Don't Overlook the Structured Settlement

by Wm. T. (Bill) Robinson III

Given the continuing problem of escalating trial verdicts, defense attorneys and their clients may be more inclined, as never before, to avoid trial in personal injury lawsuits. This is particularly true in mass tort litigation and in cases involving a highly sympathetic claimant—a brain damaged child, for example.

So settlement is often more appealing than trial. But how can the defense attorney achieve the best settlement possible for the client?

There's no one answer, no pat solution that fits every case. However, after well over 20 years in defense work, I am convinced that a crucial part of the solution is the more frequent and more strategic use of structured settlements.

In recent years, structured settlements have become an increasingly effective way to settle difficult physical injury claims. They are now utilized by attorneys representing all sorts of clients, including such prominent plaintiffs' attorneys as Philip H. Corboy in Chicago and Joseph Jamail in Houston. Structured settlements have also won praise from such diverse groups as insurance associations, advocates for the disabled, consumer groups, and the U.S. Treasury Department.

Yet some defense attorneys inexplicably remain hesitant to use structured settlements. Many do not fully realize what makes them attractive to the plaintiff. Others may not understand the financial implications. Regardless, defense attorneys will benefit their clients (and hence their own practices) by aggressively incorporating the structured settlement option into their negotiating strategy.

Background

The first structured settlements appeared in the early 1970s, as a means of resolving birth defect cases involving thalidomide. They did not attract widespread use until 1983, when President Reagan and a bipartisan coalition in Congress agreed on legislation (P.L. 97-473) to formalize structured settlements' benefits in federal law.

Under the 1983 act, Congress approved specific tax rules to encourage the use of structured settlements to resolve physical injury actions. First, Section 104(a)(2) of the Internal Revenue Code was amended to clarify that the full amount of a structured settlement's periodic payments constitutes damages which are received by the victim free of any federal tax liability. (By contrast, the investment earnings on a lump sum are generally taxable.)

Second, Congress adopted IRC Section 130 to facilitate secure, long-term funding arrangements, funded by annuity contracts or Treasury securities, for tort victims needing long-term care and support. Since then, the public policy benefits have become so clear and advantageous that in 1997 President Clinton and a bipartisan Congressional coalition agreed to expand the use of structures in workers' compensation cases.

Advantages of Structured Settlements

At its core, the structured settlement benefits the plaintiff, who receives both a guaranteed income stream and tax-free payments—advantages not available if he or she takes a lump sum cash payment. The plaintiff does not "own" the annuity that funds the payments. By federal law, that annuity must be held by the defendant or a third-party assignee. In that way, the plaintiff (or those who would otherwise take advantage of the plaintiff's settlement proceeds) will not be able to dissipate the settlement prematurely. Indeed, federal law is quite explicit that, once a plaintiff agrees to a settlement, he or she may not "increase, decrease, accelerate or defer" the payments. IRC §130(c)(2)(B).

Though the law focuses on the benefits to the plaintiff, there's an often overlooked implication for the defense, says Joe Costello, a longtime settlement broker at EPS Settlements, and President of the National Structured Settlements Trade Association (www.NSSTA.com). "Congress in effect codified a proven way for the defense and plaintiff to agree on a settlement without a jury trial and without a cash settlement," says Costello. "Jury trials are inherently risky for both sides. Structures reduce that risk and increase certainty."

For the defense bar, there is another important consideration. Offering a structured settlement helps focus both sides on future payments for the plaintiff's basic living needs, medical needs, and lost wages. This often helps inch both sides toward a mutually acceptable closure. As Costello notes, "Negotiations are usually not creative. If I'm at $300,000 and you're at $500,000, we might compromise at $400,000. But is that sufficient for the plaintiff's needs? Once you bring in a structured settlement, you'll do things based on needs."

The tremendous tax advantages to the plaintiff that Congress created to advance the use of structures—tax advantages not available if the plaintiff takes a lump sum settlement—can help resolve difficult cases. Structures can create a "win-win" situation for both sides.

Using Structures: A Primer

Some defense attorneys may shy away from structured settlements, because they are either unfamiliar with the process, or suspicious about bringing another party, such as a settlement broker, to the negotiating table. Carefully selecting a highly qualified professional structured settlement consultant should allay these concerns.

The process for bringing structures into pre-trial negotiations is challenging. Claims representatives will identify open cases in which a structure seems appropriate, and then bring in an approved structured settlement broker. From there, the focus should be on the plaintiff: How to make him or her whole? How to replicate lost earnings? Future medical and living needs?

Information is crucial. "It's very important for the structured settlement broker to gather as much information as possible about needs and objectives of claimants prior to preparing an offer," advises Chuck Harlan, President of Structured Settlements Financial Associates in Baltimore. "Where possible, the broker should really meet with the claimant."

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The nature of the settlement talks should also change. "In most cases, it's counterproductive to make cash-only settlement offers concurrent with structured settlement offers," says Len Blonder of EPS Settlements in Los Angeles. "That's because you're trying to translate needs of an injured party into a settlement that replicates his or her future income."

In cases involving a minor, the tax advantage of a structure can be particularly apparent. The federal tax code provides that for children under age 14, income on investment is taxed at the parents' (or guardian's) rate. Income to minors may also reduce the exemption permitted to parents or guardians. Under a structured settlement, no matter what the child's age or parents' income, the periodic payments are free of federal taxes and the exemption is unaffected.

The defense team, working together and taking advantage of federal tax benefits available to the plaintiff, can design a solution that's financially attractive to the plaintiff and his or her lawyer.

The structured settlement solution should always address any special needs the plaintiff may have. This is important because, as any defense attorney knows, negotiations can sometimes flounder on what may appear to be incredibly extraneous issues. Chuck Harlan recalls a case involving a Maryland man who sustained significant personal injuries in an accident. The major impediment to settlement was the plaintiff's desire for enough money to buy a dairy farm. The defense would not agree to a lump sum payment large enough to purchase the dairy farm, so the dispute continued.

That's when the defense lawyer in the case brought Harlan in. In a few days, he had put together a payment plan for the claimant that took advantage of the tax-free payment stream enjoyed by structured settlements, plus the interest deduction from the mortgage on the dairy farm. Taking advantage of the dual tax benefits, the claimant agreed to settle and the case was immediately resolved. (An interesting side note: Shortly after the claimant purchased his dairy farm, prices for dairy products dropped considerably. The claimant wound up losing his farm, but still had his structured payments on which to fall back. Though it's obviously speculation, one must wonder if he would have been similarly "fluid" had he taken his entire settlement in a lump sum.)

Some defense lawyers, accustomed to negotiating one-on-one with plaintiff's counsel, may initially find it cumbersome to create a settlement "team" that includes a claims professional and a structure broker. And, of course, there is no requirement that these professionals be involved. Still, good results speak for themselves. Having a qualified structured settlement broker in the room, listening to the negotiations, can provide you with a wealth of helpful information. A good broker can discuss the plaintiff's needs, analyze numbers within the carrier's cost limitations, and suggest ways to resolve differences. The bottom line is that the structure broker's job is to listen and, if he does his job well, he will recognize information that helps settle the case.

Kyle Hording, a structured settlements broker in Pasadena, recall, "Once I was at a meeting which was going nowhere. We all took a break. The plaintiffs talked among themselves about Social Security and whether it would even be

around when they retired [they were in their late 40s]. I got out my computer, ran some numbers utilizing a 'retirement fund' of payments beginning when the oldest turned 60, and had the payments paid jointly or to the survivor. The case settled."

Finally, there is the issue of whether defense counsel should share with plaintiff's counsel the cost of the structure. In the early years of structured settlements, there was some concern among defendants that disclosing this information might trigger adverse tax consequences. Since then, the rules have been clarified, so there's no reason not to share this information. As Hording observes, "One of our biggest problems now is that the defense side used to decline to reveal costs, which were usually less than what the plaintiff's economist determined. The plaintiffs' bar is savvy and has the resources to determine settlement value. I always present the cost."

Structures and Case Size

Which cases are the most logical to handle with a structure? At first glance, industry figures seem to vary widely on this issue. On closer inspection, a clearer picture emerges.

On the issue of claim size, the Insurance Services Office's latest closed claim survey results confirm that the larger the claim and the more severe the injury, the more likely it is that a structured settlement will be used in resolving the claim. In settling claims involving losses of $75,000 to $99,999, structured settlements were used less than seven percent of the time. In settling claims involving losses of $1 million or more, structured settlements were used 29 percent of the time. The ISO survey concludes, "The average payment in claims involving structured settlements… was more than 59 percent greater than the average payment for claims paid in a single lump-sum…"

Structured settlements *are* often used to resolve smaller claims, but these usually fall into one of two categories: workers' compensation claims, for which continuing payments are often mandated by law, and claims arising from injuries to minors, whose parents or guardians choose structured settlements to protect against early dissipation. That's why a company such as Ringler Associates, a leading structured settlement brokerage company, shows statistics indicating that 52 percent of its 1999 cases settled for less than $50,000. The company is known for handling a large volume of workers' compensation cases, which should increase as a result of the 1997 change in the law mentioned above.

The Plaintiff's Counsel's Perspective

Finally, no discussion of personal injury settlements would be complete without a mention of the plaintiff's attorney. There is an increasing interest in the plaintiffs' bar in the use of structured settlements as a means of ensuring their clients' financial security. "Since the mid-1990s, there has been a surge in interest among plaintiffs' lawyers in structures," says Wm. T. "Tay" Robinson IV, President of Strategic Settlements in Kentucky. "More and more outside defense attorneys have embraced this shift. They tend to settle more cases, which has helped grow their practices."

For the vast majority of plaintiffs' attorneys, there is nothing so disheartening as seeing a former client lose compensation intended to last a lifetime—whether through poor investments, unscrupulous "friends," or outright fraud. Structured settlements combat this problem and, as such, have caught the attention of the plaintiffs' bar. Remember, the plaintiff's attorney must base his or her fee on the *cost* of the settlement, not the ultimate pay-out. Defense counsel must, therefore, factor that into the negotiations, for settlement to have any real chance.

To further protect the structured settlement transaction, in recent years state trial lawyer associations around the nation have formed alliances with insurance companies and defense attorneys on the issue of structured settlements. In nearly 20 states, they have successfully worked with legislators to pass consumer protection legislation against third party companies that purchase structured settlement payment streams from injury victims, often at a significant discount.

Such efforts further indicate the extent to which structured settlements are an area in tort practice that has managed to transcend the canyon of historical mistrust that too often has separated the plaintiffs' and defense bars. The defense lawyer who truly wants to best serve his or her client will do well to become intimately familiar with structures, why plaintiffs find them attractive, and how, working with a professional consultant with a proven track record, a structured settlement can help them resolve cases earlier and to the substantial financial benefit of the defense client. FD

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is not truly a part of discovery. Rather, testimony of this type is being taken, at least potentially, for use in lieu of live testimony at trial. As a result, aged, departing, or ill witnesses should be carefully interviewed and prepared for their depositions, just as if they were being presented in the courtroom.

To the extent that depositions need not be taken of, for instance, friendly witnesses who are likely to be available at trial, they should be avoided. The testimony of that friendly witness, once captured in a deposition transcript, can no longer be refreshed or molded to conform with the testimony of other witnesses. Furthermore, the testimony that the friendly witness will provide for the advocate's case at trial has now been advertised in great detail to the opponent.

In all but a few cases, the only witnesses who should be deposed are those whose position is hostile or adverse to the inquirer. Such depositions should be limited to gauging the effectiveness of the witness and learning just how the opposition witness will describe the key events, the key meetings, the key documents, and other key pieces of evidence that will be central features of the trial. Armed with this knowledge, the advocate can prepare his or her own case, recognizing that it is unwise to base one's case on points scored through cross-examination of the opponent's witnesses. On the contrary, one's own witnesses, by telling their own version of events, must meet and neutralize the adverse evidence the other side will present.

The defense advocate dedicated to true trial preparation avoids motion practice and discovery disputes to the greatest extent possible. Indeed, every potential motion and every potential discovery scuffle should be analyzed by asking, "Will this really matter at trial?" This analysis can be usefully applied both to motions and discovery disputes that one initiates and to motions and discovery issues brought forward by the other side. Why not ignore the one or two counts that might be removed from the case by summary judgment? Why not allow a particular question to be answered or category of documents to be produced, rather than forcing the case to stand still while these issues are resolved by the court?

Negotiations and Experts

The deepest hole into which the defense advo-