changes and alert to counter-arguments from Defendants.

With any pension loss remember:-

- Ignore inflation
- Take account of real prospects of future promotion, ensuring that salary rates 'fit with' the claim for lost earnings

Money Purchase Pension Schemes

In a money purchase scheme the employee and employer each make contributions. The eventual pension is dependant upon the contributions made, the performance of the fund, the management charges of the fund and the resultant annuity rate on retirement!

Attempts to project fund growth and the eventual pension on retirement are generally not now accepted as an appropriate means of quantifying potential pension loss. Apart from the obvious high degree of speculation, concerning so many aspects of the pension, there is the logical argument that will be deployed that the Courts Risk Free Discount Rate (currently 2.5% p.a.) is the growth rate that the Court will recognise – hence no loss can result!

In recent years there have been two important changes to pensions:-

- From April 2001 we have stakeholder pensions. These enable individuals to make Gross Pension Contributions to a limit of £3,600 per annum (equivalent to £300 per week!).
- From April 2006 the minimum allowable pension contribution is £3,600 per annum and the maximum is the lower of a scheme member's annual earnings or £215,000 (for the tax year 2006/7).

The important implication of the above changes is that many personal injury Claimants will have the opportunity to mitigate any potential loss arising from their lost investment of pension contributions out of lost earnings by make appropriate pension contributions out of their award for special damages (i.e. the lost earnings they are awarded).

The probable loss arising where there is a Money Purchase pension scheme will arise in respect of the loss of the Employer's Contributions to the scheme.

Kemp (11-004) proposes that one approaches the claim by identifying the annual contribution the employer would have made and then applying the appropriate net earnings multiplier selected from the appropriate Ogden Table.

Example – Defined Contribution Scheme
Male Claimant aged 48 at injury and 50 at trial. But for accident would have earned £20,000 p.a. gross from aged 48 to retirement at age 60. Employer contributed 6% to Money Purchase pension scheme.

Employers annual pension contribution £1,200
Ogden Table 7 – (Males) Multiplier for loss to pension age 60 – aged 50 @ Trial = 8.66 times
Lost benefit of employer's pension contributions = £1,200 x 8.66 times = £10,392 plus pre-trial lost contributions of £2,400 (£1,200 X 2 years) giving a total of £ 12,792

(Note- It is arguable that one could uplift/enhance the pre-trial contributions, say by a factor of 2.5% p.a.)

The above approach treats the employer's pension contribution as if it were real earnings. In my view it is arguable that a more suitable measure of the benefit that has been lost is an investment fund (or capital asset) at retirement. An alternative approach to valuing the benefit, that acknowledges the Claimant sees no benefit until normal retirement, is to multiply the prospective annual pension contribution from the employer by the number of years to retirement and then discount this lump sum back to the trial date.

Example – Defined Contribution Scheme, alternative approach
Again, male Claimant aged 48 at injury and 50 at trial. But for accident would have earned £20,000 p.a. gross and have retired at age 60. Employer contributed 6% to Money Purchase pension scheme.

Lost pension fund value of employer's pension contribution is 12 years at £1,200 p.a. = £14,400. Discount factor for 10 years from age 60 to age 50 at trial (using Ogden table 27 – discounting factors for term certain) = 0.7812.

Adjust for Mortality based on English Life Tables
Age 50 population remaining 94,946.2
Age 60 population remaining 89,582.7
Mortality factor = 1- (94,946.2 – 89,582.7) / 94,946.2 = 0.9435

Hence mortality adjusted discount factor for the period of 10 years = 0.7812 X 0.9435 = 0.737

Giving a total loss of (£14,400 X 0.737) = £10,613

In either of the above examples one would need to make a further adjustment for contingencies other than mortality along the lines as advised by Explanatory Notes Section B, Ogden Tables 6th Edition.

In addition, whilst I have not yet seen it advanced, I can see the grounds for an argument that there is potentially a further deduction to be made because the bulk of any benefit eventually derived by the Claimant (i.e. the pension) will be taxable in their hands – hence a potential deduction of say 22% (i.e. basic rate tax) on a portion of the capital sum.

Final Salary Pension Schemes

(Notes:-

1 - A Claimant whose employment brings with it the benefit of a final salary pension may well have a significant pension loss and when formulating this aspect of their claim for lost pension it is probably worth seeking appropriate professional advice from an early stage

2- There are two approaches that can be used to quantify a pension loss on a final salary pension scheme –namely 'Auty' and 'Wells/Ogden Tables'. In practical terms such pension losses are worked using the latter, and so the examples given reflex the Ogden Tables approach to pension loss

3- For an illustration of how the 'Auty' and 'Wells/Ogden Tables' produce different results see page 35 of Facts & Figures 2007/8)

In a Final Salary (or Defined Benefits) pension scheme again the employee and employer each make contributions but in these schemes the eventual pension and benefits are pre-determined via the scheme rules.

Typically, the pension is a function of Pensionable Salary and either 60ths or 80ths of Pensionable Service. (Note - The Services use the 'Band of Brothers' concept where one has Pensionable Service and Rank on Leaving).

Usually a summary of the scheme rules can be obtained as a pdf file via the internet.

Losses will either arise because the Claimant will have a shortfall in pensionable salary (e.g. they will not now get a promotion) or a shortfall in pensionable service (e.g. they will not work as long with that employer). The approach is the same – i.e. identify/compare the 'expected' and 'but for' salary/service and hence the lost pension & lump sum.

Having identified the lost annual pension one then applies a suitable multiplier derived from the Loss of Pension Ogden tables 15 to 26.

The lost tax-free lump sum element of the pension will need to be discounted from retirement to trial using a mathematical discount factor derived from Ogden table 27. This will need to be adjusted for mortality – using English Life Tables.

Example – Final Salary Scheme
Female Claimant aged 50 at trial, educated to degree level. But for accident has lost 10 years of pensionable service however their pensionable salary remains the same at £25,000 per annum. She is in her employer's 60ths final salary scheme that gives a three times pension lump sum on retirement. She is not expected to get awarded an ill-health pension.

Annual pension loss, gross = £25,000 X 10 X 1/60ths = £4,166 p.a.
Lost Lump sum = £4,166 X 3 = £12,498
Assume marginal tax in retirement at basic rate of 22%
Annual net pension loss = £3,249 p.a.
Pension multiplier @ 2.5 % p.a. per Table 20 = 14.64 times

Table 27 discount factor for term certain of 10 years @ 2.5% p.a. = 0.7812
Adjust for Mortality based on English Life Tables
Age 50 population remaining 96,857.4
Age 60 population remaining 93,272.8
Mortality factor = 1- (96,857.4-93,272.8)/96,857.4 = 0.963
Hence mortality adjusted discount factor for a period of 10 years = 0.7812 X 0.963 = 0.752

Loss of Net Annual Pension = £3,249 X 14.64 = £47,565 *

Loss of Lump Sum = £12,498 X 0.752 = £9,398 *

* Note - in the above example there needs to be further adjustment for contingencies other than mortality in accordance with Explanatory Notes Section B to the Ogden Tables 6th edition. This will need to take into account any doubts about future pension rights and/or the ability of the fund to pay the pension rights. Also, there needs to be consideration of whether the Claimant may change their job to one with comparable pension rights.

Ill-health Pension

If the Claimant is in receipt of an ill-health/incapacity or disability pension from their Occupational Pension scheme then the pension payments under that scheme are not recognised for pension loss purposes until the intended retirement age, after which credit should be given for them against any pension loss.

Any tax-free lump sum awarded as part of an ill-health pension will fall to be treated as partly relating to the ill-health (and so ignored) and partly as an acceleration of the pension lump sum (as so treated as a credit against the lump sum element of the pension loss). The apportionment is in accordance with the Longden case and that of London Ambulance Service NHS Trust v Swain (– see Kemp 11-041 and 11-049)

Widow's Pension

Where the Claimant's spouse/civil-partner has a life expectancy greater than that of the Claimant and there are provisions in the Occupation Pension scheme for a 'widow's pension' payable on the Claimant's death then there is potentially a further loss to be quantified. This can be done relatively simply using the Ogden Tables using the 'life-time' tables 1 and 2.

Example
At Trial Claimant (husband) aged 60 and their wife is aged 50.

Multiplier for pecuniary loss for life – male aged 60 at trial		17.30
Multiplier for pecuniary loss for life – female aged 50 at trial		23.37
	Difference	6.07 times

Mitigation of Pension Loss

Those advising Claimants need to be aware of the potential arguments for mitigation of pension loss.

For example an argument may be advanced that a teacher might be unable to teach but might get a job in administration in local or central government – hence prompting comparison of not overly dissimilar Final Salary Pension Schemes.

Alternatively, it may be argued that the Claimant could find alternative employment that brings the benefit of a Money Purchase Pension Scheme into which the employer will contribute, hence prompting the calculation of the value of the benefit that the alternative employer will contribute.

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8 November 2007

PERSONAL INJURY
PENSION LOSS INFORMATION CHECKLIST

For members of Defined Contribution or Defined Benefits Company Schemes

a. Pleadings ☐

b. Date of birth of Claimant ☐

c. Details of potential and actual **gross** earnings at the date of the trial (from loss of earnings comp) ☐

d. Details of potential future **gross** earnings at date of retirement (from loss of earnings comp) ☐

e. Latest copy (pdf file) of Pension scheme 'handbook' and/or policy schedule ☐

f. Intended retirement age ☐

g. Date Claimant joined scheme ☐

h. Date of birth of spouse/civil partner ☐

i. Claimant's witness statement ☐

j. Most recent Benefits Statement from Pension Scheme ☐

k. Initial Benefits Statement provided when the pension started to be paid on early retirement - if relevant ☐

l. Details of any early retirement pension/lump sums received and the dates they were received ☐

m. Details of any current ill-health pension ☐

n. Details of commutation factors for lump sum at normal retirement and early retirement ☐

Employers contributions

o. Details of contributions paid historically by the employee into the scheme - amounts paid, frequency of the payments and whether the company was bound by any contractual obligations to pay contributions ☐

p. Details of any likely changes in the amount and timing of employers' contributions ☐

Employee contributions

q. Details of contribution paid historically by the employee into the scheme – amounts paid and frequency of the payments ☐

r. Any evidence relating to the intended level of contributions if the accident had not occurred ☐

Also, for Personal Pension and Stakeholder Schemes or where Additional Voluntary Contributions being made

s. Tax returns and assessments for the period from 3 years pre accident to current date ☐

t. Most recent Personal Benefits Statement from Pension Scheme ☐

(Monahans, Nov 07)

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Richard F. Formby FCA MAE

Richard Formby is a Chartered Accountant, a Fellow of the Institute of Chartered Accountants in England and Wales and a partner in Monahans.

He has more than 15 years experience of undertaking financial investigations, forensic accounting and expert witness work and I have been a practising member of the Academy of Experts since 1995.

In 1993, having worked in Corporate Finance and Financial Investigations with a Big Six accountancy firm, Richard launched a litigation support service for Monahans, since when he has specialised in forensic accounting and expert witness work.

Richard has been instructed as an Expert Witness, or Expert Adviser, in more than 500 cases including: -

- PI earnings and dependency loss reports in respect of claims involving a broad variety of employed individuals and businesses - frequently situations where the relevant business was in a start-up, growth or decline phase
- Commercial disputes and reports on consequential loss arising from a variety of 'events' such as business interruption and professional negligence (of accountants and lawyers)
- Shareholder and partnership disputes – share/business valuations and statements of account
- Investigation, examination and reporting in matters of prosecution for theft and false accounting. I have been instructed in fraud cases prosecuted by the Dti and HM Revenue & Customs
- 'Other matters' include - pension loss, employment benefit loss claims / financial aspects of matrimonial settlements / disputed estate accounts / warranty claims

In broad terms, Richard has received instructions in equal numbers on behalf of Claimants as Defendants and has increasingly taken instructions as Single Joint Expert Witness - such that these now form the majority of his witness appointments, certainly in personal injury cases.

Further information on our forensic services can be located at
http://www.monahans.co.uk/web/services-accounting.asp

Monahans is a leading independent firm of Chartered Accountants and Independent Financial Advisers based in the South West. We provide a complete range of services to a client base of in excess of 11,000 clients, from 5 offices. The practice has 20 partners and directors and some 160 staff serving a "general" client base as well as those requiring more specialist services such as schools, charities and regulated financial businesses. We also provide Insolvency, Corporate Finance and IT consultancy.

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