TAB 3

Structuring The Settlement With An Eye To Capacity Issues

Dale Orlando
McLeish Orlando LLP

Alison Keagan
McLeish Orlando LLP

Personal Injury and Mental Capacity Law
Strategies for Claims Involving Incapable Parties

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CONTINUING LEGAL EDUCATION

STRUCTURING THE SETTLEMENT WITH AN EYE TO CAPACITY ISSUES

By Dale V. Orlando & Alison Keagan, McLeish Orlando LLP

Personal Injury and Mental Capacity Law –
Strategies for Claims Involving Incapable Parties

Introduction

Knowing when to settle a personal injury claim and on what terms is a challenge and will vary with each case. However, getting the settlement funds flowing to your client, who has suffered a serious brain injury and may lack capacity to make decisions, is a bigger challenge. At a time when courts are scrutinizing settlements of claims involving persons under disabilities, under Rule 7.08 of the *Rules of Civil Procedure*, it is important that plaintiff's counsel always be aware that they will have to answer to the court when asking for approval of the settlement at the end of these types of cases. As Court of Appeal stated in *Tsaoussis (Litigation guardian of) v. Baetz*,

> Proposed settlements of ... personal injury claims, ... with head injuries, raise real concerns about the adequacy of compensation provided by those settlements. The risk of under-compensation in those cases is very real. That risk demands that the court vigorously exercise its *parens patriae* jurisdiction when asked to approve a settlement.[1]

The purpose of this paper is to discuss settlement of personal injury claims involving clients with capacity issues and specifically, when to settle the claim, when to structure the claim and also to provide you some practical tips to speed up the process of obtaining court approval of the settlement.

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[1] [1998] O.J. No. 3516 (C.A.).

When to Settle the Claim

"Settlement efforts should be undertaken when your case is at its strongest and/or the defendant's position is at its weakest."[2] The time to settle a claim will be different for each case and will depend on whether it is a tort claim or an accident benefits claim or both. The one advantage of settling the accident benefits claim before the tort claim is your client will receive a lump sum of money, without having to wait for their case to proceed through the litigation process. Presently, the earliest date some Ontario Superior Courts are scheduling trials to commence is 2011. However, the decision to settle the accident benefits claim must be considered with section 267.8 (1),(4),(6) of the *Insurance Act*. These sections require a plaintiff who recovers damages at trial for past and future loss of income, loss of earning capacity, health care expenses and other pecuniary costs to have their damages reduced by the amounts already received before the trial for certain collateral benefits, such as:

1. Income loss and loss of earning capacity by way of statutory accident benefits, sick leave plan through employment and any other income continuation plan.

2. Health care expenses received by way of statutory accident benefits or other medical, surgical, dental, rehabilitation of long term care plan.

3. Other pecuniary losses other than income loss and health care expenses.[3]

Similarly, section 267.8(9) requires that the plaintiff hold in hold in trust for the benefit of the defendant amounts received after the trial for the same benefits mentioned above.

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[2] Roger G. Oatley & John A. McLeish, "*The Oatley-McLeish Guide to Personal Injury Practice in Motor Vehicle Cases*", looseleaf (Aurora, ON: Canada Law Book, 2007) at p. 33-1.
[3] *Insurance Act*, R.S.O. 1990, c.I.8, Part VI , s. 267.8(9).

In some cases, these collateral benefits will have a significant value. This is particularly the case with a catastrophically injured client that has significant ongoing medical, rehabilitation and attendant care needs that are being met by the accident benefit insurer. The value of these past and future benefits will have to be considered when determining the amount that you will accept as a final settlement of your client's accident benefits, otherwise the tort defendant may allege you made an improvident settlement and ask for a significant discount on damages.

The allegation of an improvident settlement of an accident benefit claim was discussed in *Morrison v. Gravina*.[4] In *Morrison v, Gravina*, the plaintiff settled her past and future accident benefits for $20,914.00 and then proceeded to trial with her tort claim. At the conclusion of the trial, the jury awarded the plaintiff damages for past loss of income. The defendant brought a motion arguing that the award should be reduced by the improvident settlement of the plaintiff's income replacement benefits, which she settled for $0. The plaintiff advised the court that she had applied for income replacement benefits and non-earner benefits several times before she settled her claim, but the accident benefit insurer denied her claim for those benefits. The settlement of $20,914.00 reflected her entitlement to past and future medical rehabilitation benefits.[5]

In determining that the plaintiff had not made an improvident settlement, the court held that the onus was on the defendant to show the plaintiff had settled her accident benefits in "bad faith", that is, she settled the claim with an "ill will or an improper or illegal design" so as to deceive the accident benefits carrier.[6] The court also made reference to section 267.8 (21) of the *Insurance Act*, which provides that a collateral benefit shall be deemed not to be available to a plaintiff

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[4] [2001] O.J. No. 2060 (C.A.).
[5] *Ibid.*
[6] *Ibid* at ¶ 49, 50.

if the plaintiff made an application for the payment and the application was denied.[7]

The courts have held that section 267.8(21) does not apply to future entitlement to accident benefits.[8] However, the tort defendant is entitled to an assignment of future accident benefits upon settlement of the claim or, more commonly, the tort defendant will ask for a discount in exchange for allowing the plaintiff to retain the rights to their accident benefits claim. Therefore, it is always good practice when you are considering settling your client's accident benefits claim before the tort claim, that you properly value your client's potential future accident benefits and ensure that your client has applied for those benefits from the accident benefit insurer that your client is claiming in the tort action. Otherwise, the defendant could ask for a significant discount for those benefits.

A. Accident Benefits Claim

The accident benefits claim is supposed to be non-adversarial. Unfortunately, the accident benefits claim is often the most adversarial aspect of a person's claim following a motor vehicle collision. Many accident benefits adjusters have become jaded as a result of dealings with real and perceived fraudulent claimants. As a result, they choose to deal with all claimants as if they are advancing a bogus claim. Some insurance adjusters will put your client through the proverbial wringer before paying the benefits that are properly owed, creating uncertainty and inconvenience in the life of the client. As a result, your client will often instruct you to approach the accident benefit carrier for a lump sum settlement of their future entitlement to accident benefits.

There is no way for you to force an insurance company to pay a lump sum settlement of their future entitlement to accident benefits. Often times, you will

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[7] *Insurance Act*, R.S.O. 1990, c.I.8, Part VI , s. 267.8(21).
[8] *Peloso v. 778561 Ontario Inc.* [2005] O.J. No. 2489.

end up filing a lawsuit against your client's accident benefits insurance company for benefits, such as in a situation where the insurance company stops paying income replacement benefits and your client is not yet able to return to work. In these types of cases, all that you can hope to do is win the lawsuit and have a court order the insurance company to pay the arrears of benefits owed. The court cannot order the insurance company to pay the benefits for a fixed period of time into the future.

However, insurance companies, like their insured, also have a need for certainty. By settling a person's claim for past, present and future accident benefits for a set amount, the insurance company is able to close their file for a set sum of money without the fear of additional claims being made in the future. For the insurer, a closed file is a good file. They no longer have to staff the file with an insurance adjuster. They eliminate their future exposure to the costs of medical examinations. They remove the risk that the relationship with the insured person will deteriorate to the point that litigation is commenced, along with all of its associated costs.

If counsel is considering pursuing a lump sum settlement on behalf of their client, there are certain preparations that need to be made before entering into settlement negotiations with the insurance company. You must remember when acting for the plaintiff in a personal injury claim that an injured person is in a recovery/healing mode for approximately two years. If it is premature to obtain a prognosis for the future, it is too early to consider a lump sum settlement of your client's future accident benefits claim.

Once your client's condition has stabilized and a future prognosis is obtained, the next step is to retain a reputable expert to prepare a long term needs and cost analysis. This report will examine the medical, rehabilitation and attendant care benefits that your client will likely require over the remainder of their claim. In catastrophic injury claims, your client has a lifetime to claim these

types of benefits, subject to a million dollar maximum for medical and rehabilitation benefits and an additional million dollars for attendant care benefits.

In order to consider what an appropriate amount would be for a cash-out of your client's accident benefit entitlement, you should request what is referred to as a "burn rate" letter from the insurance company to determine the total amount that has been paid to your client under each section of the Statutory Accident Benefits Schedule and the rate at which benefits are being paid by the insurer.

In addition, it is appropriate to determine how much to discount the total future exposure on the accident benefits claim. There is a time value to money and an appropriate discount, usually 1.5% - 2.5% per year for indexed benefits or benefits paid as incurred, is applied to account for the future stream of payments that will be paid up front to the injured person. If the benefit being considered is not indexed for inflation, like income replacement benefits, a 5-6% discount rate is more appropriate.

An insurance company may also want other factors considered in determining the discount amount. For example, in almost all cases the insurance company will look at the life expectancy of your client. If you have an elderly person, who is catastrophically injured and the prognosis for recovery is poor, the insurance company will want the discount rate to reflect this. Another factor the insurer will consider is the rate at which your client is claiming benefits at the time you attempt to settle the claim. For a variety of reasons, people do not claim benefits that they may be entitled to claim at the time of the settlement. Sometimes their condition improves, or they move away and it becomes inconvenient to continue to claim benefits, or they simply get worn down by the process and give up. Nonetheless, the insurer will ask for a discount for this factor.

For the above reasons, an insurance company will not pay their full exposure on an accident benefits claim. Depending on the significance of the above noted factors, insurers will demand a discount of 25 to 50 percent. After a period of negotiations, the discount will be in the area of 5 to 25 percent. If the discount demanded is too high, it is not in the best interests of the client to settle their claim.

B. Tort Claim

While every tort claim should be organized and prepared as though it is going to trial, the reality is that most tort claims settle at some point after examinations for discovery and before trial. The key consideration in positioning a tort claim for settlement is risk assessment. A properly thought out offer to settle will increase the risk to your opponent, making it difficult for them to justify going to trial.

For example, the first form of settlement to consider in any tort case is the formal offer to settle in Rule 49 of the *Rules of Civil Procedure*, which has cost consequences for failure to accept the offer. While on the face of it, it would seem that it is advantageous to serve a formal offer early on, there are practical considerations that affect the timing of the settlement offer. When acting for the plaintiff in a personal injury case it is important to remember that an injured person is in a recovery/healing mode for approximately two years. During this time a medical prognosis, and other reports that build on the prognosis, cannot likely be obtained. Without reports like vocational assessments, future cost of care reports and economic loss reports, the amount contained in a formal offer to settle may be no more than a guess. Until damages have been accurately assessed, it is not practical to serve an offer.

In cases where your client's damages will exceed the insurance policy limits that are responding to the claim, you should consider making an offer to

settle within the limits of the insurance policy. However, before making the offer to settle, you should ensure that there are no other assets to pay the damages in excess of the insurance policies or that it will be very onerous and costly to collect on those assets. As well, you should include as a term of the settlement that the defendant has no right to an assignment of the accident benefits until judgment has been paid in full.

The advantage to the plaintiff in the above scenario is they will receive their settlement funds immediately without having to attend a trial, obtain a judgment against the defendant and collect on the judgement in excess of the insurance policy by seizing personal or business assets of the defendant. Similarly, the advantage for the defendant in accepting this offer is it limits their personal exposure to damages and costs. The advantage to the insurer is they will have settled the claim and perhaps saved a small amount on their insurance limits. Further, an offer to settle within the insurance limits puts pressure on the insurer to accept because, if they do not accept, then they can be exposed to a claim of bad faith by the defendant should the result at trial exceed the available insurance limits. Where such an offer is made and the insurer decides to go to trial in an attempt to minimize its liability, it is said the insurer has put its interests ahead of the insured.

Also, if it is expected that a case will be mediated, you may want to delay delivery of an offer to settle until the conclusion of the mediation. It seems that there is an expectation at mediation that there will be several rounds of offers and the plaintiff will compromise considerably from their initial settlement position. If this pattern is not followed, you may be faced with the assertion that you are not "bargaining in good faith". If you have delivered a settlement offer that is an accurate assessment of the higher end of the reasonable range of damages, you will not have left yourself with enough bargaining room to satisfy some defence counsel and mediators.

One of the most powerful strategies for settling cases with multiple defendants is a Mary Carter agreement. Before discussing possible scenarios where this type of agreement is useful, it is necessary to first define the characteristics of a Mary Carter agreement.

A Mary Carter agreement is essentially a contract between the plaintiff and at least one of two or more co-defendants. The contracting defendant advances settlement monies to the plaintiff, but the plaintiff agrees to repay the contracting defendant a percentage or portion of those funds from any recovery against the other party or parties. The contracting defendant remains in the lawsuit. The effect is to make the plaintiff and the contracting defendant partners in attacking the other defendant(s).

The court was called on to analyze the propriety of a Mary Carter agreement in *Pettey v. Avis Car Inc.* and came to the conclusion such an agreement is valid, provided it is disclosed to the court.[9] The only element of the agreement that is not required to be disclosed to the court (and the non-settling defendant) is the dollar amount to be paid. It is important to remember the disclosure obligations when drafting the agreement. Language such as "... co-operate to establish liability against defendant X" should be avoided. Otherwise, the only limitation on the features of the agreement is the needs of the contracting parties and the imagination of counsel.

Most Mary Carter agreements grow partially from the needs of the contracting parties, but more significantly from the mutual desire to eliminate the potential for the unexpected but possible bizarre results that sometimes occurs with jury verdicts. Fear of the unknown is a powerful motivator in encouraging settlement. Typically, the plaintiff is concerned about proving liability or establishing their claim in damages, whereas the defendant is motivated to cap their total exposure and is prepared to pay a price to do so. Once again it is all

[9] (1993), 13 O.R. (3d) 725 (Gen. Div.).

about an assessment of the risks and minimizing those risks where possible. The beauty of Mary Carter agreements becomes obvious when one considers the impact on the parties after the agreement is reached.

One of the most attractive features of a Mary Carter agreement is that it positions both the plaintiff and the contracting defendant into a win-win situation. The plaintiff is assured a meaningful recovery, minimizing any risk associated with trying the case to the conclusion. The contracting defendant has capped its exposure to damages and costs. Consequently, the contracting defendant is free to make an effort to recover some of its loss without any risk of exposure to a bad faith claim from the insured.

Another benefit of this type of agreement is the direct impact on the parties in the courtroom after the agreement is announced to the court and the non-contracting defendants. Namely, the most exposed defendant who has taken the lead on defending the damages claim is no longer taking a position on damages. As a result, the other defendants are left without the ally they were counting on to assist in trying to minimize damages. Even more disconcerting to the non-contracting defendants is the fact the plaintiff and the contracting defendant are allies whose focus at trial is to succeed against them.

To summarize, Mary Carter agreements are genius when it comes to minimizing risk of the contracting parties. They also serve to put non-contracting defendants in the unenviable position of being forced to settle or face a large risk in going to trial. Essentially, the non-contracting defendants are backed into a corner. That being said, there are some cases that are more conducive than others to this type of agreement.

When to Structure the Claim

If you are trying to resolve a claim that involves a client that does not have capacity and the claim is likely to exceed $100,000.00, you should consider structuring the settlement. A structure is an alternative to a lump sum settlement. Rather than parties settling a matter and forwarding a lump sum payment to the client or their guardian, the settlement funds are either all or in part, paid to a claimant by means of periodic payments.

Much of the impetus to develop a periodic payment scheme arose as a reflection of the need to secure the payments for the benefit of those who are unable to manage their own affairs. For example, once the money is put into the structure, it cannot be taken out, other than in accordance with the payment schedule. This feature provides significant safeguards to people who may otherwise suffer at the hands of a well meaning or not so well meaning family member or friend who has a "great" investment opportunity. Because of this significant safeguard, structured settlements are becoming the preference of the court when approving settlement of claims involving persons under disabilities.

In addition to the safeguard mentioned above, there are some other significant advantages to structuring some or all of a settlement. A structure reduces the risk that that your client might outlive their settlement monies. The consequences of living longer than expected for someone who has major medical needs and limited or no earning capacity, are disastrous. Most structures for seriously injured clients are based upon life annuities. With a life annuity, your client cannot outlive their settlement fund; the structure will pay for as long as they live for however long that may be.

Another advantage of a structure is it protects your client from losing their settlement monies because of bad investment decisions. For virtually any investment, other than products like a Government of Canada bond, there is a

risk that the investment may perform badly. Stock markets have been known to crash, mutual funds often experience losses, particularly over the shorter term and even real estate markets have boom and bust periods. On the other hand, with a structured settlement, all of the future payments are guaranteed at the time of the settlement.

Lastly, a key advantage of the structured settlement compared with a lump sum settlement is it is tax-free. This benefit is especially significant in cases involving serious brain injuries that put clients in the high marginal tax brackets. The important distinction is that while a lump sum payment is tax-free when initially received, any income which that money generates is taxable to the client. By contrast, all structure payments are tax-free to your client, despite the fact that the structure has both a principal and an interest element.

A structured settlement should be tailored to meet the unique circumstances of your client's needs today and for the remainder of their life. Therefore, it is important to retain a reputable company who has experience with structured settlements, such as McKellar Structured Settlements, to review the relevant documents and develop different structures that fit your client's financial needs. You should retain your structured settlement expert after you have received all your medical, future care and economic loss reports, but before you begin settlement negotiations. At this point in the case, you will have an understanding of your client's present and future needs and losses and your expert can provide different scenarios for a structured settlement based on the medical and economic loss reports. As well, if you are successful in settling your case, then you can insist as part of the terms of settlement that the funds be structured by your expert.

There are several different options that must be considered when deciding on a structure. The most basic structure is one in which a certain amount of money is invested and the structure pays out a fixed monthly amount for the

lifetime of the claimant. This option will yield the highest monthly payment, but is unlikely to be the most suitable option for the injured person. Your client may decide to vary the start date of payments from the structure, the duration of payments from the structure and the size of the structure payments from time to time. For the most part, people select a payment period that ends with their death. Once these options have been decided upon, an appropriate guarantee period must be decided upon. A guarantee period refers to the length of time that the structure pays out at a minimum, regardless of the death of the claimant.

Most insurers will insist on a specific guarantee period and a reversionary interest in the structure. This means that if the person passes away during the guarantee period, the structure will continue to pay for the remainder of the guarantee period. However, the payments will be made to the accident benefit insurer. Whether the insurer is entitled to a reversionary interest in the structure is often a point of negotiation since many people wish to create an estate for their dependants should they die before the expiry of the guarantee period. This is obviously not accomplished if the structure payments revert back to the insurer. Recently, some companies are offering double reversions, meaning the structure payments will continue to both the accident benefit insurer and to the survivors of the injured person, for the remainder of the guarantee period.

How to get the Settlement Funds Flowing to your Client

Severely injured clients, such as persons who have suffered a serious brain injury, usually need to begin drawing an income from their settlement immediately in order to meet their needs. This is especially true if you settle the accident benefits claim and the accident benefit insurer had been paying monthly income replacement and attendant care benefits to your client. However, the *Rules of Civil Procedure* make it clear that any final settlement of an entitlement to a person who is a minor or who lacks capacity as a result of a brain injury or

some other reason has to be approved by the court. This involves making an application to the court, providing a detailed breakdown of how the settlement was arrived at and disclosing the lawyer's legal fees on the file, all of which takes several weeks to compile into affidavit evidence.

The job of the court is to ensure that the settlement is in the best interests of the injured person and that the lawyer is charging a fair amount for the services that they have provided. However, reconciling the immediate needs of your client, with the lengthy court approval process is a growing challenge for plaintiff personal injury lawyers.

If you know in advance of the mediation or settlement negotiations that your client will most likely receive a large settlement, and that it will take months to get court approval of the settlement, then consider asking for an advance payment from the insurer. Although advance payments still require court approval, as long as the advance payment is under $100,000 and no lawyer's fees will be paid out of the advance payment, your client will receive this payment much quicker then preparing and waiting for court approval of a large final settlement.[10] This advance payment will bridge the gap between the time your client's case settles and you obtain court approval of the final settlement.

It is possible to have funds transferred into a structured annuity while awaiting court approval of the settlement. However, Justice Wilkins provided the following cautionary comments about this practice:

> By further comment, I would note that there now has developed a process of taking the money and paying it into a structured annuity prior to the court approval, or setting monies aside prior to the court approval, or in other words, embarking upon steps related to disposition of funds prior to approval of the settlement itself, let alone approval of how those funds should be distributed. In the event that it is in the best interests of the person under a disability for these steps to be undertaken, it is my view that satisfactory information should be placed before the approvals judge in order to explain what was done and why, as well as how it is in the

[10] *Carter et al. v. Junkin et al.* (1984), 47 O.R. (2d) 427; *Marcoccia v. Gill,* [2007] O.J. No. 12.

> plaintiff's best interests. Included in this information, in my view, should be the amount of the commission being charged by the structured settlement broker if that commission reduces the amount of money available to make payments on behalf of the plaintiff under a disability. In my view, the Court should know how much that commission reduces the stream of payments in the annuity.[11]

In addition, Justice Wilkins suggested that one judge be seized of all the court approval steps involved with persons under disabilities, including approval of the monetary sum of the settlement, the appointment of the guardian as to property, the disposition of the funds and the management scheme together with a scheme of reporting, which could add to the delay of getting settlement funds to your client.[12] His honour concluded:

> Rule 7.08 and the provisions of the applicable statutes require that there be a serious consideration by a judge of all of the various steps necessary to complete the settlement in total. Justice, fairness and the protection of the person under a disability require that the provisions of rule 7.08 be followed. Failure to have the entirety of the completed settlement process placed before the same judge at the same time could, in some circumstances, work to the disadvantage of a plaintiff under a disability and create a circumstance involving an inappropriate result. The Court, in my view, should err on the side of protecting the person under a disability and although it may require more time effort and expense, it is my view the Court should require compliance with the rule.[13]

Given the uncertainty created by the decision of *Marcoccia v.Gill*, and those court decisions that have followed, there are not a lot of steps that counsel can take to get the settlement funds flowing to your client before obtaining court approval. However, the following are strategies that may help speed up the process of obtaining court approval of the quantum and structure of the settlement:

a) Obtain court approval of your retainer agreement or contingency fee arrangement at the commencement of litigation;

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[11] *Marcoccia v. Gill*, [2007] O.J. No. 12 ¶ 25.
[12] *Ibid* ¶ 21.
[13] *Ibid* ¶ 25.

b) Obtain a capacity assessment of your client at the commencement of litigation or as soon as you become aware that capacity may be an issue in the case;

c) Appoint a Guardian of Property to manage your clients financial affairs at the commencement of litigation; and

d) Retain a firm with expertise in the area, to assist you with the court approval process, including an estimate of the future guardianship fees and legal fees, immediately after settlement.

Conclusion

The growing uncertainty and lengthy process of obtaining court approval of settlements of persons under disabilities can be an impediment to getting settlement funds flowing to your client. The goal of this paper was to provide you with some strategies on when to settle and how to structure these types of personal injury claims to maximize your client's settlement monies. However, until there is further direction from the courts, counsel should be cautious about trying to find alternative ways to get settlement funds flowing to their clients before obtaining court approval.