Qualified Settlement Fund Sequence

The use of a QSF involves a few more documents than a settlement where the defendant makes the qualified assignment, but it protects the claimants from the common abuses practiced by the defense and gives the attorney assurance that his or her client will have no grounds for a legal malpractice suit because the defense was allowed to invade the plaintiff's privacy or commit fraud. Many of these same steps occur even when the original defendant or insurer makes the qualified assignment and there is no QSF. Although this is a typical sequence of events, facts and circumstances of a particular case may dictate otherwise.

• Agreement to Create the QSF (468B Trust)

The QSF can be initiated by either side. For purposes of this illustration, it is initiated by the plaintiff, through the plaintiff's attorney. An attorney who specializes in QSF documentation should be engaged, as one set of forms does not necessarily fit all. An administrator (trustee) is selected (often the QSF attorney). Earnings of the QSF, which otherwise would be taxed to the QSF, can be applied toward the attorney and administrator fees without costing the plaintiff.

• Creation of QSF Trust Agreement

The Trust Agreement pertains only to the QSF administrator, the plaintiff, plaintiff's attorney and the court. It often is not filed, but is submitted to the court for its *in camera* review.

• Petition or Motion to Establish the QSF

Plaintiff petitions the court to establish the QSF. Sometimes this is done *ex parte*, as the opposing party should not have standing to object. This does not need to be the trial court, as a probate court may be better suited to exercise jurisdiction if the settlement is being made on behalf of an estate, minor or protected (incompetent) adult. A QSF may be established by any entity of government, including but not necessarily a court.

• Order Establishing the QSF

The order should contain all elements prescribed in 26 CFR § 1.468B-1 necessary for a QSF. It should approve the QSF Trust Agreement and the appointment of the administrator.

• Petition or Motion to Approve Settlement Between Defendant(s) and Plaintiff(s)

If any claim is being made on behalf of an estate, minor or protected adult, approval is necessary by the court having jurisdiction. Plaintiff petitions the court.

• Order to Approve Settlement Between Defendant(s) and Plaintiff(s)

If court approval is required, order approves total cash amount being paid by defendant(s). Allocation among plaintiffs and to lienholders is not usually made at this time. For confidentiality, order may omit reference to settlement amount, referring to settlement agreement, which may be reviewed *in camera* and not filed or else filed and sealed.

• Application for Federal Tax ID Number (EIN)

This step to obtain an Employer Identification Number (EIN) from the IRS is taken by the administrator, who then provides an IRS Form W-9 on behalf of the QSF to the plaintiff's attorney to be forwarded to the defendant or liability insurer (through defense counsel). This is the only tax ID number that should be given to the defense, as the QSF will be the only payee from the defendant or insurer.

• Establish QSF Bank Account

This is also done by the administrator, subject to court order establishing QSF. Use of a bank where the plaintiff's attorney has an established relationship can be perceived as the exercise of control over QSF funds on behalf of the plaintiff and is discouraged. Court maintains oversight on QSF.

• Settlement Agreement and Release Between Defendant(s) and Plaintiff(s)

It usually works best if the defense prepares the initial draft of the release, as a cash settlement, as it will be presumed to contain the release language required by the defense. The QSF attorney should always review this document to see that it does not contain any problematic language that might jeopardize tax benefits and that the agreement is to be signed by all parties, not just plaintiff(s), inasmuch as it will contain stipulations and promises. Essentially, the parties agree to the sufficiency of the money the defendant or its insurer will *spend for the benefit* of (not *pay to*) the plaintiff(s), paid to the QSF, in exchange for the release and dismissal with prejudice of the defendant. The QSF becomes the substitute defendant by novation and assumes the ability of the original defendant to make a 26 USC § 130 qualified assignment of a periodic payment obligation created in the settlement agreement.

• Settlement Check or Wire Transfer from Defendant(s) or Insurer

Must be able to be deposited directly by administrator into QSF. Defendant(s) or insurer reports payment amount to IRS using QSF's EIN, which has been provided on Form W-9. Transferor gets current year tax deduction per 26 USC § 461(h).

• Dismissal with Prejudice

The original defendant(s) are completely released and dismissed from the tort liability. There is no legitimate reason for the defense to refuse to cooperate. Whatever form is used for the Dismissal with Prejudice, it should dismiss only the released parties from the plaintiff's cause and not the cause itself, as the cause will remain alive with the QSF being liable. If the cause is dismissed, a trial court may lose its jurisdiction to oversee the remainder of the transaction and the plaintiff has nothing to give up as consideration for receiving payments from the QSF when the subsequent agreement with the QSF is executed.

• Settlement Agreement and Release Between QSF (Releasee) and Plaintiffs (Releasors)

Not to be confused with the earlier settlement agreement between plaintiff(s) and original defendant(s). This agreement should bear a different name than the earlier release. Does not involve released defendant(s). Need not be filed with court. Makes allocations of QSF assets, promises periodic payments, etc.

• Qualified Assignment, Release and Pledge (Assigning the Periodic Payment Obligation)

Structured settlement broker prepares using uniform or model document and payment amounts from annuity quote. Assignor is QSF administrator, per Rev. Proc. 93-34. Attorney fee may also be structured; separate qualified assignment is prepared. Defense is not involved in selecting broker or annuity issuer. Participation of defense broker would constitute a beneficial interest of transferor in QSF assets.

• Petition or Motion for Order Approving the Settlement (if estate, minor or protected adult), Ordering Distribution of QSF Assets, Releasing QSF, Dismissing Cause and Administrator, and Terminating QSF

Original released defendant(s) should not be involved, or even be required to receive notice, as they are no longer a party. QSF administrator must receive notice, as QSF is now a party, but administrator may waive appearance.

• Order Approving the Settlement (if estate, minor or protected adult), Ordering Distribution of QSF Assets, Releasing QSF, Dismissing Cause and Administrator, and Terminating QSF

May be accomplished in separate orders, especially if the court overseeing the QSF does not have jurisdiction over the tort claim. For confidentiality (including from original defendants), details of the settlement, such as allocation among plaintiffs, periodic payment details, etc., may be omitted from the order, referring to the settlement agreement and qualified assignment, which are reviewed *in camera* and not filed or else filed and sealed. QSF is released and indemnified then terminated. Administrator is dismissed after Form 1120SF tax return is filed.