Structured Settlements 101: How Structured Settlements Work

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Sample of Content:

An overview of structured settlements, including what they are, how they're used, benefits, drawbacks, and consumer tips.

Content:

You have probably heard the term â€œStructured Settlementâ€• on a television or print ad and wondered what it meant. After all, the term is not a part of our everyday lexicon.

A structured settlement is a contract under which an insurance company undertakes to make periodic payments to an injured party as part of a bodily injury claim settlement or to a surviving family member to whom a large settlement has been awarded. These are just two examples of where a structured settlement might be used. Structured settlements have become popular because they offer substantial benefits to all parties involved in the settlement agreement.

A brief review of the dictionary reveals the following definition: a structured settlement is simply a financial package that permits a settlement to be paid in regular payment installments for either a set period of time or over a lifetime. In short, a structured settlement is a package that is tailor made for the individual or payee by the payer or an interested third-party. Some structures include immediate payment to cover any special damages that may have occurred or will occur.

The system of structured settlements was first introduced in Canada in the early 1970â€™s and spread into the United States very quickly. Within a few years, the idea had found its way to many countries including Australia and most member states of the European Union.

Benefits of a Structured Settlement

A structured settlement annuity provides a payment stream that is tax-free over a determined period of time. Most investment options such as stocks and bonds, real estate, savings accounts, and similar vehicles simply cannot match the flexibility and security of a Structured Settlement Annuity.

Another benefit of a structured settlement annuity is that it can be designed so that payments are made over an extended period of time, even throughout the life of the payee. In the event of the recipient's death, a guaranteed portion of the settlement may be paid to the person's estate or to a named beneficiary.

Structured Settlements have become quite common and offer the additional security of regulation by both Federal and State statutes. There are also provisions in IRS and Medicare/Medicaid guidelines which take them into account.

Alternatives to Structured Settlements

Itâ€™s quite easy to see that a structured settlement can work to the advantage of all parties in a variety of circumstances. However, there are occasions when the beneficiary of a structured settlement would prefer not to have periodic payments, preferring instead a lump sum payment. Such might be the case where an individual would like an amount of money to purchase a home, perhaps to cover large medical bills or to pay off a mortgage.

This option has also proved especially popular with lottery winners. There are a number of insurance companies and others that provide this service for a fee. In such instances the insurance company or another interested third-party makes the lump sum payment with a charge for expenses and interest deducted. It is important to consider these fees and read the fine print carefully to be sure that you are not signing away the bulk of your payment.

How do the alternatives work?

The settlement contract is sold to a financial institution which then accepts the periodic payments from the payer and gives the beneficiary a lump sum. Commonly, the financial institution involved will be another major insurance company.

The insurance company charges a handling fee which will usually be calculated to take into account adjustments for interest charges and handling costs. Again, if you are considering taking this option you must bear in mind that the company buying the payments for a cash sum is in business to make money. The amount of the one-off payment will certainly be considerably less than the gross amount that would have been received over the original extended period.

Unless the amount of the lump sum is very substantial and the recipient can be sure of consistent investment income, itâ€™s almost certainly going to be better to stick with the original arrangements. An exception might be where the recipient is a younger person in good health with a substantial expectation of gainful employment for the long term.

Again, as with any contracts be sure to read and understand the terms of the agreement you are making. Make a list of questions and ask until you understand. It is also a good idea to cast a wide net when looking for an alternative to structured settlements as fees and services and thus your bottom line can vary greatly.

Adam Short is freelance writer and creator of http://www.structuredsettlementinfo.info - a site providing the latest news and information on structured settlements.

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