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Commutation of a Structured Settlement
By Thomas D. Begley, Jr., Esquire

COMMUTATION OF A STRUCTURED SETTLEMENT

by Thomas D. Begley, Jr.

Unfortunately, claimants receiving the periodic payments under a structured settlement often face unforeseen events, such as unexpected medical bills, housing needs, school tuition, etc. One solution would be to have the plaintiff commute the structured settlement. A structured settlement can be commuted in whole or in part. When the structure is commuted, the payee receives a discounted lump sum. Typically, the payee receives the currently discounted value of the remaining periodic payments, commonly known as the present value. The obligation of the insurance company to make future payments is thereby terminated.

- *Commutation and I.R.C. §130*. There may be an issue as to whether a non-automatic commutation of a structured settlement violates the "no acceleration" provisions of §130. If the transaction is viewed from the perspective of the qualified assignee, the assignee is the legal owner of the annuity and has the right and power to change its terms. From that perspective, a non-automatic commutation is arguably an acceleration.[1]

- *Automatic Commutation Provisions*. Many structured settlements are written with a commutation rider that provides that the contract may be commuted at the payee's option upon certain events outside the payee's control and outside the control of the

[1] I.R.C. §2033.

annuity issuer. For example, a structured settlement may permit a partial commutation of the contract upon the death of the injured person so that monies are available to pay death taxes, or the structure may provide that the contract can be commuted in its entirety and that the remaining payments be made in a lump sum to named beneficiaries. It is not likely that the I.R.S. would view these types of commutations as violating the provisions of I.R.C. §130 prohibiting acceleration of payments.

If the payee of a structured settlement dies before the end of the guarantee period, the present value of the unpaid payments as of the date of death are includable in the estate of the decedent.[2] The gross estate includes the value of an annuity or other payment receivable by any beneficiary by reason of surviving the decedent under any form of contract or agreement if, under such contract or agreement, an annuity or other payment was payable to the decedent, or the decedent possessed the right to receive such annuity or payment, either alone or in conjunction with another for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death.[3] In cases involving large structured settlements, estate taxes must be considered unless the annuity is payable to a trust having sufficient cash to pay the anticipated tax, a commutation rider should be considered at the time the structure is established.

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[2] Structured Settlements: Factor vs. Commute?, Robert W. Wood, Tax Notes, Dec. 25, 2006.
[3] I.R.C. §2039(a).

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