HOUSE RESEARCH ORGANIZATION bill analysis | 4/23/2001 | HB 1920 Counts (CSHB 1920 by Bosse)

SUBJECT: Regulating the transfer of structured settlements

COMMITTEE: Civil Practices — committee substitute recommended

VOTE: 6 ayes — Bosse, Clark, Dutton, Martinez Fischer, Nixon, Smithee

0 nays

3 absent — Janek, Hope, Zbranek

WITNESSES: For — Randy Dyer, National Structured Settlement Trade Association; Richard C. Hile, Texas Trial Lawyers Association; Earl S. Nesbitt, Settlement Capital Corp. and National Association of Settlement Purchasers; Terry Taylor

Against — None

BACKGROUND: Structured settlements allow a person to receive periodic payments instead of a lump sum. Such settlements are common in personal injury and workers' compensation suits, but they also may be created for lottery winnings or other guarantees of future income. Structured settlements also are common in cases where children are injured or are the dependents of an injured person. U.S. Internal Revenue Service rules exclude structured settlement payments from the recipient's gross income.

Recipients of structured settlements sometimes sell the right to receive future payments from the settlement in order to obtain an immediate cash payment.

DIGEST: CSHB 1920 would regulate the transfer of structured settlement agreements. The bill would not apply to creation or perfection of a security interest in a payment entered into with an insured depository institution. It would apply to periodic payments arising from settlement or judgment to resolve tort claims and workers' compensation claims.

Required notice. The person to whom a structured settlement was transferred ("transferee") would have to provide specific written information to the person transferring the structured settlement ("payee") at least three days before the day when the payee signed the transfer agreement. That information would have to include:

- amounts and due dates of the structured settlement payments to be transferred;
- the aggregate amount of payments;
- the discounted present value of payments to be transferred, including the amount of the Applicable Federal Rate used to calculate the discounted present value;
- the gross advance amount;
- an itemized list of all applicable transfer expenses, including the transferee's estimate of the amount, other than attorney's fees and related costs payable in connection with the transferee's application for approval of the transfer;
- the net advance amount;
- the amount of penalties or liquidated damages the payee would incur if he or she breached the transfer agreement; and
- a statement that the payee could cancel the transfer agreement without penalty or obligation no later than the third business day after the day the payee signed the agreement.

Court approval required. All direct and indirect transfers of a structured settlement would be ineffective unless approved in advance in a final order, either by the court of original jurisdiction that authorized or approved the structured settlement or, if that court no longer had jurisdiction, by a statutory county court or district court located in the county where the payee lived. The court order would have to find expressly that:

- the transfer was in the best interest of the payee, taking into account the welfare and support of the payee's dependents;
- the transferee had advised the payee in writing to seek independent professional advice regarding the transfer;
- the payee either had received such advice or knowingly had waived the advice in writing; and
- the transfer did not violate any applicable statute, court order, or order of another governmental authority.

Post-transfer obligations. After a transfer of a structured settlement agreement, the structured settlement obligor (insurance company) and the annuity issuer would be discharged from all liability to everyone except the transferee for the transferred payments. The transferee would be liable to the obligor and annuity issuer for any taxes incurred because the transfer had contravened the terms of the structured settlement and for any other liabilities or costs necessary for the parties to comply with the court order.

The transferee would be liable to the obligor, annuity issuer, and payee for liabilities or costs as a consequence of the transferee's failure to comply with the rules set forth in the bill. The transferee also would be liable to the payee for any taxes incurred by the payee for violating the terms of the structured settlement. The transfer could not require the obligor or annuity issuer to divide any payment between the payee and the transferee or assignee or between two or more transferees or assignees. Any further transfer or payment rights could be made only in compliance with this law.

Transfer approval procedure. CSHB 1920 would require all transfer applications to be made in court. At least 20 days before the court hearing, the transferee would have to file the application and a notice with the court and would have to serve a copy on each interested party. The notice would have to include:

- a copy of the application, of the transfer agreement, and of the required disclosure statement;
- a list of the payee's dependents and their ages;
- notice that interested parties could respond to the application, in person or through counsel, via written testimony or participation in the hearing; and
- notice of the time and place of the hearing and the deadline for written responses to be considered by the court.

Written responses to the application would have to be filed on or after the 15th day after the date the notice was served.

General provisions. The payee could not waive the following provisions.

If the payee lived in Texas, the transfer agreement would have to provide that disputes regarding the transfer agreement be determined in Texas according to Texas law. The transfer agreement could not authorize any party to confess judgment or to consent to entry of judgment against the payee.

Life-contingent payments could not be transferred unless the transferee had established procedures to confirm the payee's survival periodically and to notify the obligor if the payee died. These procedures would have to be acceptable to the obligor and the annuity issuer and be established before the date when the payee signed the transfer agreement.

A payee could not be responsible for any penalty, fee, or payment or otherwise incur liability to the proposed transferee or assignee based on failure of the transfer to satisfy these conditions. Compliance with the notice requirement and conditions required for approval of a structured settlement payment would be the sole responsibility of the transferee.

The bill could not be construed to authorize a transfer of a structured settlement in violation of any law, nor to imply that a transfer agreement entered into before the bill's effective date was valid or invalid.

The bill would take effect September 1, 2001, and would apply only to a transfer agreement entered into on or after that date.

SUPPORTERS SAY:

CSHB 1920 would establish uniform procedures and protections for the transfer of structured settlements. Structured settlements allow an injured person to receive a guaranteed income in the form of periodic payments over a term of years. When a large lump sum is awarded with the intent to compensate an injured person for life, the injured person often spends that sum quickly, leaving him or her without income or support. A structured settlement may allow an injured person to survive financially without seeking governmental assistance. Federal laws govern these settlements — for example, structured settlement money must be invested in an annuity or a government security.

To provide flexibility in structured settlements, so-called factoring companies often buy the future rights to payments under structured settlements in exchange for an immediate cash payment. While this may enable a payee to make a large purchase, such as to start a business or attend college, or to pay for medical emergencies or other significant unanticipated costs, many payees do not have a thorough understanding of the amount of money they are giving up to receive cash immediately.

CSHB 1920 would address both a state problem and a federal problem. Congress recognized the benefits of structured settlements and created tax incentives for these settlements. These incentives are not just for the payee but also flow to the insurance company (obligor) and the annuity company. Upon transfer of a structured settlement, these tax incentives are disrupted, incurring liabilities for the insurance company and the annuity company. As a result, when a payee attempts to transfer a structured settlement, the insurance company often files suit, driving up court costs, attorney fees, and other transfer-related expenses and significantly delaying the transfer.

Under current law, factoring companies are largely unregulated. Because factoring companies are not considered insurance companies or banks, they are not subject to the laws that govern those businesses. There are no legal restrictions or requirements regarding the cash payment, which may be as little as 13 percent of the present value of the structured settlement. Factoring companies say the discount rate is high because of the costs they incur in defending the ensuing lawsuit by the insurance company.

Requiring judicial review and approval of structured settlement transfer agreements would benefit everyone. Judicial review, in addition to the required disclosures, would help to ensure that payees understood these transactions. Payees would be offered only reasonable payments, as factoring companies would not waste their resources trying to get a judge to approve a bad deal. Disreputable factoring companies would go out of business, allowing the public to have confidence in the remaining factoring companies. In addition, a predictable and uniform transfer procedure would encourage traditional lenders, such as banks and other financial institutions, to lend against structured settlements or otherwise become involved in structure settlement transfers.

This bill would reduce uncertainty. The procedure for transferring a settlement would be predictable and uniform. Costs associated with delays would be reduced. All parties would have the assurance of a court order, resulting in less litigation after transfers.

Some degree of uniformity in state laws is highly desirable. A transfer may involve a payee, insurer, annuity company, and other interested parties living in multiple states. About 18 states have laws similar to CSHB 1920 that regulate the transfer of structured settlements. Insurers, factoring companies, and others with an interest in the transfer of structured settlements have worked together to propose similar legislation in many states.

Congress is considering H.R. 1514, which would create an excise tax on structured settlement transfers, with the tax rate being a percentage of the difference between the cash payment and the total amount of the structured settlement. However, H.R. 1514 would create an exception for structured settlement transfer agreements subject to judicial review under state laws. If CSHB 1920 does not pass, factoring companies will stop operating in Texas because the cost of doing business will become too high. This would harm structured settlement payees who would benefit from immediate access to cash to pay for major expenses and medical costs.

CSHB 1920 is not meant to put legitimate factoring companies out of business, nor to impose unreasonable limitations on the way they conduct business. It is designed to protect payees, many of whom are financially unsophisticated, from being swayed by offers of immediate cash payments without realizing what they are giving up.

OPPONENTS SAY:

The "best interest" standard in CSHB 1920 is vague, and judges may be uncomfortable with it. Reasonable judges may disagree on what is in a payee's best interest. The bill should define this standard more clearly. For example, it could create a rebuttable presumption that the transfer was in the payee's best interest if the payee was competent and filed an affidavit stating that it was in the payee's best interest.

OTHER OPPONENTS SAY:

The bill should limit transfers of structured settlements to very specific circumstances, such as using the money for education, buying a home, or paying for medical expenses. All interested parties to a structured settlement agreement should have to agree to such a transfer to make it valid.

NOTES:

The committee substitute would expand the definition of court to include a statutory county court or district court located in the county in which the payee lived if the court that authorized or approved the structured settlement no longer had jurisdiction to approve a transfer.

The substitute also amended the filed version to require the transferee to be liable to the payee for any taxes, liabilities, or costs incurred if the transfer violated the terms of the structured settlement or did not comply with the bill's requirements.

The companion bill, SB 277 by Harris, passed the Senate on April 5 on the Local and Uncontested Calendar and was reported favorably, as substituted, by the House Civil Practices Committee on April 18, making it eligible to be considered in lieu of HB 1920.

A similar bill in the 76th Legislature in 1999, HB 2691 by Counts, passed the House but was left pending in the Senate Jurisprudence Committee.