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LEGAL LIMITS ON THE STRUCTURED SETTLEMENT OF DAMAGES

RICHARD LEWIS*

A STRUCTURED settlement is a new way of paying common law damages for personal injury or death. It has received strong support from the judiciary and a very favourable response from the Law Commission in its recent consultation paper.¹ The defendant's insurer, usually after having informally agreed a lump sum figure with the plaintiff, will agree to convert part of the damages into a series of periodic payments. To fund the arrangement the insurer purchases an annuity from a life office. The payments are "structured" to meet the individual's needs and are free of tax in the plaintiff's hands. This is because the Revenue have accepted that they may be considered instalments of capital rather than income. In return for making this arrangement the insurer will bargain for a discount on the conventional lump sum figure. Although the first structure was put in place as long ago as 1981, they were not used in other than a few isolated cases until 1991. Now there are almost two hundred of them, and the annuity market, worth £30 million last year, is expected to grow rapidly. Their increasing use constitutes the most radical reform of our damages system effected in recent years.

Nevertheless, few articles have been written on the subject.² There is a dearth of information about how structures have developed and the ways in which they are presently being used. This article deals with an important, topical area of law reform which does not

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¹ *Structured Settlements and Interim and Provisional Damages*, Consultation Paper No. 125, November 1992, reviewed by the author in (1993) 137(2) Sol.J. 36.

² But see the author's previous articles "Pensions Replace Lump Sum Damages" (1988) 15 *Journal of Law and Society* 392; "Structured Settlements in Practice" (1991) 10 *Civil Justice Q.* 212; "Structured Settlements in Britain and Canada" (1993) 42 *I.C.L.Q.* (forthcoming); and "The Merits of a Structured Settlement: The Plaintiff's Perspective" (1993) 13 *O.J.L.S.* 530. For other academic reviews of developments in this country see Allen, "Structured Settlements" (1988) 104 *L.Q.R.* 448, and Scott (1988) 7 *Civil Justice Q.* 99. There are many articles by practitioners e.g. Edwards (1989) 86 *L.S.Gaz.* (26 July); Frenkel, "Structured Settlements: Practical Considerations" (1989) 5 *Personal & Medical Injuries Law Letter* (April and May); Hulls, "Structuring Personal Injury Awards" (1990) 87 *L.S.Gaz.* (21 March); Holloway, "Everyone's a Winner" (1992) 152 *Post and Insurance Monitor* (12 Sept.); Frenkel, "Salvaging the Wreckage and Healing the Wounds" (1992) 136 *Sol.J.* 8; Whitfield, "The Basics and Tactics of Structured Settlements" (1992) 142 *N.L.J.* 135. There are now two books on the subject, I. Goldrein and M. de Haas, *Structured Settlements* (1993), and R. Lewis, *Structured Settlements: The Law and Practice* (1993).

result from new legislation or case law. There is still no official law report of any structured settlement case. Instead many of the sources upon which the author has relied are unpublished. These comprise transcripts of cases, proceedings of conferences and files and case reports from a variety of firms and organisations. In addition the author has interviewed many of those occupied with the matter, including lawyers, accountants, tax and insurance representatives as well as the leading intermediaries involved in negotiating such settlements.

The article examines the legal limits upon the types of case which may be settled by this means. A plaintiff has always been able to use the damages obtained from any form of litigation to buy an annuity, but tax must be paid on the income it produces. In practice therefore such arrangements are not made. The tax advantage gained by a structured settlement is exceptional. It applies only in favour of certain types of case.

First, these cases must be funded from particular sources. Thus certain insurers who do not pay corporation tax are not able to obtain the tax benefit, and in practice have not been involved in structures.³ Nor can a structure be used if the defendant does not owe an "antecedent debt" as required by the case law upon which the Revenue rely.⁴ This may prevent the structuring of the *ex gratia* compensation awarded by the Motor Insurers Bureau or the Criminal Injuries Compensation Board, for there is no possibility of these bodies being held legally liable to pay.

Secondly, the benefit of a structure may only apply to a particular type of legal action. The Revenue are concerned that the tax position be limited to cases involving debts arising as a result of personal injury actions; it does not wish to see structures extended to other forms of litigation or to debts arising in other circumstances.

The third limit upon cases which may be structured is that certain procedures must be followed. These require that the annuity be purchased and owned by the defendant, not the plaintiff; if at any time the plaintiff becomes formally entitled to a lump sum payment then it is too late to arrange a structure of that money. The dangers of reaching a binding settlement agreement or obtaining a formal court order for a lump sum are therefore explained below. To begin, however, there is a need to correct certain mistaken views concerning cases which can, in fact, be structured.

³ However, non-liability to corporation tax has not prevented Health Authorities from arranging structures. By s. 519A of the Income and Corporation Taxes Act 1988 the Authorities are tax exempt, and are able to reclaim the tax withheld from annuity payments made to them.

⁴ The main authority is *Dott v. Brown* (1936) 154 L.T. 484; [1936] 1 All E.R. 543. For detailed analysis see Lewis, "The Tax Treatment of Structured Settlements" (1993) *British Tax Review* (forthcoming).

I. DISPELLING DOUBTS ABOUT CASES WHICH CAN BE STRUCTURED

A. *Where there is a Dispute about Liability*

Structures are not confined to cases where full liability exists; it makes no difference whether or not there is contributory negligence.⁵ If the parties are able to reach an informal agreement as to the sum to be structured, their reasons for agreeing that particular sum are of no concern. Cases have been structured where there was never any joint view as to the degree of contributory negligence involved. This, of course, may also happen in conventional lump sum settlements.

B. *Where a Fatal Accident is Involved*

Fatal Accidents Act cases can be structured. The first was set up in 1992 for the benefit of Mrs. Boobbyer, the wife of a surgeon killed in a road accident.⁶ A previous High Court hearing on the issue of liability had determined that the surgeon was 50 per cent. to blame, but neither his death, nor the finding of contributory negligence against him, prevented a structure for £350,000 from being put in place for his wife. In another case in that same year structures for dependent children were put in place for the first time following a fatal accident.⁷

C. *Cases Involving Several Defendants*

Structuring can be arranged here in either of two ways.

(1) Separate settlements can be made with each defendant, some or all of them agreeing to put in place their own structure for the plaintiff.

(2) Alternatively, one defendant can agree to implement a single structure on behalf of the others. This defendant would receive contributions from the others to cover their agreed share of the premium, and to meet the operating and administrative costs of the structure.

⁵ *E.g.*, *Boobbyer v. Johnson*, *The Times*, 21 January 1992, the case of NJO cited in Kemp and Kemp, *The Quantum of Damages*, para. 6A-047, and *Moxon v. Senior*, unreported transcript 10 July 1991, where the damages were reduced by a third for contributory negligence. P. Cornes, *Coping with Catastrophic Injury* (1993) p. 22 reveals that of cases settled for £150,000 or more by insurers in 1987 and 1988 there were clear indications of reductions for contributory negligence in only nine per cent. of cases, but it features in the negotiations in other cases without the outcome being clear.

⁶ *Ibid.* For further details see Bawdon, "A System where Both Sides Win?" (1992) 6(6) *The Lawyer* 5.

⁷ *Greene v. Moore*, unreported, transcript 9 October 1992.

D. Where there has been a Payment into Court

The tax-free benefit of a structure is lost if a plaintiff formally accepts a lump sum paid into court under R.S.C. Ord. 22. Nothing can be done retrospectively if a binding contract for the settlement of a case has been concluded. If plaintiffs' lawyers fail to appreciate this they may expose themselves to an action for negligence. Unless it is formally accepted, a payment into court does not of itself preclude a successful structured settlement, although it may cause a minor logistical problem in obtaining the monies lodged with the court funds office. There is also a danger that the monies in court will be paid out direct to the life office, instead of being returned to the defendant's solicitors, the liability insurer then providing the funds for the purchase of the annuity. More important is the fact that a payment in may lead to a more aggressive adversarial approach, and can put pressure on the plaintiff to think only in terms of the conventional lump sum. It can thus impede any discussion of a structure.

E. Where a Court Judgment is Involved

A court has no power to order a structure against the wishes of either of the parties. Even where the parties are both prepared to arrange a structure they will be prevented from doing so if there is a judgment awarding damages and a formal order is made which entitles the plaintiff to a lump sum. Again this is because a structure cannot be organised retrospectively; if the plaintiff is legally entitled to a lump sum it is too late to arrange instalment payments on favourable tax terms.

This limit upon structuring is made less significant by two factors. First, it remains comparatively rare for damages to be awarded by a judge as opposed to being agreed by the parties;⁸ and secondly, certain decisions made by a court need not prevent the parties from arranging a structure if they both agree to do so. For example, a court judgment solely concerning liability will not preclude a structure.⁹ Even a judgment awarding damages will not do so if the parties request the judge to make only findings of fact as to the value of the heads of claim.¹⁰ Using this indication of the amount of damages the judge has in mind, the parties may then adjourn to investigate whether a structure might be arranged before any formal order

⁸ P. Cornes, *Coping With Catastrophic Injury* (1993), p. 20 reveals that even in cases involving damages of £150,000 or more paid by insurers in 1987 and 1988, only 10 per cent. were the result of formal court judgments. Whether this figure includes consent orders is not known. Of personal injury claims in general—most being for very small sums—only one per cent. get as far as the door of a court. *Report of The Royal Commission on Civil Liability and Compensation for Personal Injury* (1978, Cmnd. 7054) vol. 2, table 12.

⁹ As in the *Boobbyer* case above.

¹⁰ There is power to do this under R.S.C. Ord. 33, r. 3.

discharging the action by consent is sought.¹¹ The plaintiff may seek an undertaking from the defendant that interest will be paid from the adjournment either to the date of the structure, or if the structure fails, to the date when the lump sum is eventually paid.¹²

F. Settlements out of Court where no Judge may be Involved

Provided that the plaintiff is not under any disability which prevents him from understanding the nature of the proposed settlement, there is no reason why a court need be involved in a structure. In half of the structures presently in place, however, the court's approval was necessary because the plaintiff was either a minor or had been mentally impaired by the accident. This meant that the consent of the Court of Protection as well as that of the High Court was required.¹³

II. CASES WHERE THE TAX POSITION DISCOURAGES A STRUCTURE

A. Where a Mutual Insurance Company is Involved

A mutual insurance company has no shareholders. Its owners are its policyholders and they share in the profits it makes. At present mutual insurers can only take part in structures if they are prepared to accept a tax loss. In practice, therefore, no structures have been put in place directly involving such companies. Although there are relatively few mutual as opposed to proprietary companies, and in spite of the fact that several of them have recently transformed themselves into proprietary companies, they constitute a significant part of the market against which there is discrimination with regard to structures.

The discrimination arises because of the tax position of the mutual insurer. The Revenue at present require that the life office pays tax on the payments arising from the annuities which form the structure, with the result that the liability insurer must gross them up in order for the plaintiff to receive the payments in full. The liability insurer reclaims the grossed-up amount by offsetting it against its liability to pay corporation tax. Mutual insurers cannot offset this amount

¹¹ As in *Payne v. Thackray* (1991) 7 *Personal and Medical Injuries Law Letter* 60.

¹² The plaintiff may seek interest at the highest rate, as prescribed by the Judgment Act 1838, s. 17, and an undertaking from the defendant may help avoid the difficulties in obtaining this rate which may be caused by *Thomas v. Bunn* [1991] 1 A.C. 362. Claiming interest is also referred to by Whitfield, "The Basics And Tactics Of Structured Settlements" (1992) 142 *New L.J.* 135.

¹³ Under R.S.C. Ord. 80. As indicated above, the need for such consent does not bar a structure. According to the evidence submitted to the Law Commission by the Master of the Court of Protection in March 1993, the court had participated in 87 structures. The author estimates this to be about half of all the structures which had been put in place at that time.

because they do not pay corporation tax on their trading operations; they trade only with their own members and do not make a taxable trading profit. They are, however, taxed on their investment income. The money arising from the annuity is treated as investment income and has tax withheld by the life office, but the payments to the plaintiff which must be made are considered to be part of the mutual activity and cannot be offset against the investment income. Any structure would therefore have to write off the tax suffered on the investment income, and this makes them uneconomic.

This does not mean that a mutual insurer can never be involved in a structure. There have already been three types of case where, albeit indirectly, such companies have been involved. In the first of them a wholly owned subsidiary, not itself a mutual company, was able to structure because of its different tax position. In the second there was another insurer also defending the case in addition to the mutual company, and a deal was struck to take advantage of that insurer's tax position. The third case involved the insured party itself standing in place of the mutual insurer in the structuring agreement. Using the insurance money it obtained from the mutual company, the insured party then purchased the annuities directly, and used its own tax position to reclaim the grossed-up amount. The case in which this happened involved the Municipal Mutual, formerly the insurer of most local authorities.¹⁴ The insured, Westminster City Council, was substituted for the insurer in the structuring agreement, the judge being convinced that the local authority was substantial enough to be able to ensure that the payments would continue for the period of time envisaged.¹⁵ It received the insurance monies from the mutual company to enable it to purchase the annuity, and thus the insurance company was able to participate indirectly in the structure that was set up.

The Law Commission considers that the disincentive on mutual insurers' taking part in structures is significant. It provisionally proposes that one of two solutions be adopted. It suggests that the Revenue should permit mutual companies to reclaim the tax, just as Health Authorities have now been permitted to do¹⁶ Alternatively, and this is the more radical solution, it would allow the life office to pay the instalments of damages in full and directly to the plaintiff, thus cutting out the need for the liability insurer to gross-up and reclaim the payments. It supports legislation to allow the same tax-

¹⁴ *Marshall v. Westminster City Council*, unreported, transcript 8 March 1991.

¹⁵ This was a fortunate decision because in fact it was the Municipal Mutual that later become insolvent. Most of its obligations were taken over by the Zurich Insurance Company in early 1993.

¹⁶ Law Commission Consultation Paper No. 125, *op. cit.* note 1 above, para. 3.32.

free status to be given to all annuities bought by defendants in actions for personal injury. Careful definition of "personal injury" would be required to ensure that advantage could not be taken of the resulting tax benefits by others seeking to avoid the sharply different treatment accorded by the Revenue to income as opposed to capital.¹⁷ In other respects the actual mechanics of the change could be implemented easily.¹⁸ This reform would also assist the other non-taxpayers discussed below to participate in the benefits of a structure. It would thus create a "level playing field" for all, instead of the current position where the plaintiff's ability to structure depends upon the nature of the organisation funding the damages.

B. Cases against Medical Defence Organisations

Mutual indemnity associations in effect insure doctors against liability without themselves being classified as insurance companies.¹⁹ Their tax position is similar to the mutual companies discussed above and this discourages the implementation of a structure.²⁰ In addition, concern has been expressed as to the long-term security of any arrangement entered into with one of these organisations.

The importance of the defence organisations to the compensation system has, however, recently been much reduced. This is because there has been a change in the way in which compensation is funded following a successful claim for negligence against a hospital. Following the introduction of "NHS Indemnity" in 1990,²¹ District Health Authorities now assume responsibility for all new and existing claims of medical negligence. They no longer require their staff to subscribe to a defence organisation nor do they seek a contribution from such an organisation if damages must be paid. Defence organisations now only have a role to play where injury results exclusively from medical negligence which is not connected with hospital treatment, as when it occurs in treatment given by a general practitioner. The limitation upon structuring therefore affects only a minority of medical cases, for if a hospital is involved and the liability of the Health Authority is in question then a structure can be put in place.

¹⁷ It has been suggested that some form of policing of the new class of tax-free annuities might be required. Safeguards could include requiring that the court approve any settlement involving such annuities, or that solicitors for both sides should certify that the annuity was purchased in respect of a personal injury case. See Ashcroft, "Structured Settlements; A Practitioner's Viewpoint", p. 4 (unpublished paper presented to the Law Commission, June 1992).

¹⁸ *Ibid.*

¹⁹ *Medical Defence Union v. Department of Trade and Industry* [1980] Ch. 82.

²⁰ Evidence of the Medical Defence Union to the Law Commission, December 1992. However, the MDU has been involved with two structures in Canada.

²¹ P. Fenn and R. Dingwall, "Medical Negligence and Crown Indemnity" in A. Harrison and J. Grettton (eds.), *Health Care Law UK 1989* (1990); M. Jones, *Medical Negligence* (1991) p. 290; Lewis, "Health Authorities and the Payment of Damages by Means of a Pension" (1993) 56 M.L.R. 844.

C. *Where Foreign Insurers are Involved*

Even if foreign insurers transact no business in this country, they may still become liable to pay claims brought by British residents. This may occur, for example, where their insured party is involved in a motor accident while visiting Britain.²² A plaintiff in such a case may not benefit from a structure if the foreign insurer's tax position is such that it is unable to reclaim the amount by which it grosses-up the payments to the plaintiff. Such an insurer would then suffer from the same disincentive to structure as affects mutual insurers and medical defence organisations. Whether a foreign insurer is actually affected in this way depends upon whether it must pay tax on the annuity under its own domestic law, and whether the particular country involved has entered into a double tax treaty with Britain.²³ Even if in law a foreign insurer can reclaim or avoid paying tax upon the annuity, the complexities are such that it may wish to avoid using this form of settlement. In addition the concern of plaintiffs that the long-term arrangement made by a structure may not prove secure is made greater where a foreign insurer is involved: it is less likely that there will be any financial safety net if such an insurer becomes insolvent.

The problem will be made more serious with the expansion in the market for overseas insurers following the introduction of "freedom of services" within the European Community.²⁴ Although foreign insurers will be required to appoint an agent in this country to deal with claims, the compensation paid will be funded from a foreign source, and therefore is likely to give rise to the tax disincentive to structure.

²² In fact the claim is usually dealt with by the Motor Insurers' Bureau, acting in its capacity as the UK Green Card Bureau. Under a system organised under the auspices of the United Nations the Bureau is deemed to be the insurer acting on behalf of 31 countries which have signed certain agreements. However, the funds for the settlement will derive from the overseas insurer.

²³ If so it is possible to apply for a certificate of exemption under the Double Taxation Relief (Taxes On Income) (General) Regulations 1970 (S.I. No. 488). The annuity may then be paid to the plaintiff gross, thus saving the foreign insurer the need to reclaim the tax. No allowance for this possibility was made by Newstead, "The View from Somerset House" (1989) 7(10) *The Litigation Letter* 78. He refers to the need to deduct tax in the case of a foreign insurer as an "absolute requirement" under The Income And Corporation Taxes Act 1988, s. 437(1). This ignores s. 788(3) of that Act which permits the provisions of a double tax treaty to override anything to the contrary in UK domestic law.

²⁴ The various EC directives are discussed by Devine in (1993) 81 B.Ins.L.J. 10, and Coates, "Europe and the Way Ahead" (1993) 2 *International Insurance Law Review* 38. They are contained in J. Maitland-Walker, *EC Insurance Directives*.

III. CASES WHICH CANNOT BE STRUCTURED

A. *Where Either of the Parties Refuses to Structure*

Structures can only be arranged if both parties consent. They must freely enter into the settlement contract. Neither can be compelled to do so even by a court. This was decided in *Burke v. Tower Hamlets Health Authority*²⁵ where the judge refused an application for an order that the defendant pay the plaintiff's nursing home costs not in one lump sum, but as they arose during the remainder of the plaintiff's life. Although this decision has not gone without criticism,²⁶ the same conclusion was reached shortly thereafter by the Supreme Court of Canada.²⁷ The Law Commission is at present considering whether the court should be given the power to impose a structure against the wishes of either of the parties.²⁸

B. *Where the Plaintiff has Received or is Entitled to a Lump Sum under a Formal Settlement or Court Order*

The utmost care should be taken to ensure that the defendant has not already discharged his debt before entering into the structured settlement. If he has, it will prevent any structuring of the monies involved even if both parties wish to make such an arrangement. The transaction will be treated as the purchase of an annuity by the plaintiff, and the tax benefits are then lost. This was confirmed by the Inland Revenue after they had been approached by Frenkel Topping on behalf of parties who had already made a formal settlement.²⁹ There have been cases in the USA where structures failed because plaintiffs' lawyers only contacted brokers after receiving cheques from defendants.³⁰ No formal settlement should be agreed before the arrangements for a structure are put in place.

Formal court orders must similarly be avoided.³¹ However, as explained above, a structure is not necessarily precluded by the need to go to court to obtain a ruling. The number of cases of personal injury that actually proceed to judgment as opposed to being settled

²⁵ *The Times*, 10 August 1989.

²⁶ Croxon, "Has a Court Power to Make an Order other than a Lump Sum for Damages for Personal Injury?" (July 1990) *AVMA Medical and Legal Journal* 4.

²⁷ *Watkins v. Olafson* (1990) 50 C.C.L.T. 101.

²⁸ *Op. cit.* note 1 above, para. 3.71 *et seq.*

²⁹ Kemp and Kemp, *The Quantum of Damages*, para. 6A-058.

³⁰ Macmillan and Yamasaki, "Myths and Misconceptions Concerning Structured Settlements" (1987) 20 *Hawaii Bar Journal* 137 at p. 143.

³¹ This may not always be easy to achieve. For example, even though an insurer may be entitled to avoid a defendant's liability policy in respect of a road accident, the insurer may be obliged to satisfy any judgment obtained against the defendant. The insurer's obligation stems from the Road Traffic Act 1989, s. 151, but it does not arise until seven days after the date of judgment. A structure may therefore only be possible if the insurer agrees that the formal proceedings required under the Act need not be instituted.

are relatively few: the Pearson Commission found that they numbered only one per cent. of all the cases brought, although this figure included even small claims, which are almost bound to be settled.³² However, the more serious the case, the greater the likelihood that a court appearance will prove necessary. It seems anomalous that in spite of the parties' consent, no structure is possible in these cases unless great care is taken in drafting the orders made by the court. The Law Commission are therefore in favour of legislation to enable judges to order a structure where the parties consent to it.³³

C. *Criminal Injuries Compensation*

The Criminal Injuries Compensation Scheme was set up in 1964.³⁴ It enables those who suffer personal injury as a result of a crime to claim compensation from the state, unless their injury relates to an accident involving a motor vehicle.³⁵ The compensation is assessed using common law principles, and therefore in cases of serious injury it can amount to substantial sums. At present, however, there is no way in which this money can be structured. The main reason for this relates to the status of the scheme itself: it is administrative in nature with payments being made by a Board *ex gratia*. Although legislation which would put it on a statutory basis has been passed, it is not yet in force, and there are no current plans to implement it.³⁶ Accordingly a decision of the Board does not "give the applicant any right to sue either the Board or the Crown for that sum".³⁷ Since the Board is not under a legal obligation to make payments, claimants cannot establish that there is an "antecedent debt" owed to them. It was held in *Dott v. Brown*³⁸ that it is essential for such a debt to exist in order for the periodic payments under a structure to be considered capital and not subject to tax.

The Law Commission view this as most unsatisfactory. The *ex*

³² *Report of the Royal Commission on Civil Liability and Personal Injury* (1978; Cmnd. 7054), vol. 2, table 104.

³³ *Op. cit.* note 1 above, para. 3.38. There was a suggestion that the court had such a power in *Metcalf v. London Passenger Transport Board* [1938] 2 All E.R. 352.

³⁴ See D. R. Miers, *Compensation for Criminal Injuries* (1990), D. Greer, *Criminal Injuries Compensation* (1991), and D. Foster, *Claiming on the Criminal Injuries Compensation Board* (1991).

³⁵ The presumption then being that compulsory liability insurance will be in force and that compensation can be obtained at common law, or from the Motor Insurers Bureau as discussed below. There are other exceptions to the scheme, including injuries received as a result of domestic violence.

³⁶ The Criminal Justice Act 1988, ss. 108–117 establish the scheme, but under s. 171(1) it only comes into effect from a day to be appointed. Miers, *op. cit.*, p. 11 states that this is some years away.

³⁷ *Per* Diplock L.J. in *R. v. Criminal Injuries Compensation Board, ex p. Lain* [1967] 2 Q.B. 864, 883.

³⁸ (1936) 154 L.T. 484; [1936] 1 All E.R. 543.

gratia nature of the payments is a fiction in practice because the Board is in effect compelled to compensate all those who come within its terms, refusal to do so being subject to challenge by judicial review. Reliance upon this fiction to exclude victims of crime from the benefits of structuring is seen as anomalous. The Commission are in favour of extending those benefits to all victims of personal injury who purchase annuities with the damages awarded to them.³⁹ Its preferred solution departs entirely from the limitations imposed by *Dott v. Brown*. It would legislate to allow a life office to pay directly to a plaintiff the instalments of damages arranged by the liability insurer. In addition, the life office would be allowed to pay the plaintiff in full, without deducting any of the tax withheld at present, provided that the case involved personal injury and fell within permitted limits. These would be defined so as to include claims made for criminal injuries compensation.

If this tax problem is solved a second issue then arises. Does the Criminal Injuries Compensation Board have the power to purchase annuities and award compensation in the form of a structured settlement? This is presently being considered by the Home Office who are responsible for the scheme.⁴⁰ Although the rules of the scheme state that compensation is normally to take the form of a lump sum, the Board is given a general discretion to make special arrangements for the administration of an award. It may be that this is sufficient for it to implement structured awards.⁴¹ If, however, the legislation which puts the scheme on a statutory basis were to be implemented, the Board would undoubtedly have the power to buy annuities in the same way that Health Authorities, as Crown bodies, have recently been able to do. Despite the preliminary inquiry of the Home Office into the feasibility of structuring,⁴² such settlements cannot realistically be contemplated until the status and powers of the Board are made clear and the tax position is changed.

In March 1993 the Home Secretary announced that changes were to be made to the basis upon which compensation is to be paid.⁴³ The present scheme is to be replaced by a tariff system from April 1994. Compensation will no longer be assessed on the basis of common law damages, but will be related to the severity of the injury suffered rather than its effect upon the individual. Although the details are

³⁹ *Op. cit.* note 1 above, para. 3.33.

⁴⁰ Letter from the Home Office to the Commission, 14 July 1992.

⁴¹ See paras. 9 and 12 of the revised 1990 scheme, H.L. Deb. vol. 163, cols 410-417, 8 December 1989; Greer, *op. cit.*, appendix B. However, the Commission suggests that the scheme might require amendment.

⁴² Frenkel Topping in its evidence to the Law Commission, April 1993, note that they were consulted by the Board who, at that stage, were hoping eventually to follow the path of Health Authorities and themselves fund structures.

⁴³ H.C. Deb. vol. 221, cols. 501-507 (18 March 1993).

not yet settled, the new scheme will continue to be non-statutory and its payments *ex gratia*.⁴⁴ This will continue to prevent the claims being structured.

IV. CASES WHERE DOUBT EXISTS AS TO THE POSSIBILITY OF STRUCTURING

A. Motor Insurers' Bureau Cases

The MIB is a guarantee fund set up by all motor insurers in order to compensate the victims of uninsured and untraced motorists who cause injury as a result of their negligent driving.⁴⁵ Some of these cases involve very severe injuries: at present the Board is dealing with 300 cases in each of which half a million pounds is at stake. There are about 25 new such cases each year, in addition to thousands of smaller claims. The Bureau was formed in 1946 after the Government put pressure on insurers to close some of the loopholes which left certain persons injured through the fault of drivers without an effective right to common law damages.⁴⁶ The Bureau is not the product of legislation, but operates on the basis of a series of agreements with the Secretary of State for Transport.⁴⁷ Its constitution is therefore extremely unusual, and leaves victims with no direct right of action against the Bureau itself.

The peculiar status of the Bureau gives rise to problems with regard to structuring which are very similar to those already discussed in relation to criminal injuries. Again difficulties are caused because *ex gratia* payments may be involved, and there are doubts about the tax status of the organisation and whether it has the power to purchase annuities. It pays only minimal corporation tax and even if it were able to structure it would suffer from the same problem which affects mutual insurers: it would be unable to reclaim the amount of tax deducted at source by the life office.⁴⁸ The Law Commission here favours the removal of these disincentives to structure just as they do in cases of criminal injury and claims against mutual insurers. It proposes that any annuity purchased by defendants (to include the MIB) in respect of a personal injury claim be paid directly to the

⁴⁴ Letter from the Home Office to the Law Commission, 13 April 1993.

⁴⁵ D.B. Williams, *The Motor Insurers Bureau*; P.S. Atiyah, *Accidents Compensation and The Law* (4th ed., 1987) pp. 247-252; R.L. Colinaux, *The Law of Insurance* (6th ed., 1990) pp. 350-362.

⁴⁶ Lewis, "Insurers' Agreements not to Enforce Strict Legal Rights" (1985) 48 M.L.R. 275, 279.

⁴⁷ The current agreements are reproduced in I. Goldrein and M. de Haas, *Butterworths Personal Injury Litigation Service*, vol. 1, Div. 3F.

⁴⁸ Even if the tax could be reclaimed problems would be caused by the Bureau's present system of funding. This is based upon insurers contributing to the cost of claims paid in the current year rather than when the accident occurred.

plaintiff by the life insurer without deduction of tax.⁴⁹ Although the Bureau agrees that this would solve the majority of its problems, other administrative difficulties would remain.⁵⁰ Its preferred solution is to allow plaintiffs themselves to use their compensation to purchase tax-free annuities directly.⁵¹

As yet no case involving the MIB has been structured. Whether it is possible to do so depends upon which of the three classes of case dealt with by the MIB is being considered. Although the position remains uncertain, it may be that the first of them considered below can be structured, whereas the preliminary view of the Revenue upon the other two is that they cannot be structured.

1. A driver with insurance which can be avoided by the insurer

Here an insurer issues a policy in respect of the defendant, but is entitled to avoid it because, for example, it was obtained as a result of a misrepresentation.⁵² Insurers engaged in underwriting motor liability are all bound by the "domestic regulations"⁵³ under which the insurer who issued the policy in the first place will not throw the liability back upon the financial pool created by the MIB, but instead will use its own resources to meet the claim. Acting on behalf of the MIB, Frenkel Topping have received a carefully worded letter from the Revenue.⁵⁴ It states: "It would seem from your description of the normal settlement procedure for [this class of case] that no special factors arise which would prevent the plaintiff from settling his or her claim by entering into an agreement with the 'Domestic Insurer' in terms which would generate a structured series of capital payments." This letter may be viewed with some optimism. Those hoping to extend structures may point to the importance of the contract which existed between the defendant driver and the insurer, for this may form some basis for establishing an antecedent debt owed by that insurer. On the other hand others may be more dubious about the possibility of structuring even these claims. After all the contract was avoided by the insurer, and some other basis for establishing the debt may be required, as discussed under the next heading.

⁴⁹ *Op. cit.* note 1 above, paras. 3.33 and 3.36.

⁵⁰ For example, the Bureau deals with claims by allocating them to insurers to handle on its behalf. It would be unlikely that the additional costs resulting from a structure would be spread equally among its members, and a system of compensation would have to be devised.

⁵¹ Evidence of the MIB to the Law Commission, March 1993.

⁵² Avoidance is possible under the Road Traffic Act 1988, s. 152(2).

⁵³ The memorandum and articles of association of the Bureau were amended in June 1992 so as to replace the "domestic agreement", and avoid the necessity for changes having to be signed by every member of the Bureau.

⁵⁴ Ashcroft, *op. cit.* note 17 above, p. 15. Certain information given in this section has been supplied to the author by Mr. Snook, claims manager for the Bureau.

2. *An identified driver who has no insurance policy*

Unlike the domestic regulations cases, here there is no obvious insurer to take responsibility for the liability of the particular driver known to have caused the accident. The Bureau therefore becomes directly involved. It tries to establish a contractual relationship with the uninsured driver by offering to act on his behalf in return for an undertaking that it should have the right to reclaim from that driver any compensation it pays. If the uninsured driver will not cooperate the Bureau can either take executive action and negotiate a settlement, relinquishing its right to any chance of recovery, or it can wait until the court action begins when it may apply to be added as a defendant. The difficulty in structuring these cases is that it is likely that there will be no contractual relationship between the defendant and the MIB. If there is no such relationship, any payment made will be *ex gratia*, and as with criminal injuries compensation, this will prevent a structure from being put into place: there is no antecedent debt, as required by the case law, upon which to found any tax-free instalment payments. In addition, if a judgment has to be obtained against the defendant before the MIB will take responsibility, the possibility of structuring the case will be lost.

3. *An unidentified driver*

The MIB are also responsible for providing compensation in cases involving hit-and-run drivers who are not later identified. They may or may not have been insured. Here there is no possibility of there being any contractual relationship between the driver and the Board. Again, therefore, payments are made on an *ex gratia* basis so that it is not possible to establish an antecedent debt upon which to base the tax-free annuities of a structure.

B. Where Provisional Damages are Involved

If there is a chance that the plaintiff will suffer some serious deterioration in his condition it may be advisable to obtain a provisional award of damages. This allows the plaintiff to return for a further sum later if his condition in fact gets worse. Applications for such orders are few. It appears that they may prevent a structure taking place, although this is not certain.

There are two obstacles to structuring such awards. First, they cannot be brought within the terms of the 1987 model agreement for structures, as drawn up by the Association of British Insurers and approved by the Revenue. This is because the standard form used in the model requires the plaintiff to "discontinue any proceedings . . . in connection with the claim", and this would not happen in

a provisional award because the plaintiff is free to recommence proceedings if necessary. It is not evident, however, why those seeking a provisional award should be excluded from the benefits of structuring. Modifications to the model agreement have been accepted by the Revenue in other types of case, and some may think that the agreement could not have been drafted with cases of provisional damages in mind. On the other hand it may be that the ABI were well aware of provisional damages when drafts of the model agreement were being considered. Insurers strongly oppose structures being subject to review if this means either that new money may have to be introduced into the settlement at some distant date, or that encouragement may be given to extending the grounds for review. The fear is that there might be no clear limit to the extent or duration of insurers' liability. The model agreement as presently drafted therefore excludes any form of review. However, with structures as they are at present there is no question of insurers' fears being realised: no new money is being sought by those wishing to structure provisional damages, nor are the grounds for review being increased from what they are at present.

If a departure from the model agreement were accepted by the Revenue, a second problem would arise. As described above, care must be taken to ensure that a structure is put in place before a court issues a formal order awarding the plaintiff a lump sum, whereas provisional damages can only be arranged via a court order.⁵⁵ It is uncertain whether it is possible for a court to issue such an order which incorporates by reference the terms of the agreed structured settlement, and still allows application at a later date for further damages. Although the court has discretion to make an order "on such terms as it thinks just",⁵⁶ the present procedures seem to envisage settlements and court orders based only on lump sum awards.

Without examining the complexities involved, the Law Commission state that a provisional damages award cannot be structured because it results from a court judgment.⁵⁷ The conclusion may be correct, but the matter is by no means clear. The Commission provisionally conclude that it is nevertheless desirable to facilitate the structuring of such awards. This could be done by requiring the Revenue "to recognise court orders facilitating structured . . . provisional awards as a type of 'Model Agreement'", and by amending the rules on provisional damages.⁵⁸

⁵⁵ By R.S.C. Ord. 37 r. 8 and r. 9. The procedural issues are examined by D. Brennan, *Provisional Damages* (1986), p. 31.

⁵⁶ R.S.C. Ord. 37 r. 8.

⁵⁷ *Op. cit.*, para. 5.21.

⁵⁸ *Ibid.*

C. Awards of Interim Damages

For reasons similar to those discussed in relation to provisional damages, it is doubtful whether awards of interim damages can be structured. This is, however, of little practical importance, since such awards are usually for limited sums.⁵⁹ They are often sought to enable a plaintiff to establish a care regime for the immediate future, and are not viewed as providing damages for life. Nevertheless the Law Commission are in favour of the parties being able to structure interim damages if they so wish.⁶⁰

When considering the amount to be sought as an interim payment a plaintiff's lawyer must balance the advantage to be gained by having the money in the plaintiff's hands rather than the defendant's (thus e.g. securing a full rate of interest), against the disadvantage of removing capital from the potential structure. However, given that the eventual settlements will usually make provision in any event for a capital sum to cover contingencies, it is unlikely that much disservice will be done to the plaintiff by seeking as large an interim award as possible.⁶¹ Thus in *Grainger v. Hagan* an interim award of £350,000 was obtained.⁶² This was not thought sufficient to prejudice any later structure of the outstanding damages of more than a million pounds, and a structure was later put in place.

D. Cases Not Involving Personal Injury

Any attempt to extend the use of structures to other than cases of personal injury would receive very close scrutiny from the Revenue. The tax agreement with the ABI was reached for economic and social reasons in order to give preferential treatment to the victims of personal injury: they have long-term future needs, and, without structures are more likely to become dependent upon the state. It is by no means clear, however, that the legal authorities which allow the tax-free payment of a capital debt by means of instalments are necessarily to be confined to cases of personal injury.

In so far as structures blur the distinction between income and capital, tax advisers might seek to utilise the concept in situations far removed from that originally envisaged. In a family law context it is already employed in North America by those rich enough to be able to purchase an annuity to reduce the cost of paying maintenance to a

⁵⁹ However, they may be for a "reasonable proportion" of the damages the plaintiff would get at trial.

⁶⁰ *Op. cit.* note 1 above, para. 5.21.

⁶¹ Contrast Cherry, "Interim Payment And Provisional Damages" [1993] (1) *Quantum* 6.

⁶² (1993) 9 *Personal and Medical Injuries Law Letter* 18.

separated spouse.⁶³ There is also discussion of whether it might be used to settle breach of contract claims in employment cases,⁶⁴ and to provide a means for the parties to settle environmental damage claims, especially if the cost of cleaning up the pollution is high and the work involved likely to take some time.⁶⁵ The possibility of structuring environmental damage claims is already being investigated in this country. Any long-term obligation to continue to provide care and support, even if not in a personal injury context, is likely to attract the attention of those at the forefront of the development of structured settlements.⁶⁶

The Law Commission made no detailed comment upon the extension of structuring into these new areas because its focus was upon personal injury cases. However, it did note that the victims of other torts are less likely to have continuing long-term future needs, and that preferential treatment for them might be less justified.⁶⁷

CONCLUSION

In looking at the ways in which encouragement can be given to litigants to use structured settlements, it is essential to understand the present legal regime which imposes restrictions upon the use of the new form of compensation. The legal rules involved are complex and bring together difficult issues of civil procedure, tax and insurance law as well as the substantive law of tort. There is a considerable amount of confusion as to the limits these rules impose upon structures, and it is hoped that the analysis offered here clarifies the issues involved. In particular, the article has sought to relate the theoretical constraints imposed by the law to the realities of structured settlement practice.

⁶³ F. McKellar, *Structured Settlements: A Practitioner's Manual*, p. 33, and Gross and Campbell, "The American Experience" in I. Goldrein and M. de Haas (eds.), *Structured Settlements* (1993), p. 232.

⁶⁴ Winslow, "Structured Settlements in Employment Litigation", *Los Angeles Lawyer*, April 1988.

⁶⁵ Kagels, "Structured Settlements under Superfund" (1992) 4(3) *Environmental Claims J.* 349; Gross and Campbell, *op. cit.*, p. 230. The National Structured Settlement Trade Association estimates that over the next 10 years or so structures for environmental claims could exceed those for personal injury.

⁶⁶ Further developments are signposted by Middlemass, "Structured Settlements" (1992) *Canadian Lawyer* (Dec. issue) 41.

⁶⁷ *Op. cit.* note 1 above, para. 3.87.