

Settlement Planning for Plaintiffs with Special Needs

Using the Special Needs Trust and Qualified Settlement Fund
by Kevin Urbatsch

Settlement planning is the process of ensuring that a plaintiff who has a significant disability, lacks capacity, or has a difficult financial situation will receive his or her litigation proceeds in such a way that it will not jeopardize his or her future. Too often plaintiffs receive a settlement that will cause harm because a plan has not been implemented. This may be due to the lack of time that such decisions need to be made or because the plaintiff's attorney is unaware of available planning options. Settlement planning is generally accomplished by bringing together experts in several fields, which includes some or all of the following:

- Special Needs Planning Attorney;
- Estate Planning Attorney
- Medicare Set-Aside Specialist
- Lien Resolution Expert
- CPA, and
- Financial Advisor.

The tools at the disposal of the settlement planner include the Special Needs Trust (SNT), the Medicare Set-Aside Arrangement, the structured settlement annuity, and the Qualified Settlement Fund. These tools can be used independently or together to maximize the litigation recovery for the client. The end result of the successful settlement planning process is that the personal injury attorney's client receives the litigation recovery in such a way that it:

1. Preserves eligibility for essential public benefits when necessary;
2. Is set up in an appropriate legal

vehicle (such as in a trust, conservatorship/guardianship, or through special bank accounts like UTMA or blocked accounts);

3. Is managed by an appropriate individual or entity with an excellent understanding of his or her fiduciary duties;
4. Protects the client from his or her own lack of knowledge in money management;
5. Is distributed to the client in the most tax efficient manner; and
6. Provides the appropriate financial resources throughout the life of the client.

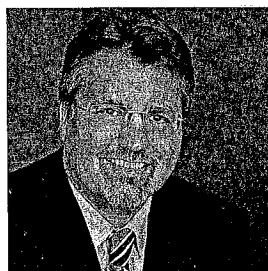
One type of plaintiff who requires a special plan is a plaintiff who is disabled and receiving needs-based public benefits (like Supplemental Security Income (SSI) or Medi-Cal) at the time he or she receives a settlement or judgment. Good planning is essential because receipt of assets will cause the person with a disability to lose his or her SSI and Medi-Cal until the assets are spent to below \$2,000 for an individual or \$3,000 for an eligible couple (i.e., the resource limits for SSI and Medi-Cal). If the person with the disability needs long term care and

is married to someone who is not disabled (the "community spouse"), then the community spouse may be able to keep a larger amount of assets.

Special Needs Trust

The primary planning tool in this situation is transferring the assets into a qualified first party SNT either placing assets in a trust authorized under 42 U.S.C. §1396p(d)(4)(A) (commonly called a (d)(4)(A) SNT) or joining a pooled SNT authorized under 42 U.S.C. §1396p(d)(4)(C). These are not the only planning options, others are:

1. Doing nothing and losing needs-based public benefits until assets are spent below the eligibility limits;
2. Spending the assets on exempt assets such as a personal residence or automobile or other qualified expenditures until assets are below the eligibility limits. This is commonly called a spend-down;
3. Gifting, transferring, or disclaiming assets, which results in the loss of needs-based public benefits for a period of time. Generally not favorable due to loss of benefits; or
4. Some combination of the above.



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Because a person with a disability is currently not allowed to establish his or her own (d)(4)(A) SNT, determining the correct procedure to establish the trust is often a very difficult task. The choice of the proper procedure depends on a number of variables, the most critical of which are whether:

- There is a parent, grandparent or legal guardian willing to assist, or, if not, whether a court order can be obtained;
- The person has capacity; and
- The person is a minor, age 18 or over but under age 65, or age 65 or over.

For a plaintiff who is 65 years of age or older, it is not possible to establish a (d)(4)(A) SNT due to the legal age requirement. For these plaintiffs, it is required that SNT alternatives be considered or they join a Pooled SNT.

There is only one situation in which a first-party SNT must be established by the court; i.e., if a minor or incapacitated adult with a disability receives a litigation recovery and is also the recipient of needs-based public benefits (See Probate Code §§3600–3613). Oftentimes, if a court petition is required, to establish the (d)(4)(A) SNT, the process can take weeks. Thus, it is important for personal injury attorneys to engage special needs planning attorneys as early as possible so the trust can be established in a timely manner.

At the time of settlement, there is often a mad scramble trying to execute and finalize settlement agreements, make financial decisions, negotiate liens, establish SNTs, or make tax decisions; each of which could have enormous irrevoca-

ble and life-long financial or personal ramifications for the plaintiff and the plaintiff's attorney. In order to provide the time for proper planning without sacrificing the final settlement with a defendant, there is an underutilized tool called the Qualified Settlement Fund (QSF) or sometimes called the 468B Trust. The QSF was created by IRS statute (IRC §468B) and the regulations implementing it.

Qualified Settlement Fund

A QSF can be used in many situations. The following example provides some of the uses of a QSF. John Doe is married to Jane and their case settles for policy limits with a third-party tortfeasor. John has a traumatic brain injury and there are questions of his legal capacity. John was injured on the job but also has a products liability claim. He receives both Medi-Cal and Medicare benefits. Medicare and Medi-Cal both have substantial liens along with the Workers' Compensation carrier. Jane has a loss of consortium claim and there are issues of allocation of the settlement to her and the couple's children that have yet to be resolved. A Medicare Set-Aside Arrangement may be necessary to preserve Medicare, and a SNT is a must to preserve his Medi-Cal eligibility. A structured settlement is also being considered for part of the settlement proceeds for the plaintiff and the plaintiff's attorney.

How can all of these issues be handled? How can the attorney get the money from the defendant immediately without ruining the client's available settlement planning options? The answer to all of these questions is to use a QSF.



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Settlement proceeds can be placed into a QSF and the defendant receives an immediate tax deduction and plaintiff(s) can execute a settlement agreement and release with defendant. This is a large benefit to the defendant as normally a defendant cannot claim a deduction until the funds are received by the claimant which can be delayed in a complicated settlement. However, even though funds have been distributed to the QSF, plaintiff and plaintiff's attorney are not treated as having received actual or constructive receipt of the funds by the IRS. The parties can thus influence timing of income by preserving the right of plaintiff or plaintiff's attorney to utilize a tax-free structured settlement annuity and to plan for plaintiff or plaintiff's tax recognition from receipt of the settlement funds. At the same time, funds held in the QSF preserve plaintiff's public benefit eligibility that would be jeopardized if the funds were placed into an attorney-client trust account or distributed to plaintiff. This also allows time to create SNT without holding up payment to plaintiff's attorneys of

their fee. Further, while the money is held in the QSF, liens can be negotiated and allocations of the settlement funds between parties can be resolved.

The QSF is relatively easy to establish. Any court, with or without jurisdiction over the matter, may sign the order creating the QSF and exert continuing jurisdiction over the trust. There are only three requirements for establishing a QSF.

1. It must be created by a court order with continuing jurisdiction over the QSF.
2. The trust is set up to resolve tort, contract or other legal claims prescribed by the Treasury regulations.
3. Finally, it must be a separate account, or trust under applicable state law.

Thus, the QSF is a temporary holding tank for the litigation settlement proceeds. It does not typically exist in perpetuity and is not meant to be a support trust for plaintiffs or their attorneys. Instead, it exists for as long as there

are issues that need to be planned for prior to disbursement. It can exist for weeks, months or even years; there is no limitation. It is truly a remarkable settlement planning tool.

All plaintiffs could benefit from some form of settlement planning. For adults without a disability and without a complicated personal or financial situation, the planning can be as simple as doing a financial or estate plan specifying what happens to the recovery in the event of death or incapacity of the plaintiff. For plaintiffs who may have a more complicated personal or financial situation, planning can include more advanced forms of estate planning to protect against the estate tax. There may be family issues (child support or spousal support) that need to be resolved, debts that need to be managed, and concerns with the client's ability to manage a significant sum of money for the first time in his or her life. A settlement planning professional can assist in identifying and resolving these issues. ■

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