PRESENTED AT

14th Annual Changes and Trends Affecting Special Needs Trusts

February 15-16, 2018
Austin, Texas

Structured Settlement Solutions for Beneficiaries with Special Needs

Materials By
Carola M. Davis, CFS &
Elisa Dillard Rainey

Presented by
Elisa Dillard Rainey

Elisa Dillard Rainey, CELA*
Rainey & Rainey Attorneys at Law, LP
2900 West Waco Drive
Waco, Texas 76712
(254) 752-8644
elisa@RaineyAndRainey.com
www.RaineyAndRainey.com
*Certified as an Elder Law Attorney by the National Elder Law Foundation as recognized by the Texas Board of Legal Specialization

Carola M. Davis, CFS
Davis Settlement Partners
388 Comal Avenue
New Braunfels, Texas 78130
(830) 609-5555
Cmdavis388@gmail.com
www.DavisSettlementPartners.com

Structured Settlement Solutions for Beneficiaries with Special Needs

Elisa Dillard Rainey, JD, CELA
Carola M. Davis, CFS

Personal injury attorneys work not only to maximize the overall settlement of the case, but also to structure the payout in a way that will best meet the plaintiff's needs. This often includes the use of structured settlement annuities. Annuities have the potential to provide the beneficiary with a higher gross settlement over time than would a one-time lump sum distribution. The payout is structured in a way that guarantees a long-term source of income and, in some cases, protects plaintiffs from their own propensity to exhaust the recovery in the short term. Structured settlement annuities can be used to fund a special needs trust in order to protect the beneficiary's critical government program benefits and guarantee long-term replenishment of the trust throughout the beneficiary's lifetime.

In some cases, a personal injury attorney may be so enthusiastic about the benefits of a structured settlement annuity that he or she may advocate the structuring of the entire recovery. However, a trust practitioner involved in the settlement process should educate the plaintiff and his attorney about the prudence of balancing the annuity planning with ample up-front funding of a supplemental needs trust. It is important to fund the trust immediately with sufficient assets to meet the beneficiary's short-term needs and possible unforeseen circumstances as well as to make it practical for a corporate trustee to accept management of the trust.

I. STRUCTURED SETTLEMENT ANNUITY BASICS

A structured settlement is a special type of annuity purchased by the defendant in a personal injury lawsuit to pay the annuitant, the plaintiff, future periodic payments. The payments are tax-free under the Internal Revenue Code 104(a)(2) and have certain creditor/judgment protections. [1]

Historically, damages paid in an injury lawsuit came in the form of a single lump sum. This kind of payment, especially in catastrophic injury cases, often placed the plaintiff or the plaintiff's family in a difficult financial position. With plaintiffs focused on adapting to a new lifestyle, they often lacked the time, experience or inclination to manage large sums of money in a way that would assure their long-term stability.

This lack of skilled management can lead to serious trouble. A person who exhausts funds intended to pay for a lifetime of medical and living expenses does so at the risk of sacrificing critical medical care and independence. The proper use of a supplemental needs trust to shelter a personal injury recovery can provide for professional management of the funds and prevent the loss of Medicaid and SSI benefits. A carefully crafted structure as part of the trust planning can help in managing the beneficiary's expectations, guarantees replenishment of the trust corpus

[1] 26 U.S.C. § 104(a)(2); Texas Insurance Code § 1108.051.

according to the terms of the trust, and provides tax-free growth of the sum placed in the structure.

In 1982, a bipartisan Congressional coalition passed legislation that amended the federal tax code with The Periodic Payment Settlement Act of 1982 (Public Law 97-473).[2] This legislation formally recognized and encouraged the use of structured settlement annuities in personal injury cases. Section 104(a)(2) of the Internal Revenue Code clarified that the full amount of structured settlement payments is tax-free to the plaintiff.

The requirements to establish a qualified settlement are set out in Section 130(c) of the Internal Revenue Code:

- The assignee (the insurance company) assumes the liability from the defendant;
- Periodic payments are fixed and determinable as to amount and time of payment;
- The payment schedule cannot be "accelerated, deferred, increased, or decreased by the recipient of such payments";
- The injury must be a physical sickness or injury; and
- The payment stream is excludable from the recipient's gross income under IRC § 104(a)(2).[3]

Section 130(d) sets out the requirements of the annuity contract and the issuing company.[4]

In failing to consider a structured settlement annuity in the course of settlement, a plaintiff forever loses the opportunity to participate in one of the most significant tax breaks available. The tax savings when structuring either non-taxable or taxable (punitive or non-physical) damages can result in a sizeable difference in the long-term performance of the recovery. The plaintiff must balance the tax benefits of an annuity, which pays a modest rate of return, with a potentially higher rate of return from the investment of a lump sum payment, but the income from which is fully taxable. Furthermore, in weighing the potential return on the investment of a lump sum recovery, a prudent advisor cannot ignore the investment's vulnerability to market downturns.

II. ADVANTAGES OF A FIXED-TERM PLUS PAYOUT FROM A STRUCTURED SETTLEMENT ANNUITY

A structured settlement annuity works well to fund the future monthly expenses of the beneficiary, providing a guaranteed source of income for the life of the beneficiary and allowing the trustee more flexibility in the management of the funds already held in trust. A structured settlement annuity specialist can work with a plaintiff and a trustee to determine a good balance of cash and structured settlement annuity funding for the trust based on the short term and

[2] H.R. 5470 — 97th Congress: Periodic Payment Settlement Tax Act of 1982." www.GovTrack.us. 1982. February 4, 2018 <https://www.govtrack.us/congress/bills/97/hr5470>
[3] 26 U.S.C. § 104(a)(2)
[4] 26 U.S.C. § 130(d)

Title search: Structured Settlement Solutions for Beneficiaries with Special Needs

Also available as part of the eCourse
Answer Bar: Considering a Special Needs Trust

First appeared as part of the conference materials for the
14th Annual Changes and Trends Affecting Special Needs Trusts session
"Making Sense of Structured Settlements"