

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/CS/SB 108

SPONSOR: Judiciary Committee, Banking and Insurance Committee and Senator Geller

SUBJECT: Structured Settlements

DATE: March 20, 2001

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Johnson</u>	<u>Deffenbaugh</u>	<u>BI</u>	<u>Favorable/CS</u>
2.	<u>Forgas</u>	<u>Johnson</u>	<u>JU</u>	<u>Favorable/CS</u>
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

Structured settlements are increasingly being used as means to settle personal injury claims. The structured settlement provides periodic payments for future medical expenses and wage replacement. As an alternative to continuing to receive these long-term payments, some individuals may assign or sell their settlement payments to a factoring company for a discounted, lump-sum payment. The bill would require court review and approval for all such transfers of structured settlements for the resolution of tort claims. Since s. 440.22, F.S., prohibits the assignment, release, or commutation of compensation or benefits due or payable under this chapter, this bill would not apply to workers' compensation structured settlements. In addition, the bill would require such transfer agreements to contain specific disclosures regarding the costs of the transactions and a comparison of the amount to be received in the transfer in comparison to the amount to be received through the structured settlement.

This bill creates yet to be designated sections of the Florida Statutes.

II. Present Situation:

Structured Settlements

A structured settlement is an arrangement to satisfy a legal liability, which involves the periodic payment of money through an annuity (or other financial product). Under a structured settlement involving an annuity arrangement, one party pays a lump sum premium to an insurance company to purchase an annuity in the name of the claimant. The premium varies depending on the number and length of payments. The insurance company then makes periodic payments to the claimant for the negotiated period of time.

The use of structured settlements has increased in recent years for wrongful death or injury awards. According to the *Wall Street Journal*, the total amount of structured settlements has

reached \$5 billion. A structured settlement may be agreed to in a pre-trial settlement or it may be required by a court order, particularly in the case of judgments involving minors.

Structured settlements are commonly used as an alternative to simple lump sum settlements. Structured settlements can offer some advantages to both parties involved in the settlement. For claimants, a structured settlement can provide long-term financial protection and income, which may be necessary for claimants with long-term medical needs and dependents. Also, money paid to a claimant through a structured settlement receives more favorable federal tax treatment. Unlike investment earnings on a lump sum payment, which are taxable, payments made under a structured settlement are not taxable. However, claimants must weigh these advantages against the disadvantage of not having access at any one time to the entire amount of money received in the settlement.

For the paying party, structured settlements can provide a more cost effective means of extinguishing the legal liability. For example, a \$2 million lump sum payment would cost \$2 million. However, \$2 million paid over time through a structured settlement might be accomplished through purchasing an annuity that costs only \$500,000 -- a savings of \$1.5 million.

Transfer or Factoring of Structured Settlements

In recent years, concerns have been raised regarding the transfer or factoring of structured settlements. Settlement purchasing companies, also known as "factoring companies," buy the remaining payments due under the settlement in exchange for a smaller lump-sum payment. According to the American Insurance Association, typically the person receiving the payments requests a change of address to the life insurance company that provided the annuity for the periodic payments. The new address is actually the address used by a settlement purchasing company that then endorses and cashes the checks. Since neither the life insurance company nor the property-casualty insurance company knows a settlement has been purchased, it can violate the contractual terms of the settlement or annuity or state laws. It is conceivable that an insurer could end up paying twice for the same settlement.

Since 1983, the Internal Revenue Code has contained a series of special tax rules intended to facilitate the use of structured settlements to resolve personal injury claims. One of the requirements for this preferable tax treatment is that the periodic payments cannot be accelerated, deferred, increased or decreased by the injured person. According to the Department of Treasury testimony before Congress in 1999, the transferring of structured settlements undermine the policy objective underlying the structured settlement tax regime of protecting the long-term financial needs of injured persons. The factoring transaction also effectively contravenes the statutory conditioning of favorable tax treatment to the various parties to the arrangement on the injured person's inability to accelerate such payments. According to the Department of Treasury there have been reports of heavily discounting in the range of 16-75 percent by certain factoring companies. It was noted that, although almost all structured settlement arrangements contain anti-assignment clauses that are intended to satisfy the Internal Revenue requirements regarding settlements, many factoring companies are willing to contravene these anti-assignment clauses and purchase such settlements.

In addition to the insurer's potential additional liability for the settlement, the long-term financial security of the injured claimant is at risk, if the claimant does not understand the terms or consequences of such a financial transaction. Although the individual is provided with a lump-sum payment, the amount of the payment may not meet the long-term medical costs, living expenses, and dependent financial support the individual ultimately needs. However, due to changes in an individual's circumstances, a lump-sum payment may meet their current needs.

According to the National Structured Settlement Trade Association, 12 states (California, Georgia, Maine, Missouri, Illinois, Minnesota, Kentucky, Connecticut, Virginia, West Virginia, Pennsylvania, and North Carolina) have enacted laws that are designed to protect consumers engaging in these types of transactions by requiring specific disclosures regarding the costs of such agreements and requiring court approval prior to such a transfer. North Carolina places limitations on the discount rate, fees, and commissions associated with a transfer. Some states have adopted a requirement that the payee must show that a transfer is necessary to avoid imminent financial hardship and will not subject the payee or dependents to undue financial hardship in the future or that the transfer is in the best interest of the payee and the payee's dependents. Some states require the payee to be represented by counsel or receive independent professional advice regarding the legal, tax, and financial implications of such a transfer. Some of these states prohibit the assignment of worker's compensation benefits, including Florida.

Section 440.22, F.S., prohibits the assignment, release, or commutation of compensation or benefits due or payable under this chapter, except as provided by this chapter. Section 440.20(11)(a), F.S., authorizes lump-sum payments in exchange for the employer's or carrier's release from liability for future medical expenses, as well as future payments of compensation expenses. The lump-sum payment is authorized at any time in any case in which the employer or carrier has filed a written notice of denial within 120 days after the date of injury, and the judge finds a justiciable controversy as to legal or medical compensability of the claimed injury or alleged accident. Upon the joint petition of all interested parties and after giving consideration of all interested parties, a judge of compensation claims may enter a compensation order approving and discharging the employer's liability by the payment of a lump-sum. Lump sum payments are also authorized at any time in any case after the injured worker has reached maximum medical improvement.

Federal legislation has been proposed in recent years that would impose a substantial excise tax on the difference between the amount paid by the factoring company and the undiscounted value of the acquired payment stream. However, the excise tax would not be imposed on transfers of structured-settlement payment rights if the purchase is pursuant to a court order finding that certain extraordinary and unanticipated needs of the original intended recipient render such a transaction desirable.

III. Effect of Proposed Changes:

Section 1. Subsection (1) provides that the purpose of this section is to protect recipients of structured settlements who are involved in the process of transferring structured-settlement-payment rights.

Subsection (2) provides definitions for terms used in a transfer of a structured settlement. These terms include:

“Annuity issuer” means an insurer that has issued an annuity contract to be used to fund periodic payments under a structured settlement.

“Applicable federal rate” means the most recently published applicable rate for determining the present value of an annuity, as issued by the United States Internal Revenue Service pursuant to section 7520 of the United States Internal Revenue Code, as amended.

“Assignee” means any party that acquires structured-settlement-payment rights directly or indirectly from a transferee of such rights.

“Discount and finance charge” means the sum of all charges that are payable directly or indirectly from assigned structured settlement payments and imposed directly or indirectly by the transferee and that are incident to a transfer of structured-settlement-payment rights, including:

1. Interest charges, discounts, or other compensation for the time value of money;
2. All application, origination, processing, underwriting, closing, filing, and notary fees and all similar charges, however, denominated; and
3. All charges for commissions or brokerage, regardless of the identity of the party to whom such charges are paid or payable.

However, the term does not include any fee or other obligation incurred by a payee in obtaining independent professional advice concerning a transfer of structured-settlement-payment rights.

“Discounted present value” means, with respect to a proposed transfer of a structured-settlement-payment rights, the fair present value of future payments, as determined by discounting the payments to the present using the most recently published applicable federal rate as the discount rate.

“Payee” means an individual who is receiving tax-free damage payment under a structured settlement and proposes to make a transfer of payment rights under the structured settlement.

“Qualified-assignment agreement” means an agreement providing for a qualified assignment, as authorized by Title 26, section 130 of the Internal Revenue Code, as amended.

“Settled claim” means the original tort claim resolved by a structured settlement.

“Structured settlement” means an arrangement for periodic payment of damages for personal injuries or sickness established by settlement or judgment in resolution of a tort claim.

“Terms of the structured settlement” means the terms of the agreement, the annuity contract, a qualified assignment agreement; or an order of approval of a court or other government authority authorizing or approving the structured settlement.

“Transfer” means a sale, assignment, pledge, hypothecation, or other form of alienation or encumbrance made by a payee for consideration.

“Transfer agreement” means the agreement providing for transfer of structured-settlement payment rights from a payee to a transferee.

“Transferee” means a person who is receiving or who will receive structured-settlement-payment rights resulting from a transfer.

Subsection (3) establishes conditions to transfer structured-settlement-payment rights and structured settlement agreements. Such a transfer is not effective unless the transfer is authorized in advance in a final order by a court of competent jurisdiction. Such a final order would be based on the written express findings by the court that:

1. The transfer complies with this section and does not contravene other applicable law;
2. At least 10 days prior to the date the payee first incurred obligation with respect to the transfer, the transferee provided a disclosure statement in bold type, no smaller than 14 font, which specifies:
 - The amounts and due dates of the structured settlement payments to be transferred;
 - The aggregate amount of the payments;
 - The discounted present value of the payments, together with the discount rate used in determining the discounted present value;
 - The gross amount payable to the payee in exchange for the payments;
 - An itemized listing of all brokers’ commissions, service charges, application fees, processing fees, closing costs, filing fees, referral fees, administrative fees, legal fees, and notary fees and other commissions, fees, costs, and charges payable by the payee or deductible from the gross amount otherwise payable to the payee;
 - The net amount payable to the payee after deducting all commissions, fees, costs, expenses, and charges described above;
 - The following statement, “The net amount that you will receive in exchange for your future structured settlement payments represents __percent of the estimated current value of the payments”;
 - The following statement, “Based on the net amount that you will receive from us and the amounts and timing of the structured-settlement payments that you are turning over to us, you will in effect, be paying interest to us at a rate of __ percent per year”; and
 - The amount of any penalty and the aggregate amount of any liquidated damages, including penalties, payable by the payee in the event of a breach of the transfer agreement by the payee;
3. The payee has established that the transfer is in the best interests of the payee and the payee’s dependents;
4. The payee has received, or waived his or her right to receive, independent professional advice regarding the legal, tax, and financial implications of the transfer;

5. The transferee has given written notice of the transferee's name, address, and taxpayer identification number to the annuity issuer and the structured-settlement obligor and has filed a copy of the notice with the court;
6. The transfer agreement provides that if the payee is domiciled in Florida, any disputes between the parties will be governed by the laws of Florida;
7. The court has determined that the net amount payable to the payee is fair, just, and reasonable under the circumstances then existing.

Subsection (3) also provides that if the proposed transfer contravenes the terms of the structured settlement, upon the filing of a written objection by any interested party, the court may grant, deny, or impose conditions upon the proposed transfer. Any order approving a transfer must require the transferee to indemnify the annuity issuer and the structured-settlement obligor for any liabilities, including reasonable costs and attorney fees, which arise from compliance by the issuer or obligor with the order of the court.

Subsection (3) would also require a structured-settlement obligor, while negotiating a structured settlement of claims, to disclose in writing to the claimant or the claimant's legal representative, that any transfer of the periodic payments by the claimant may subject the claimant to serious adverse tax consequences.

Subsection (4) requires that at least 20 days before the scheduled hearing on an application for authorizing a transfer, the transferee must file with the court and all interested parties a notice of the proposed transfer and the application for its authorization. The notice must also include a copy of the transfer agreement, the disclosure statement, and notification that an interested party may support or oppose the application by submitting written comments to the court or by participating in the hearing, and notification of the time and place of the hearing and the manner in which and the deadline for filing any written response in order to be considered by the court. A written response to an application must be filed within 15 days after service of the transferee's notice.

Subsection (5) prohibits the waiver of any of the provisions of this section. In the event the transfer fails to meet the conditions of subsection (3), the payee who proposed the transfer would not incur any penalty, forfeit any application fee or other payment, or otherwise incur any liability to the proposed transferee.

Subsection (6) provides that if a transferee violates the requirements for stipulating the discount and finance charge, neither the transferee or any assignee may collect from the transferred payments, or from the payee, any amount in excess of the net advance amount. The payee would be authorized to recover from the transferee or any assignee a refund of any excess amounts previously received by the transferee or any assignee, reasonable costs and attorney fees, and a penalty in an amount determined by the court, but not in excess of 3 times the amount of the discount and finance charge.

If the transferee violates the disclosure requirements, the transferee and any assignee are liable to the payee for reasonable costs and attorney fees and a penalty in an amount to be determined by the court, but not in excess of 3 times the amount of the discount and finance charge.

The subsection also provides that, notwithstanding any other law, an action may not be brought under this section more than 1 year after the due date of: the last transferred payment, in the case of a violation of the requirements for stipulating the discount and finance charge or the first transferred payment in the case of a violation of the disclosure requirements of subsection (3).

The subsection authorizes the state attorney to bring a civil action for injunctive relief, penalties, and any other relief that is appropriate to secure compliance with this section.

Section 2. Provides that this act shall take effect October 1, 2001.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The bill would require an independent party, a court, to determine whether such a transaction would be in the best interest of the individual and his or her dependents and approve or disapprove such a transaction. The bill would require transfer agreements to contain specific disclosures relating to the transaction that would assist consumers in evaluating the costs and benefits of such a lump-sum payment transaction versus continuing the structured settlement periodic payments.

Since the federal tax consequences of such a transfer for the claimant are unknown, the bill requires that the agreement disclose that any such transfer of a structured settlement may subject the claimant to serious adverse tax consequences.

C. Government Sector Impact:

The Division of Risk Management of the Department of Insurance, which is responsible for providing casualty insurance for the State of Florida, is authorized to enter into structured settlements. According to the department, the impact of this bill is indeterminate.

Since such transfer agreements would require prior court review and approval, the courts may experience an indeterminate amount of additional costs associated with reviewing such agreements.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
