Back pay and front pay calculations in employment termination cases

Most plaintiffs in employment termination cases will ultimately become re-employed. However, for some plaintiffs, the termination of their employment produces significant economic damage to their earnings, retirement pension, and fringe benefits. For other plaintiffs, an employment termination causes little to no measurable economic harm. The individual plaintiff’s efforts and ability to regain comparable replacement employment is often the key difference between the two types of plaintiffs.

Explore the process of accounting for re-employment and mitgation efforts.

The goal of this article is to provide a conceptual and practical introduction to the factors that comprise a standard economic damage model in an employment termination case. We briefly examine the economic factors and assumptions that comprise an economic damages model in an employment termination case and also provide a discussion of the valuation of employee fringe benefits and employee stock option valuations.

The economic damage model in an employment termination case

A typical economic damage analysis of the plaintiff’s lost earnings in an employment termination case involves three main pieces. The first part of the economic analysis involves determining the earnings, fringe benefits, and retirement income that the terminated employee would have received had he or she not been terminated by the defendant. The actual determination of the projected non-termination earnings, or what is frequently referred to 'butfor earnings', is made by examining factors such as the person’s earnings history, level of educational attainment, the labor market potential of similarly situated persons, and employer specific factors.

The second phase of the calculation involves determining the amount of income that the person can now expect to earn in their current or expected replacement employment. Similar to but-for earnings calculations, factors such as the past earnings and the plaintiff’s labor market potential are considered when calculating the expected earnings of the plaintiff.

The third portion of the economic damage calculation generally involves determining the present value of any future economic losses. Conceptually, the present value calculation involves determining how much money would have to be deposited in a relatively safe investment today to compensate the plaintiff for the dollar income losses that the plaintiff is expected to experience over the relevant portions of the person’s work life. The amount to be deposited in a safe investment, such as a U.S. treasury security, is called the present value of the future stream of income.

The underlying premise in the present value calculation is that a dollar received tomorrow is worth less than a dollar received today, because a dollar received today can be invested or deposited in a bank account that will earn interest, until the time the money is needed. To calculate the present day value of the plaintiff’s economic damages, the economist uses actuarial tables, work life tables, interest rate data and relevant tax tables.

Questions or comments

Dwight Steward, Ph.D.
Economist and Director

dsteward@employstats.com
www.employstats.com