Benefits of Small-Dollar Structured Settlements

By Patrick C. Farber and Patrick E. Stockalper

An individual is injured in a car accident and both defense and plaintiff attorneys agree to a $45,000 settlement. Instead of a lump sum payout, a structured settlement is put in place that will pay the settlement over a set period. Structured settlements for large-dollar claims are commonplace, but surprisingly, so are structures for settlements under $200,000.

During the first three quarters of 2011, 21,846 cases were structured, totaling approximately $3.633 billion in annuity premiums. The average case size was about $166,000. These results are based on figures released independently by 11 life insurance companies that issue structured settlement annuities.

Over the past 20 years, more than 50 percent of the structured settlements facilitated by Ringler Associates, a national structured settlements brokerage firm, were less than $50,000. Another approximately 17 percent were between $50,000 and $100,000. These figures are typical of most annuity brokerage firms.

In most cases, neither plaintiff or defense want to see cases go to trial, particularly with small cases where small-dollar structured settlements makes more financial sense than a protracted, unpredictable jury trial. If defense counsel can highlight the advantages of structured settlement benefits to the plaintiff, these cases are more likely to be resolved in the client's best interest.

Tax Advantages

Although smaller annuities are more difficult to justify today because of historically low interest rates, plaintiffs are seeing them as a way to bolster their retirement. Many have had their retirement savings take a beating over the last 10 years. Small annuities can subsidize retirement savings--even with today's low interest rates. The money accrues tax-free and plaintiffs have the peace of mind of knowing they will have these additional funds when they retire.

Small settlements can be structured so they combine a lump sum payout to pay for immediate needs and an annuity for possible expenses down the road. Let's say a worker injured his hand at his job and received a $60,000 settlement. He can go back to work, but only part time while receiving medical treatment. It is determined that it will take six to eight months of physical therapy for his hand to improve so he can resume working fulltime. A settlement is reached in which he receives a $40,000 lump sum at the time of settlement to cover medical costs and living expenses while he is working part time. The remaining $20,000 will or can be paid out in future years for use if additional surgery is needed. If the injured party finds that surgery is not required, the money is still received tax-free.

Another structured settlement advantage is that the funds cannot be spent quickly by the injured party (as can be the case with a lump sum payout) so there is the

continued on page 26

opportunity for financial management and tax planning. Guaranteed, scheduled payouts are not subject to market whims or economic calamities. Funds are placed in AAA rated bonds and Treasury securities by the life insurance carrier. For plaintiffs who can easily succumb to demands from friends and family for cash, or from well meaning individuals with the latest can't miss investments, a structured settlement is the protective answer.

Protecting Medi-Cal and Medicare Benefits

Cases involving injured parties who are eligible or soon-to-become eligible for Medi-Cal can use a special needs trust (SNT) annuity to protect their government benefits while still enabling them to collect tax-free settlement payouts. Individuals who are eligible for Medi-Cal and receive a litigation recovery will lose Medi-Cal coverage until the litigation recovery's balance is below $2,000 for an individual or $3,000 for a couple (the resource limits for Medi-Cal). The most common solution to protect Medi-Cal government benefits and settlement proceeds is to place the litigation settlement into a qualifying first party SNT – either an individual SNT or a pooled SNT with money paid to the injured party from the trust.

Much like an SNT used to preserve a plaintiff's eligibility for Medi-Cal, a Medicare Set Aside Arrangement (MSA) is used to preserve a plaintiff's future eligibility for Medicare. For example, a 35-year-old male slips and falls at a grocery store and injures his back resulting in multiple surgeries including future surgeries. He sues the grocery chain and the case settles for $230,000. An MSA would be created for a portion of the settlement to pay for future medical costs related to the injury. Why? In cases that involve a claim for future medical costs resulting from an injury, the plaintiff is required to use settlement funds allocated for future injury-related medical costs first to pay for the medical care. Until that allocated amount is spent, Medicare will not cover the plaintiff for treatment related to those injuries involved in the settlement.

In the above example, the MSA could be set up to receive $7,500 in cash and $2,500 a year for 20 years to pay for future back treatments. An annuity would cover the $2,500 a year payments. The MSA's present value would actually be $30,000, but the annuity could be purchased for as little as $19,500 for a savings to the defendant of $10,500.

Small Structures and Minors

The majority of smaller structured settlements are for minors. In fact, when minors are involved, judges often require that settlements be structured before approval regardless of the settlement amount.

With structures, parents can ensure that their children are unable to access the funds until they turn 18 or age of majority. They

continued on page 27

Structured Settlements – continued from page 26

also give parents a chance to plan financially for their child's college years and beyond. In the case of young children, settlements of as little as $5,000 or $10,000 can be structured so the money is available in later years. Be aware, however, that some life insurance companies charge "small case fees" if the structured amount is very small. These fees eat up a large percentage of the settlement.

The negative consequences of an older child receiving a lump sum injury settlement as the child nears college age are significant. He or she may not be eligible for state grants and low interest loans because the worse off the financial situation a young person is in when applying for financial aid, the better chance for qualifying for these grants and loans.

If an older child nearing college age receives a lump sum payout, say for $50,000, the income would be counted against the child when seeking to qualify for college financial aid. Instead, if structured, the family could decide on a minimum payment per year for incidentals at school and wait until the child graduates to receive the remainder of the settlement. This could be used to pay off low interest college loans that are required to be paid after graduation. Here, not only do the parents see tax savings, but also have the opportunity to have their child qualify for grants and low-interest loans that would not be available if the settlement had been paid in a lump sum prior to the child's entering college.

The Big Picture on Small Structures

Structured settlement annuities help smooth out investment ups and downs for the injured party. The regular income that even a small annuity brings can be used to supplement money from other sources, pay for everyday living expenses or to see the injured party through until recovery.

For the defense, expenses associated with small claim payments are eliminated with structured settlements since the payment obligation and all liability are transferred to the insurance company managing the annuity. Defendants can close the books on these cases as soon as the settlement papers are signed.

Still, the results of a 2007 survey by the National Structured Settlement Trade Association (NSSTA) of attorneys involved in structured settlements estimated that only 7 percent of all personal injury settlements between $75,000 and $100,000 were structured, even though 95 percent of the attorneys surveyed said they were proponents of structured settlements. This means many smaller settlements that can be structured are still being handed out in lump sums.

Ultimately, the amount of the structured settlement is not as critical as is creating a settlement that meets the needs of the injured party. An annuity paid over a set number of years offering guaranteed tax-free income can be an attractive alternative to low interest bearing bank accounts or higher yielding, but riskier investments.

Patrick C. Farber *is a structured settlements broker in California. He specializes in settling medical malpractice, physical injury, non-physical injury, product liability, workers' compensation, mass torts, punitive damages, employment and elder abuse cases with structured settlements in court hearings, arbitrations and settlement conferences. 800-734-3910,* pat@patrickfarber.com.

Patrick E. Stockalper *is a partner with the firm of Reback McAndrews Kjar Warford & Stockalper and specializes in the areas of medical/dental/professional liabiltiy defense and personal injury defense. Mr. Stockalper, an ASCDC Board of Directors member, is the 2009-2010 President of the Litigation Counsel of America.*