

# Transfers of Structured Settlement Payment Rights: What Judges Should Know About Structured Settlement Protection Acts

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Structured settlements have enjoyed widespread acceptance and have become an established part of our legal landscape over the past twenty-five years. More than \$6 billion is now paid each year to fund new structured settlements in the United States, and an estimated \$100 billion or more has been paid in the aggregate to fund structured settlements that are in force today. Little controversy attended the development of structured settlements. Much controversy has accompanied the development of a secondary market, in which structured settlement “factoring” companies acquire from settlement recipients their rights to receive future payments.

Since 1997, the controversy surrounding structured settlement factoring has led thirty-eight states to enact statutes that make transfers of payment rights under structured settlements ineffective unless those transfers receive advance court approval. Since 2002, the Internal Revenue Code (IRC) has reinforced the state statutes by imposing a 40 percent federal excise tax if a transfer of structured settlement payment rights does not receive the required court approval.

Because of this unusual combination of state law requirements and federal tax sanctions, state courts throughout the country are being asked to rule on growing numbers of applications for approval of transfers of payment rights under state structured settlement protection acts (SSPAs). This article explains the

SSPAs and their relationship to the IRC and discusses some of the key questions that courts need to address in ruling on SSPA applications.

## Structured Settlements and the Rise of Factoring

Structured settlements are settlements of tort claims involving physical injuries or physical sickness, and workers' compensation claims, under which settlement proceeds take the form of periodic payments, including scheduled lump sum payments. Structured settlements generally are funded by single-premium annuity contracts held by the party that is contractually obligated to make the future settlement payments.<sup>1</sup> Under federal tax rules designed to encourage the use of structured settlements, the full amount of each periodic payment, including the amount attributable to earnings under the annuity contract, is excludable from the settlement recipient's income under IRC section 104(a)(1) or (2). Congress has endorsed use of structured settlements as a means of assuring continuing income to injury victims and minimizing the risk that lump sum recoveries will be dissipated, leaving victims of disabling injuries to fall back on public assistance.

Consistent with the congressional policy favoring use of structured settlements, and for reasons linked to their tax treatment, structured settlement agreements typically provide that a settlement recipient's rights to receive future payments may not be assigned or otherwise transferred. In some cases, transfers of payment rights are also restricted or prohibited under applicable statutes or court orders. Notwithstanding these restric-

tions, an active secondary market in structured settlement payment rights developed in the early 1990s.

Through aggressive advertising, specialized finance companies—now commonly referred to as structured settlement factoring companies—began persuading structured settlement recipients (referred to herein as “payees”) to trade future payments for present cash.

To circumvent the restrictions on assignment of payment rights, factoring companies arranged for payees to redirect their payments to factoring company addresses. The factoring companies would then collect the payments (endorsing checks in the payees' names, using powers of attorney and signature stamps) without informing insurers that payment rights had been assigned.

Many payees who dealt with factoring companies were exploited. By fashioning transactions as purchases of future payment rights or as loans originated in states with generous usury laws, factoring companies often charged sharp discounts to payees who were ill equipped to appreciate the value of their future payments or to understand the onerous terms of factoring agreements. In some cases, factoring companies charged discounts equivalent to annual interest rates as high as 70 percent.<sup>2</sup> Payees who defaulted often were sued in remote forums specified in the factoring companies' form contracts. In many cases, these actions commenced with entry of confessed judgments against payees. Insurers responsible for making ostensibly nonassignable settlement payments became embroiled in collection actions brought by factoring companies. Insurers also faced uncertain tax consequences and risks of multiple

liability when assigned settlement payments became subject to competing claims.

### Enactment of State SSPAs

Beginning in Illinois in 1997, state legislatures recognized the need to protect structured settlements against the abuses of factoring. As explained by legislators in New Jersey:

Structured settlements provide strong public policy benefits. They provide long-term protection for injury victims and their families. They provide against the loss or dissipation of lump sum recoveries. Factoring companies, commonly using phone banks, advertising and high-pressure sales to “buy” a settlement for a small lump-sum, undermine these benefits and may exploit an injured person at a time when they need cash.<sup>3</sup>

The legislatures in New Jersey and at least thirty-seven other states have responded by enacting SSPAs. As this article was going to press, SSPA legislation was nearing enactment in four additional states: Arkansas (House Bill 2614), Kansas (House Bill 2160), Montana (Senate Bill 122), and New Mexico (House Bill 495). SSPA bills were also pending in Alabama (House Bill 91) and Oregon (Senate Bill 645).

Although they are not uniform, all of the SSPAs are derived from the same model legislation,<sup>4</sup> and they all reflect the same basic legislative scheme. Under each of the SSPAs:

- The transferee—that is, the factoring company—is required to make a series of disclosures designed to highlight the value of transferred payments and to contrast that value with the net amount that a payee stands to receive in exchange for the transferred payments. In most states, the transferee is required to disclose the discounted present value of the transferred payments, as determined by using the “Applicable Federal Rate” most recently published by the Internal Revenue Service for purposes of valuing annuities.<sup>5</sup>

- The effectiveness of any transfer of structured settlement payment rights is conditioned on advance court approval of the transfer,<sup>6</sup> based on findings that the transfer (1) will serve the best interests of the payee and the payee’s dependents and/or is necessary to enable them to avoid hardships, and (2) will not contravene “applicable law” or, more specifically, applicable statutes or orders.<sup>7</sup> Ten SSPAs expressly require an affirmative finding regarding the fairness and reasonableness of a proposed transfer, a finding that generally should be implicit in any finding that a transfer will serve the best interests of a payee and his or her dependents.<sup>8</sup> Fourteen SSPAs expressly require a finding that a proposed transfer complies with those SSPAs.<sup>9</sup> Thirty-three SSPAs also require either a finding that the payee has received “independent professional advice” concerning the proposed transfer or, alternatively, a finding that the payee has been advised to seek independent professional advice and has either received it or knowingly waived that advice.<sup>10</sup>

- At least some aspects of the procedure for seeking approval of proposed transfers are spelled out. For example, the statutes identify the categories of “interested parties” that are entitled to receive notice of a proposed transfer, the contents of the notice, and the minimum notice period that must elapse before an application can be heard.

- Key terms—e.g., “structured settlement,” “structured settlement payment rights,” and “transfer”<sup>11</sup>—are defined.

To this basic menu of statutory provisions, many SSPAs add supplemental protections for payees and their dependents and/or for structured settlement obligors and annuity issuers. For example, twenty-five SSPAs mandate that the transfer agreement between a payee and a factoring company be governed by the law of the payee’s home state and/or that any disputes between the payee and the factoring company be heard

in the courts of that state.<sup>12</sup> These same acts also prohibit or restrict transfer agreement provisions authorizing a factoring company to confess judgment against a payee.

Nineteen SSPAs provide that structured settlement obligors and annuity issuers cannot be required to divide payments between multiple recipients and/or provide that life-contingent payments may not be transferred in the absence of appropriate, agreed-upon mechanisms for confirming the payee’s survival (or notifying the structured settlement obligor and annuity issuer in the event of the payee’s death).<sup>13</sup>

### Enactment of IRC Section 5891

The abuses associated with structured settlement factoring drew attention not only from state legislators but also from the U.S. Treasury Department and Congress. Beginning in the federal budget for fiscal year 1999, the Treasury Department proposed that Congress impose a punitive federal excise tax on transfers of structured settlement payment rights, except in cases in which courts find that “the extraordinary and unanticipated needs of the original intended recipient” make these transfers desirable.<sup>14</sup> This proposal was incorporated in a series of bills sponsored in the U.S. House of Representatives by Rep. E. Clay Shaw, Jr. (R-Fla.) and Rep. Fortney (Pete) Stark (D-Cal.) and in the U.S. Senate by Sen. John Chafee (R-R.I.) and, following Sen. Chafee’s death, by Sen. Max Baucus (D-Mont.). The legislation ultimately was enacted as part of the Victims of Terrorism Tax Relief Act of 2001<sup>15</sup> and is now codified as IRC section 5891.

Section 5891 recognizes and reinforces the SSPAs.<sup>16</sup> Section 5891(a) imposes a 40 percent excise tax on any party that acquires payment rights in a “structured settlement factoring transaction,” a term whose definition in section 5891(c)(3) closely resembles the definition of “transfer” in the SSPAs. Section 5891(b) excepts from the 40

## State Structured Settlement Protection Statutes

State	Statute
Alaska	ALASKA STAT. §§ 09.68.200–09.68.230
Arizona	ARIZ. REV. STAT. ANN. §§ 12-2901–12-2904
California	CAL. INS. CODE §§ 10134–10139.5
Colorado	COLO. REV. STAT. §§ 13-23-101 to 13-23-108
Connecticut	CONN. GEN. STAT. § 52-225g–52-225l
Delaware	DEL. CODE ANN. tit. 10, §§ 6601–6604
Florida	FLA. STAT. ANN. § 626.99296
Georgia	GA. CODE ANN. § 51-12-70-72, §§ 51-12-70-76 to 51-12-70-77
Idaho	IDAHO CODE § 28-9-109
Illinois	215 ILL. COMP. STAT. §§ 153/1–153/35
Indiana	IND. CODE ANN. §§ 34-50-2-1 to 34-50-2-11
Iowa	IOWA CODE ANN. §§ 682.1–682.7
Kentucky	KY. REV. STAT. ANN. §§ 454.430–454.435
Louisiana	LA. REV. STAT. ANN. § 9:2715
Maine	ME. REV. STAT. ANN. tit. 24A §§ 601.25, 2241–2246
Maryland	MD. CODE ANN. CTS. & JUD. PROC. §§ 5-1101–5-1105
Massachusetts	MASS. GEN. LAWS ANN. ch. 231C, § 1–5
Michigan	MICH. COMP. LAWS. ANN. §§ 691.1191–691.1197
Minnesota	MINN. STAT. §§ 549.30–549.34
Mississippi	MISS. CODE ANN. §§ 11-57-1–11-57-15
Missouri	MO. REV. STAT. §§ 407.1060–407.1068
Nebraska	NEB. REV. STAT. §§ 25-3101–25-3107
Nevada	NEV. REV. STAT. § 42.030
New Jersey	N.J. STAT. ANN. §§ 2A:16-63–2A:16-69
New York	N.Y. GEN. OBLIG. LAW §§ 5-1701–5-1709
North Carolina	N.C. GEN. STAT. art. 44B §§ 1-543.10–1-543.15; art. 33 § 1-394.1
Ohio	OHIO REV. CODE ANN. §§ 2323.58–2323.587
Oklahoma	OKLA. STAT. ANN. tit. 12 §§ 3238–3245
Pennsylvania	40 PA. CONS. STAT. ANN. §§ 4001–4009
Rhode Island	R.I. GEN. LAWS ANN. §§ 27-9.3-1 to 27-9.3-7
South Carolina	S.C. CODE ANN. §§ 15-50-10–15-50-70
South Dakota	S.D. CODIFIED LAWS §§ 21-3B-1–21-3B-12
Tennessee	TENN. CODE ANN. tit. 47, ch. 18 §§ 1–7
Texas	TEX. REV. CIV. STAT. ANN. §§ 141.001–141.007
Utah	UTAH CODE ANN. §§ 78-59-101–78-59-108
Virginia	VA. CODE ANN. §§ 59.1-475–59.1-477
Washington	WASH. REV. CODE ANN. §§ 19.205.010–19.205.060, § 19.205.900
West Virginia	W. VA. CODE §§ 46A-6H-1–46A-6H-8

percent excise tax “a structured settlement factoring transaction in which the transfer of structured settlement payment rights is approved in advance in a qualified order.” A “qualified order” is defined as “a final order, judgment or decree” that is issued “under the authority of an applicable State statute<sup>17</sup> by an applicable State court”<sup>18</sup> and finds that the proposed transfer “(i) does not contravene any Federal or State statute or the order of any court or responsible administrative authority, and (ii) is in the best interest of the payee, taking into account the welfare and support of the payee’s dependents.”<sup>19</sup> Thus, the conditions for exemption from the 40 percent federal excise tax coincide with the two primary conditions for an effective transfer of payment rights under the SSPAs.

Section 5891(d) clarifies that in any case in which applicable tax requirements were satisfied at the time a structured settlement was entered into, “the subsequent occurrence of a structured settlement factoring transaction” will not adversely affect the tax treatment of the parties to the settlement.

In the context of proceedings for approval of proposed transfers of payment rights under the SSPAs, section 5891 is important primarily for two reasons:

1. the threat of the 40 percent excise tax means that no informed party that is subject to the taxing authority of the United States will seek to acquire structured settlement payment rights without obtaining approval of the transaction under the appropriate SSPA; and
2. by specifying the applicable State court from which a qualified order must be obtained, section 5891 effectively dictates the choice of forum for most proceedings under the SSPAs.

### Reviewing and Ruling on Applications Under SSPAs

In any case in which a payee proposing to transfer payment rights resides in a state that has enacted an SSPA,

the transaction is almost certain to be submitted for court approval in the payee's home state, often in the payee's home county. Thus, growing numbers of state courts are being called upon to review and rule on transfer applications, and the trend will only continue as additional states enact SSPAs.

What should courts expect to see when they receive transfer applications? How should courts handle those applications, most of which will be unopposed? What issues must a court expect to rule on in every case? What other issues should a court be prepared to consider? The following sections of this article address these questions, taking into account the express requirements and the legislative objectives of the SSPAs, together with recent case law applying them.

**Contents of a transfer application.** Under most SSPAs, a transfer application is made in the name of the transferee, i.e., the factoring company,<sup>20</sup> and includes the following:

- a formal application describing the proposed transfer, alleging compliance with applicable statutory requirements and requesting entry of an order approving the proposed transfer and including the findings required (1) under the applicable SSPA(s) and (2) for a qualified order under IRC section 5891(b);
- a copy of the transfer agreement between the payee and the factoring company;
- a copy of the disclosure statement(s) given to the payee under the applicable SSPA(s);
- a copy of the notice provided to interested parties to inform them of the proposed transfer and their opportunity to oppose, support, or otherwise respond; and
- if not included in the transfer application itself, a listing of the names and ages of the payee's dependents, if any.

Even when some of the above items are not required under the SSPA(s) applicable to a specific trans-

fer, they will often be included in a transfer application because it is simpler for factoring companies to prepare and submit common denominator applications that meet the documentation requirements of many SSPA(s) rather than tailor their applications to satisfy the more limited requirements that may apply in some cases.

**Conduct of proceedings.** Must a court conduct a hearing on an application for approval of a transfer of structured settlement payment rights, even if the application is unopposed? Most SSPAs provide for a hearing and afford interested parties the opportunity to be heard, with or without filing any written response. If a hearing is not required to be scheduled under the applicable SSPA(s), or if a hearing is scheduled but no interested party registers any opposition to a proposed transfer, can the court appropriately dispense with a hearing if the applicant submits an affidavit from the payee indicating that the applicable statutory conditions will be fulfilled? While some courts are prepared to rule on transfer applications on the basis of a paper record alone or, at any rate, without hearing testimony from the payee, other courts have found that a thorough evaluation of a payee's best interest, as required under the SSPAs and IRC section 5891, requires that a court hear directly from, and be able to question, the payee.<sup>21</sup>

However it receives evidence regarding a payee's best interest, a court should expect to hear from and question an applicant's counsel concerning the statutory requirement that a proposed transfer not contravene applicable statutes and court orders (or, under some SSPAs, "applicable law"). A court should not be expected to make an affirmative finding on this subject based solely on conclusory allegations in an application, nor should it be the responsibility of a court to identify and review potentially conflicting statutes, court orders, or other sources of applicable law.

Whether or not an application is the subject of a formal hearing, and

however the court receives evidence concerning the payee's best interest, it is clear that the applicant (normally, but not always, the factoring company) has the burden of establishing that the applicable statutory requirements are met.<sup>22</sup>

**Courts must address the payee's best interest.** To qualify for exemption from the excise tax imposed under IRC section 5891, a structured settlement factoring transaction must be found to be in the "best interest of the payee taking into account the welfare and support of the payee's dependents."<sup>23</sup> To be effective under the applicable SSPA(s), a transfer must be found to satisfy that same test or a similar test plus, in ten states, the separate requirement that the transfer be found to be "fair and reasonable." All of these tests are referred to collectively in this article as the "best interest" test.

While it is commonly recognized that "[t]he heart of the SSPA's protection lies in the courts' independent discretionary determination"<sup>24</sup> whether a proposed transfer satisfies the best interest test, courts have applied differing approaches in making that determination. Some courts have required a showing of "an unforeseeable change in circumstances"<sup>25</sup> or a "compelling and reasonably informed necessity"<sup>26</sup> as a basis for best interest findings. Other courts have adopted a more flexible approach. For example, the Court of Appeals of Minnesota has explained:

We believe that the best interests determination involves a more global consideration of the facts, circumstances, and means of support available to the payee and his or her dependents. These considerations would include, among other case specific factors, the reasonable preference of the payee, in light of the payee's age, mental capacity, maturity level, and stated purpose for the transfer. . . .

The factors for consideration should also include whether the peri-

odic payments of the structured settlement were intended to cover future income loss or future medical expenses. If so, the district court should inquire whether the payee has means of support aside from the structured settlement to meet these obligations. . . . The district court should also consider whether the offered discount rate is in line with the market rate for similar transfers . . . . Finally, the district court should consider whether the transfer is in the best interests of the payee's dependents; we believe this may involve an assessment of whether the payee can meet the financial needs of and obligations to the payee's dependents if the transfer is allowed to proceed.<sup>27</sup>

A New York trial court opinion has offered the following synthesis:

Although the [New York] statute does not define the best interests of the Payee, developing case law and the intent of the statute suggest the Court should consider: (1) the Payee's age, mental capacity, physical capacity, maturity level, independent income, and ability to support dependents; (2) purpose of the intended use of the funds; (3) potential need for future medical treatment; (4) the financial acumen of the Payee; (5) whether the Payee is in a hardship situation to the extent that he or she is in "dire straits"; (6) the ability of the payee to appreciate financial consequences based on independent legal and financial advice; [and] (7) the timing of the application.<sup>28</sup>

Courts have also recognized that the evaluation of a payee's best interest contemplated by the SSPAs is analogous to best interest determinations provided for in the context of family law, probate, and guardianship proceedings,<sup>29</sup> as well as proceedings for approval of commutation of workers' compensation benefits.<sup>30</sup>

In evaluating the terms of a proposed transfer, either as part of a general best interest analysis or for purposes of making a specific finding regarding the fairness and reasonableness of the transfer, courts have understandably been troubled by the

discount rates commonly charged in factoring transactions. Those rates have been characterized as "punishingly high,"<sup>31</sup> "exorbitant,"<sup>32</sup> and "unconscionable and overreaching."<sup>33</sup> Some courts have imposed de facto caps on allowable discount rates.<sup>34</sup> Most courts have adopted a less rigid approach, recognizing that "[t]he more pressing the need, the more reasonable it may be for a payee to obtain immediate cash at a steep discount rate."<sup>35</sup>

Courts routinely require that applicants prove that proposed discount rates are reasonable.<sup>36</sup> In evaluating the reasonableness of proposed rates, courts may consider evidence of the "market" rates commonly charged in structured settlement factoring transactions, but they tend to view that evidence skeptically. A recent New York ruling explained that

while petitioner asserts that the structured settlement market is "competitive," with price quotes being given freely to interested sellers by different funding companies . . . , the Legislature's imposition of a requirement for court approval provides a strong indication of its conviction that market factors alone are not sufficient to ensure the fairness of such transactions, or to prevent abusive or predatory practices which may pervade the industry. This may be a consequence of the fact that individuals desiring to sell their payments often have no other means of obtaining cash, and are therefore, to a certain extent, "at the mercy" of firms that are in the business of purchasing such payments, creating an inherent inequality in bargaining power. Under these circumstances, the mere fact that a payee is free to "shop around" among firms to obtain the best price offered does not necessarily mean that the terms of the resulting contract will be "fair" or "reasonable."<sup>37</sup>

Neither the SSPAs themselves nor cases provide—or can be expected to provide—any precise formula for applying the best interest test, but the cases suggest, and experience confirms, that a court should:

- Recognize that under both the SSPAs and IRC section 5891 a court is expected to make its own assessment of a payee's best interest, not simply to accept conclusory assertions by the payee or the factoring company.

- Insist that the payee appear in person, if possible, because evaluation of a payee's best interest is "a task that does not lend itself to long distance litigation."<sup>38</sup> If a personal appearance is not possible, the court should consider at least interviewing the payee by telephone.

- Be prepared to question the payee and any other witnesses testifying in support of an application, whether or not there is any opposition. The direct testimony of a payee proffered by a factoring company in support of its application for approval of a transfer of payment rights often is formulaic, shedding limited light on the needs of the payee and the payee's dependents. Even when someone opposes an application, the opponent is not likely to be well situated to elicit critical information.<sup>39</sup> Unless the court is prepared to ask probing questions, it may receive little more than the fragmentary information that typically appears in affidavits submitted in support of transfer applications.

- Take into account a payee's sophistication, recognizing that in many cases payees have structured settlements precisely because their attorneys and/or their family members believed, sometimes with the concurrence of a court, that they needed the protection and security of a structured settlement rather than an all-cash settlement with the attendant dissipation risk. A court should be particularly wary in any case involving a young payee whose structured settlement was entered into before he or she reached the age of majority. These payees can be especially vulnerable to the high-pressure sales tactics sometimes employed by factoring companies.<sup>40</sup>

- Recognize the risk that a payee may enter into (or may already have entered into) other factoring transac-

tions that, in conjunction with the transaction that the court is considering, may prove to be extremely detrimental to the payee's financial position. The court should ask any payee whether he or she has been party to any prior factoring transaction, including any proposed transaction that may have been disapproved by another court.<sup>41</sup> If the answer is affirmative, the court should insist that the applicant and/or the payee provide the details of the prior transaction(s), including, in the case of any prior transaction that received court approval, (1) the anticipated use of the transaction proceeds, as described to the court that approved the prior transaction; and (2) the payee's actual use of those proceeds.<sup>42</sup>

- Find that a proposed transfer satisfies the best interest test if the applicant has established that, taking all of the relevant circumstances into account, the transfer would be reasonable, i.e., that a fully informed, reasonable person whose personal and family situation coincided with those of the payee would enter into such a transaction. If the applicant has not established that the proposed transfer meets this standard, the application should be disapproved.

In considering the appropriateness of the terms of a proposed transfer, a court should:

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- Recognize that the required disclosure of the discounted present value of transferred payments, as calculated using the Applicable Federal Rate published by the Internal Revenue Service, provides only a "rough comparison" to the net amount that a payee stands to receive in a factoring transaction.<sup>43</sup> A more precise comparison can be made by obtaining a quote for the premium that a life insurer would charge in issuing a new annuity contract providing for the same payments that are to be transferred from the payee to the factoring company. The New York SSPA requires that such a quote be obtained and included in the transferee's disclosure statement.<sup>44</sup>

- Appreciate that although they generally are documented as purchases of payment rights, structured settlement factoring transactions can be analogized to loans secured by transferred payments.<sup>45</sup> Accordingly, the interest rate that is implicit in a factoring transaction can be a useful point of reference. In considering the appropriateness of such an implicit interest rate, however, a court should be aware that the fees charged by some factoring companies can dramatically affect a payee's borrowing costs. If a factoring company charges fees that are deducted from the proceeds otherwise available to the payee, the principal amount of the putative loan is effectively reduced and the interest rate implicit in the transaction is effectively increased.<sup>46</sup>

- Compare the discount rate and/or the implicit interest rate in a proposed factoring transaction with rates charged in other transactions, including both those that have been approved and those that have been disapproved based on the best interest test. In making these comparisons, however, a court should recognize that because of the inherent inequality in bargaining power between payees and factoring companies, rates consistent with the levels established in other factoring transactions are not

necessarily fair, reasonable, or otherwise in a payee's best interest.<sup>47</sup> If the discount rate for a proposed transaction exceeds those levels, that may constitute persuasive evidence that the transaction terms are *not* in the payee's best interest; it does not follow, however, that a proposed rate that corresponds to levels established in other factoring transactions *is* in the payee's best interest.

- Consult readily available sources of information on comparative discount/implicit interest rates charged in structured settlement factoring transactions. These sources include (1) rate information disclosed in the growing numbers of SSPA rulings addressing the best interest test, and (2) the data presented in a March 2004 study prepared by the California Attorney General's Office, *Impact of Prior Court Approval on the Transfer of Structured Settlement Payment Rights*. This study, prepared for the California legislature, includes a survey of hundreds of structured settlement transfers involving California payees between 2000 and 2003, including approximately 800 transfers that were the subject of applications for court approval under the California SSPA in 2002 and 2003. The findings from this study regarding discount/interest rates are summarized in the tables at right.<sup>48</sup> Because discount rates charged by factoring companies are not systematically recorded and published, the California study is a unique resource for information about the terms of a large number of structured settlement factoring transactions.

**Courts must address noncontravention of applicable law and compliance with SSPA requirements.**

For purposes of determining whether a proposed transfer of payment rights contravenes applicable law or applicable statutes and orders, and for purposes of specifically determining whether the transfer complies with the applicable SSPA(s), where an express finding of such compliance is required, a court must consider

whether the transfer satisfies objective SSPA requirements. The following questions, among others, should be considered: Has the payee been given the required disclosures? Does the transfer agreement omit any provisions that are mandated under the applicable SSPA(s)—e.g., choice of law and choice of forum provisions? Does the agreement include any provisions that are proscribed under the applicable SSPA(s)—e.g., broad confession of judgment clauses? Does the notice furnished to interested parties include the required documents and information? These requirements are straightforward, and courts generally have little difficulty ascertaining whether they have been satisfied.

Finding that a proposed transfer would not contravene applicable law or applicable statutes and court orders can be more difficult. Both the SSPAs and IRC section 5891 provide for such findings because in some cases a transfer of payments rights, even if it is approved by a court, would conflict with preexisting legal restrictions that neither the state nor the federal legislation is intended to disturb. Sources of such legal restrictions include:

- Workers' compensation laws, most of which prohibit or sharply restrict assignment of benefits, including benefits payable through structured settlements.<sup>51</sup> Some state legislatures have addressed this potential conflict by making their SSPAs wholly inapplicable to transfers of payment rights under workers' compensation settlements.<sup>52</sup>

- State tort reform statutes and other statutory compensation schemes, which in some cases prohibit or restrict assignment of recoveries, including payment rights under structured settlements.<sup>53</sup>

- Court orders approving settlements. Because they are commonly used to resolve tort claims of minors, as well as adults who have suffered injuries that have rendered them legally incompetent, structured settlements often are submitted for court approval

#### Contract Price as a Percent of Present Value<sup>49</sup>

	<i>Mean</i>	<i>Median</i>
2000	59.9	59.9
2001	55.1	55.1
2002	54.3	55.3
2003	54.0	55.1

#### Average Contract Prices as a Percent of Present Value (By Purchaser)

	2002	2003
	<i>Mean (Median)</i>	<i>Mean (Median)</i>
JG Wentworth	52.9 (54.6)	NA
321 Henderson Receivables	57.3 (58.0)	57.0 (59.5)
Settlement Funding	52.9 (52.4)	45.8 (46.4)
Settlement Capital Corp.	53.1 (51.1)	47.8 (52.6)

#### Minimum and Maximum Contract Prices as a Percent of Present Value (By Purchaser)

	2002	2003
	<i>Min. (Max.)</i>	<i>Min. (Max.)</i>
JG Wentworth	17.6 (80.0)	NA
321 Henderson Receivables	23.5 (90.0)	13.5 (83.6)
Settlement Funding	26.4 (81.5)	14.2 (72.8)
Settlement Capital Corp.	30.0 (84.3)	17.2 (75.8)

#### Effective-Equivalent Interest Rates Compared to Alternative Sources of Credit<sup>50</sup> (As Percents)

	2000	2001	2002	2003
<b>Effective-Equivalent Interest Rates:</b>				
Mean	19.5	20.9	19.8	19.2
<b>Effective-Equivalent Interest Rates:</b>				
Median	19.8	20.1	19.9	19.3
Prime Rate	9.23	6.91	4.67	4.12
30-Year Conventional Mortgage	8.06	6.97	6.54	5.82
Credit Cards	15	15	12	12

before they are implemented. The court order approving a settlement often includes antiassignment provisions or incorporates the terms of a settlement agreement that contains antiassignment provisions.<sup>54</sup> Unless such an order has been appropriately modified, a later transfer of payment rights under the settlement is likely to conflict with the order.

• Contractual antiassignment restrictions. The settlement documents governing structured settlements typically prohibit any assignment of the payees' rights to receive future settlement payments. The effectiveness of these contractual antiassignment provisions was extensively litigated between factoring companies and insurers in the context of factoring transactions that predated the enactment of SSPAs.<sup>55</sup> Insofar as contractual antiassignment provisions were effective to bar an assignment of payment rights prior to enactment of the SSPAs, they generally remain effective for that purpose if an insurer or other party that has standing to invoke the antiassignment provisions seeks to enforce them.<sup>56</sup> Taking into account the protections available under the SSPAs and IRC section 5891, however, insurers now do not generally find it necessary to insist on enforcement of antiassignment provisions. Thus, contravention of purely contractual antiassignment provisions, as distinguished from antiassignment provisions contained in a statute or a court order, is an issue that effectively is waived in most cases.

**Courts must address independent professional advice.** Under all of the SSPAs other than the Georgia, Indiana, Kentucky, Tennessee, and West Virginia statutes, approval of a transfer of payment rights requires a finding that the payee either has received independent professional advice or has knowingly waived the right to receive it. Of the SSPAs that require these findings, eleven require findings that the payee has actually received independent professional

advice; waiver is not permitted.<sup>57</sup>

In any case in which a court is asked to find that a payee has received independent professional advice (whether or not the payee could, under the applicable SSPA(s), have waived this advice), the court should consider whether the adviser was truly independent, i.e., disinterested. As courts in several states have recognized, payees sometimes are referred to advisers—typically attorneys—by factoring companies. Sometimes the advisers are paid by factoring companies from the proceeds of the transactions on which they render ostensibly independent advice. In some instances, purportedly independent advice has been confirmed in printed form letters provided by factoring companies.<sup>58</sup> Such arrangements are difficult to reconcile with a finding that a payee has received professional advice that is truly independent.<sup>59</sup>

A court that is asked to find that a payee has received independent professional advice may also wish to ask whether the professional adviser recommended for or against the proposed transfer of payment rights. Absent evidence that the professional adviser endorsed the transfer, the court may appropriately assume that there was no such endorsement.<sup>60</sup>

When a court is asked to make a finding that a payee has knowingly waived independent professional advice, the court should be prepared to question the payee in order to satisfy itself that the payee appreciates the reasons for obtaining independent professional advice and has nevertheless made an informed decision to forego that advice.

**Identifying the applicable SSPA(s).** Each SSPA applies, at least by implication, to any transfer of payment rights by a payee who is domiciled in the enacting state.<sup>61</sup> Most SSPAs also apply under other conditions, which typically are spelled out in the statutory definition of “structured settlement.” For example, an SSPA may apply if

- the underlying structured settlement was approved by a court in the enacting state,

- the structured settlement agreement is governed by the laws of the enacting state, or

- the structured settlement obligor or the annuity issuer is domiciled in the enacting state or has its principal place of business in that state.<sup>62</sup>

Because of these multiple triggering conditions, many proposed transfers of payment rights are subject to more than one SSPA. That does not mean that these transfers must receive approval from multiple courts. It means simply that the court in the forum state in which a transfer application is filed, normally the payee's home state, should be prepared to consider whether the proposed transfer complies or fails to comply with the requirements of any other applicable SSPA, insofar as they may differ from the requirements of the forum state's SSPA. Consistent with both the doctrine of comity and the Full Faith and Credit Clause of the Constitution,<sup>63</sup> the courts in any forum state must take into account applicable SSPAs enacted in other states.

Because the substantive requirements of the SSPAs are largely the same, a proposed transfer that meets the requirements of the SSPA in the payee's home state generally will meet all or most of the requirements of any other applicable SSPA. In some cases, additional requirements will come to bear. For example, if a factoring company proposes to acquire structured settlement payment rights from a payee who is domiciled in New Jersey, the transfer will be subject to the New Jersey SSPA, and the application for approval of the transfer will be filed in a New Jersey court. If, however, the underlying structured settlement was approved by a court in Delaware, the transfer will also be subject to the Delaware SSPA. The substantive requirements of the Delaware and New Jersey SSPAs coincide in most respects. If, however, the transfer would conflict with the

terms of the structured settlement, the Delaware statute, unlike the New Jersey statute, will require that the court find that the transfer has been “expressly approved in writing” by certain interested parties and by the court that approved the settlement.<sup>64</sup> Thus, in ruling on the transfer application, the court in New Jersey should, in addition to considering the issues that are common to the two statutes, determine whether the proposed transfer has received the approvals required under the Delaware statute.<sup>65</sup>

Recognizing that proposed transfers of payment may be subject to the SSPA(s) of states other than the forum state, a court hearing a transfer application should insist that the applicant’s counsel identify all such other SSPAs and any substantive requirements of these other SSPAs that differ from the requirements of the SSPA of the forum state.

**Notice to interested parties.** With the exception of the Louisiana statute, every SSPA requires that interested parties be given notice and an opportunity to oppose (or to support or otherwise comment on) applications for approval of transfers of payment rights.<sup>66</sup> The term “interested parties” typically is defined to include the payee, certain named beneficiaries, the structured settlement obligor, the annuity issuer, and “any other party that has continuing rights or obligations” under a structured settlement. As courts have recognized, these statutory notice requirements are intended “to insure that due process is afforded to those who may be interested in a proposed transfer.”<sup>67</sup>

Consistent with their due process function, the notice requirements also reduce the risk that an approved transfer of payment rights will be vulnerable to a future challenge by someone who was a party to the underlying structured settlement and did not participate in the transfer. At a more practical level, notice affords interested parties, especially structured settle-

ment obligors and annuity issuers, an opportunity to identify potential problems affecting a proposed transfer and, where possible, to work with the applicants to resolve those problems consensually.

Although factoring companies derive valuable protection from providing effective notice to interested parties, notices often are misdirected or omitted altogether. Accordingly, courts hearing transfer applications should insist that applicants specifically identify all interested parties and submit proof that they have been duly notified. In cases in which notice requirements may not have been satisfied, courts should insist that they be satisfied before an application is heard.<sup>68</sup>

**Conflicting interests in payment rights.** A payee who is or has been the subject of a bankruptcy proceeding may not be able to transfer payment rights without having taken appropriate steps to establish that those rights are free of claims of creditors. In most cases, those steps will include exempting the payment rights from administration as property of the payee’s bankruptcy estate.<sup>69</sup> A payee’s ability to transfer payment rights may also be limited by a divorce decree or separation agreement or by applicable property laws that afford a payee’s present or former spouse an interest in payment rights. Circumstances like these should be identified and resolved before a transfer is proposed, let alone submitted for court approval. However, if a court perceives that a payee’s bankruptcy trustee or present or former spouse (or anyone else who has not joined in or consented to a proposed transfer) has, or may have, an interest in payment rights that the payee proposes to transfer, the court should insist that the circumstances be examined, disclosed, and resolved to its satisfaction.

## Conclusion

By the time courts are asked to rule on them, most applications for approval of transfers of structured settlement

payment rights are unopposed. The interested parties that are most likely to have objections to a proposed transfer—the structured settlement obligor and the annuity issuer—typically will have raised any objections informally and resolved them consensually with the factoring company before a court hears the application.

The absence of opposition does not mean, however, that a transfer application should be granted. Approval of a proposed transfer under applicable SSPA(s) depends, as does exemption from the 40 percent excise tax under IRC section 5891, on express findings that the transfer satisfies the best interest test, that the transfer will not contravene applicable law, and, in most cases, that the payee either has received or has knowingly waived independent professional advice. These findings should be made only after thorough evaluation of each transfer application and the supporting evidence in light of the statutory mandates and the well-recognized objectives of the SSPAs.

## Endnotes

1. The party contractually obligated to make future settlement payments, referred to in most SSPAs as the “structured settlement obligor,” normally is either (1) a property and casualty or workers’ compensation insurer (or a self-insured entity), or (2) an “assignment company,” typically an affiliate of the annuity issuer, which assumes the direct contractual obligation to make future settlement payments through a “qualified assignment” under IRC § 130.

2. See, e.g., *J.G. Wentworth S.S.C. v. Jones, Jefferson Cty., Ky. Cir. Ct. No. 97CI5285, July 20, 1998 Op. and Order at 2, aff’d, 28 S.W.3d 309, 315 (Ky. Ct. App. 2000)* (“[i]n the four cases here the rate of return to Wentworth varied between 36 and 68 percent per year”); *Windsor-Thomas Group, Inc. v. Parker, 782 S.2d 478, 480 (Fla. Dist. Ct. App. 2001)* (finding that “from a functional viewpoint” a factoring company’s “Fund Acquisition Agreement” with a payee was “a secured promissory note with an annual interest rate of approximately 100 percent”); Press Release, N.Y. Attorney General’s Office, Spitzer Announces First-of-Its-Kind Agreement to Protect Consumers Who Win, and Then Sell, Personal Injury Settlements (July 29, 1999) (“in a substantial number of transactions [J.G.

Wentworth] effectively received an annual rate of more than 25% of the amount paid to the consumer, and in some cases the rate was as high as 70%”).

3. Sponsor’s Statement to N.J. Assembly Bill 2146, subsequently enacted as the New Jersey SSPA, *quoted in In re Transfer of Structured Settlement Rights* by Joseph Spinelli, 803 A.2d 172, 175 (N.J. Super. Ct. 2002). *See also* 2002 Sess. Law News of N.Y., Legis. Mem. ch. 537 (McKinney’s) (Assembly Mem. in Support of A6936A, subsequently enacted as the New York SSPA).

4. Each of the current SSPAs is derived from one of several versions of the Model Structured Settlement Protection Act developed by the National Structured Settlements Trade Association and promoted by that association and other insurance industry associations, often in cooperation with state attorneys general, state bar organizations, and others concerned about protecting structured settlements. In September 2000, the National Structured Settlements Trade Association and prominent factoring companies, together with the factoring companies’ trade association, the National Association of Settlement Purchasers, agreed on a combined state and federal legislative package, including a version of the Model Structured Settlement Protection Act that both groups agreed to support. Most of the SSPAs enacted since September 2000 have been closely patterned after that agreed-upon model. In February 2004, that model was adopted by the National Conference of Insurance Legislators as its Model State Structured Settlement Protection Act, replacing a Model Structured Settlement Transfers Protection Act, also derived from the National Structured Settlements Trade Association model legislation and adopted by the National Conference of Insurance Legislators in July 2000.

5. Pursuant to IRC § 7520, the Internal Revenue Service publishes the “Applicable Federal Rate” (also referred to as the “Section 7520 rate” monthly in the *Internal Revenue Service Bulletin*. *See* Treas. Reg. § 1.7520-1. In cases in which transferred payments resemble monthly (or other regular periodic) payments on a loan (i.e., a loan equal in principal amount to the lump sum that the payee receives from the factoring company), factoring transactions can appropriately be analogized to secured loans, and disclosure of effective interest rates may be more informative than disclosure of the present value of the future payments to be transferred. Where the transferred payments include lump sums, however, or where the first transferred payment is not scheduled to be made until long in the future (so that there is, in effect, a prolonged period of negative amortization), disclosure of implied interest rates is less informative, because the transactions bear little resemblance to home mortgage loans or revolving credit arrangements with which payees are

likely to be familiar. The SSPAs in four states require disclosure of implied interest rates in addition to disclosure of the discounted present value of transferred payments. *See* CAL. INS. CODE § 10136(a)(7); LA. REV. STAT. ANN. § 9:2715(B)(2)(g); MASS. GEN. LAWS ANN. ch. 231C § 2(a)(2)(vii); NEB. REV. STAT. § 25-3104(b)(viii).

6. Some SSPAs provide for approval of a transfer of structured settlement payment rights either by a court or, if applicable, by an administrative authority that had exclusive jurisdiction over the settled claim. In practice, such administrative authorities are encountered very rarely. Accordingly, this article refers only to consideration of transfers of payment rights by courts.

7. The SSPAs in four states do not explicitly require findings that transfers will not contravene applicable law or applicable statutes and orders. However, each of those SSPAs includes a provision recognizing that the statute does not authorize any transfer that would contravene applicable law. *See* IND. CODE ANN. § 34-50-2-9(c)(1); LA. REV. STAT. ANN. § 2715(G); MD. CODE ANN. CTS. & JUD. PROC. § 5-1105(b); W. VA. CODE § 46A-6H-4.

8. The SSPAs that require express findings regarding the fairness and reasonableness of proposed transfers are those enacted in CA, DE, FL, MD, MA, NE, NY, NC, OH, and TN.

9. The SSPAs in the following states include this requirement: AK, AZ, DE, FL, GA, ME, MA, MI, MN, MO, NE, NY, OH, and TN. The West Virginia SSPA requires an express finding of compliance with the disclosure requirements of the act. *See* W. VA. CODE § 46A-6H3(f)(2).

10. The five states whose SSPAs do not require any findings concerning independent professional advice are GA, IN, KY, TN, and WV.

11. The term “transfer” typically is defined to mean a “sale, assignment, pledge, hypothecation or other alienation or encumbrance of structured settlement payment rights made by a payee for consideration.” Thus, a “transfer” entails both alienation of existing payment rights and receipt of consideration by the payee. If future structured settlement payments are rescheduled pursuant to the underlying settlement documents (as originally written or as amended by agreement among the payee, the structured settlement obligor and the annuity issuer) there is no “transfer” within the SSPA definition.

12. The SSPAs of the following states include one or both of these requirements: AK, AZ, CA, CO, CT, FL, ID, IL, IA, LA, MA, MN, MS, MO, NE, NJ, NY, OK, RI, SC, SD, TX, UT, VA, and WA.

13. The SSPAs of the following states include one or both of these provisions: AZ, CA, CO, CT, ID, IL, IA, MS, NJ, NY, OK, RI, SC, SD, TN, TX, UT, VA, and WA.

14. *See, e.g.,* FISCAL YEAR 1999 BUDGET OF THE U.S. GOVERNMENT, GENERAL

EXPLANATIONS OF THE ADMINISTRATION’S REVENUE PROPOSALS at 122 (Feb. 1998).

15. *See* § 115 of H.R. 2884, enacted as Pub. L. No. 107-134, 115 Stat. §§ 2427 *et seq.* Section 115 of H.R. 2884 was taken verbatim from H.R. 1514, 107th Cong., 1st Sess., which was the 107th Congress’s version of corresponding bills introduced by the same sponsors in the 106th and 105th Congresses. *See* S. 1045, 106th Cong., 1st Sess. (proposing enactment of IRC § 5891, imposing an excise tax on structured settlement factoring transactions); H.R. 263, 106th Cong., 1st Sess. (same); S. 2543, 105th Cong., 2d Sess. (same); H.R. 4314, 105th Cong., 2d Sess. (same).

16. By December 2001, when H.R. 2884 passed, SSPAs had been enacted in thirty states. (Several of those SSPAs have since been amended or reenacted to conform more closely to the model legislation.)

17. “Applicable State statute” is defined for this purpose as a statute that provides for entry of the appropriate order, judgment, or decree and has been enacted by:

(A) The State in which the payee of the structured settlement is domiciled, or

(B) If there is no statute described in subparagraph (A), the State in which either the party to the structured settlement [i.e., the structured settlement obligor] . . . or the person issuing the funding asset [i.e., the annuity issuer] for the structured settlement is domiciled or has its principal place of business.

IRC § 5891(b)(3).

18. “Applicable State court” means “a court of the State which enacted” the “applicable State statute,” except that if the applicable state statute is not a statute that has been enacted in the payee’s home state, the applicable state court may also be “a court of the State in which the payee of the structured settlement is domiciled.” IRC § 5891(b)(4). Like many of the SSPAs, § 5891 also contemplates possible approval of a transfer of structured settlement payment rights by an administrative authority that had exclusive jurisdiction over the settled claim. *See* § 5891(b)(2)(B)(ii) and note 6, *supra*.

19. IRC § 5891(b)(2).

20. The Indiana and Kentucky SSPAs suggest that either the transferee or the payee may apply for approval of a transfer. *See* IND. CODE ANN. §§ 34-50-2-8(b)(3)(C), 34-50-2-7(4); KY. REV. STAT. ANN. § 454.435. Under the Pennsylvania SSPA, only the payee is authorized to apply. *See* 40 PA. CONS. STAT. ANN. § 4004.

21. *See, e.g., In re R & P Capital Res., Inc. (Hildreth)*, 772 N.Y.S.2d 461, 464 (N.Y. Sup. Ct. 2003) (“In order to satisfy the court’s obligation . . . to make inquiry of the propriety of the transaction for the individual consumer petitioner, a personal appearance necessarily is required.”); *In re Transfer of Structured*

Settlement Proceeds to 321 Henderson Receivables Ltd. P'ship (*Dreyer*), Dubois Cty., Ind. Super. Ct. No. 19D01-0304-MI-0033, June 6, 2003 Order Denying Transfer ¶ 6 ("Absent personal testimony by the payee . . . Petitioner was not able to present evidence or produce information that convinces the court that the transfer contemplated is in the best interest of the payee"); cf. *In re Settlement Funding (Platt)*, 774 N.Y.S.2d 635, 637, 641 (N.Y. Sup. Ct. 2003) (noting that the payee was "present and provided the Court with an opportunity to evaluate credibility, financial acumen, and the extent to which he was or was not being compelled to make the transfer" and stressing "the Court's ability to see and hear the Payee and raise such inquiries as it felt necessary"); *In re 321 Henderson Receivables Ltd. P'ship (DeMallie)*, 769 N.Y.S.2d 859, 860 (N.Y. Sup. Ct. 2003) (payee "did not appear personally before the court, and the court has only fragmentary information about his resources, living situation, health and financial needs").

22. See, e.g., *In re Ovation Capital, LLC (Lizotte)*, 2004 WL 233327, at \*3 (Mass. Super. Ct. 2004) ("[t]he burden rests with the payee to demonstrate that the proposed transfer is in his best interests"). In seventeen states, allocation of the burden of proof is codified in SSPA provisions stating that the transferee is solely responsible for fulfilling the conditions for an effective transfer. The states that have this SSPA provision are AZ, CO, CT, ID, IL, IA, MS, NJ, NY, OK, RI, SC, SD, TX, UT, VA, and WA.

23. IRC § 5891(b)(2)(A)(ii).

24. *In re Settlement Funding (Cunningham)*, 761 N.Y.S.2d 816, 818 (N.Y. Sup. Ct. 2003).

25. *DeMallie*, 769 N.Y.S.2d at 863; *In re Settlement Funding (Asproules)*, 2003 N.Y. Slip Op. 51638(U) at \*3 (N.Y. Sup. Ct. Dec. 30, 2003); but see also *In re Settlement Capital Corp. (Ballos)*, 769 N.Y.S.2d 817, 823 (N.Y. Sup. Ct. 2003) (declining "to adopt, as a general proposition, a 'best interest' standard that bespeaks of 'desperate or dire straits' or a 'life or death emergency'"); accord, *In re David Lantz, Steuben Cty.*, N.Y. Sup. Ct., Index No. 88477, Jan. 9, 2004, Decision at 3. In discussing the best interest test, several New York courts have cited legislative history suggesting that under the New York SSPA transfers should be approved only in cases involving "true hardship." E.g., *DeMallie*, 769 N.Y.S.2d at 862; *Ballos*, 769 N.Y.S.2d at 818 n.1. The New York SSPA has recently been amended to state that "[p]rovided the court makes the [best interest/fairness and reasonableness] findings . . . there is no requirement for the court to find that an applicant is suffering from a hardship to approve the transfer of structured settlement payment rights." 2004 N.Y. Laws ch. 480 (amending N.Y. GEN. OBLIG. LAW § 5-1706(b)).

26. *In re Structured Settlement Payment Rights of Mario Curto*, Phila. Cty., Pa. Ct. of

Common Pleas, Sept. Term 2003 No. 03714, Mar. 23, 2004 Mem. at 4.

27. *Settlement Capital Corp. v. State Farm Mut. Auto. Ins. Co. (Lundgren)*, 646 N.W.2d 550, 556 (Minn. Ct. App. 2002) (citations omitted).

28. *In re* Petition of Settlement Capital Corp. (*Platt*), 774 N.Y.S.2d 635, 638–39 (N.Y. Sup. Ct. 2003) (citing *Lundgren*, *Spinelli*, 803 A.2d 172, and *Ballos*, 769 N.Y.S.2d 817). See also *Lizotte*, 2004 WL 233327, at \*3.

29. *Spinelli*, 803 A.2d 172, 175.

30. *Curto*, supra note 26, at 3.

31. *DeMallie*, 769 N.Y.S.2d at 861.

32. *In re* Johnny Bush, Allegheny Cty., Pa. Ct. of Common Pleas, Civ. No. GD04-008825, Apr. 29, 2004 Opinion and Order at 4.

33. *Asproules*, 2003 N.Y. Slip Op. 51638(U) at \*4.

34. See, e.g., *Cunningham*, 761 N.Y.S.2d at 819 ("initially an interest rate of no more than 8% would be 'fair and reasonable' so long as the transferee does not charge its counsel fees and costs to the payee as transfer expenses"). In three states, the SSPAs themselves impose statutory ceilings on discount rates. See MICH. COMP. LAWS ANN. § 691.1193(1)(a)(vi) (discount rate "used in determining the discounted present value of the structured settlement payments to be transferred may not exceed 25% per year"); NEB. REV. STAT. § 25-3104(5) (transferee may not "contract for or receive a discount or finance charge that would result in an effective annual rate in excess of the maximum interest rate per year applicable in Nebraska to a consumer loan"); N.C. GEN. STAT. § 1-543.12(6) ("[t]he discount rate used in determining the net amount payable to the payee . . . does not exceed an annual percentage rate of prime plus five percentage points calculated as if the net amount payable to the payee . . . was the principal amount of a consumer loan").

35. *DeMallie*, 769 N.Y.S.2d at 861. See also, e.g., *Platt*, 774 N.Y.S.2d at 641 ("[n]o universal percent prohibition can be adopted as a judicial standard, given the need for flexibility and the function delegated to the courts to use their discretion"); *In re* Ryan Barr, 2004 WL 2008607, at \*2–\*4 (N.Y. Sup. Ct. 2004); *Bush*, supra note 32, at 4.

36. See, e.g., *Davis v. Travelers Cas. & Sur. Co.*, 2002 Conn. Super. LEXIS 2256, at \*8 (June 10, 2002); *Ballos*, 769 N.Y.S.2d at 825–29; *In re* Chrystal Dashnaw, Washington Cty., N.Y. Sup. Ct., Index No. 57-1-2003-0206, July 31, 2003 Order and Judgment at 3.

37. *In re* Rapid Settlements, Ltd. (*Phillips*), 2004 WL 3214459, at \*2 (N.Y. Sup. Ct. Oct. 24, 2004) (citations omitted). See also, e.g., *Cunningham*, 761 N.Y.S.2d at 818–19; *Ballos*, 769 N.Y.S.2d at 826 ("basing a determination upon the comparable or prevailing interest rates in the industry is dubious"); *DeMallie*, 769 N.Y.S.2d at 861–62; *Spinelli*, 803 A.2d 172 at 178–79.

38. *Hildreth*, 772 N.Y.S.2d at 463.

39. If the party opposing an application is the structured settlement obligor or the annuity issuer, it typically will have little or no information about the payee. If the party opposing the application is a member of the payee's family or someone else who has continuing rights or obligations under the payee's structured settlement, the opponent, although perhaps acquainted with the payee's situation, is likely to be appearing pro se. Thus, even when an application is opposed, the opponent is not likely to conduct any searching cross-examination.

40. For a detailed account of such sales tactics, see *Wiggins v. Peachtree Settlement Funding (In re Wiggins)*, 273 B.R. 839, 849–50 (Bankr. D. Idaho 2001).

41. See *In re* Jessica Reehl, Rensselaer Cty. N.Y. Sup. Ct., Index No. 207392, Apr. 29, 2003 Decision/Order at 5 ("the Court is of the view that in order to assess the overall best interest of the payee, and the welfare of the payee's dependents, the application should disclose whether other periodic payments have been transferred, the date of such transfer(s), and the consideration received"). Transfer applications do not generally include such information. Nor do they include information about other instances in which proposed transfers by a payee may have been disapproved by other courts. When a transfer application has been disapproved in one forum (or withdrawn in response to opposition), it is not uncommon for a similar application, making no reference to the application that was disapproved (or withdrawn), to be filed in another forum.

42. See, e.g., *Phillips*, 2004 WL 3214459, at \*1: When . . . [the payee's first transfer of payment rights] was brought before this court for approval, Phillips claimed that she was going to use the money to put a down payment on a home, purchase a used car to enable her to work at Wal-Mart, purchase clothes for her son and furniture for the house, and put the remainder into a savings account. . . . That clearly did not happen, however, because she is once again before the court looking to sell her final payment, for even less cash, again to put a down payment on a home.

43. *Spinelli*, 803 A.2d at 178.

44. See N.Y. GEN. OBLIG. LAW § 5-1703(d).

45. See note 5, supra.

46. See *Barr*, 2004 WL 2008607, at \*1 ("[w]here fees are imposed on a modest advance payment, doing so results in a dramatic increase to the effective rate of interest if the advance were considered a loan. For example, in *Asproules*, the 19.82% discount rate jumped to an effective loan rate of 22.49% since the \$2,200 in fees reduced Mr. Asproules' gross advance of \$16,200 to a net of \$14,000.").

47. In particular, payees seeking to transfer payments for the second (or third or fourth) time may effectively have been locked into dealing with the same factoring companies with

which they dealt before. Factoring agreements, especially those entered into before enactment of SSPAs and IRC § 5891, often create encumbrances that extend to all of a payee's payment rights, not just the specific payment rights that are sold (or earmarked to repay a secured loan). These encumbrances can make it difficult, time-consuming and costly for a payee contemplating a second (or subsequent) factoring transaction to do business with a different factoring company. Even when there is no encumbrance in favor of the first factoring company with which a payee has done business, practical considerations often make it difficult for a payee to change factoring companies unless all of the payments assigned to the first factoring company have been made before the payee proposes to transfer payment rights to a different company. The discount/interest rates offered to payees in second (or subsequent) transactions are often higher, sometimes substantially higher, than the rates charged in initial transactions.

48. CALIFORNIA ATTORNEY GENERAL'S OFFICE, IMPACT OF PRIOR COURT APPROVAL ON THE TRANSFER OF STRUCTURED SETTLEMENT PAYMENT RIGHTS 9-10, tables 4-7 (2004). In these tables, "contract price" refers to the net payment made by the factoring company in exchange for transferred payment rights, and "present value" refers to the discounted present value of transferred future payments, as calculated using the discount rate published by the Internal Revenue Service for purposes of valuing annuities, i.e., the Applicable Federal Rate described in note 5, *supra*.

49. Until January 2002, the California SSPA did not require that transfers receive prior court approval, although it did require that transfer agreements be filed with the Attorney General's Office. Hence the data for 2000 and 2001 reflect a regime in which the fairness and reasonableness of transfer terms was not subject to judicial evaluation. The data for 2002 and 2003 cover transactions that were subject to court approval but without regard to whether the transactions were approved. (Most were.) Interview with Cynthia Robinson, Associate Governmental Program Analyst, Office of the California Attorney General, March 8, 2005. Thus, the rates for all years covered in the California study are those that factoring companies charged, or sought to charge, not rates that courts necessarily approved.

50. The "effective-equivalent" interest rates from which these mean and median figures are derived were taken directly from the factoring companies' disclosures of "effective equivalent interest rates," as required under CAL. INS. CODE § 10136(a)(7). Interview with Cynthia Robinson, Associate Governmental Program Analyst, Office of the California Attorney General, March 8, 2005. Those disclosures in many cases would have understated the effective cost of borrowing for customers of factoring companies that charge fees that are deducted from the transaction pro-

ceeds. See note 46, *supra*.

51. See, e.g., Florida Asset Financing Corp. v. Utah Labor Comm'n, 2004 UT App. 273, 98 P.3d 436, 439-40 (Utah Ct. App. 2004), *cert. granted*, \_\_\_ P.3d \_\_\_, 2004 WL 3210799 (Utah Dec. 3, 2004) (contrasting Utah's Workers' Compensation statute with those of states that "explicitly prohibit the assignment of [worker's compensation] benefits," including the statutes of Arizona, California, Florida, Kentucky, and Nevada); J.G. Wentworth, S.S.C., L.P. v. SAFE-CO Life Ins. Co., 755 So. 2d 138, 139 (Fla. Dist. Ct. App. 1999) (affirming summary judgment invalidating purported purchase of future payments under settlement of Florida workers' compensation claim); *In re Roger Dunn*, 2005 WL 758610, at \*1 (Ind. Cir. Ct. 2005) (finding that the Illinois Workers' Compensation Act prohibited transfer of payment rights under a workers' compensation settlement), *appeal noticed* Apr. 5, 2005; Bernard Johnson v. Friendly Hiking Servs., Inc., Cal. Workers' Comp. App. Bd. No. SF405873, June 12, 1998 Minutes of Hearing and Order ("under [California] Labor Code § 4900, a claim for Workers' Compensation, including payments of compensation to be made under a settlement agreement, cannot be assigned before payment").

52. The states in this category are CA, CO, FL, ID, IN, KY, LA, MD, MN, NE, NY, NC, OH, SC, TN, and WV. Cf. *In re StratCap Invs., Inc.*, 796 N.E.2d 73 (Ohio Ct. App. 2003) (finding that definition of "structured settlement" in Ohio SSPA does not extend to settlements of workers' compensation claims); *Dunn*, 2005 WL 758610, at \*2 (same, under Indiana SSPA).

53. See, e.g., COLO. REV. STAT. § 13-64-209 (restricting assignment of rights to receive periodic payments under postjudgment settlements of medical malpractice actions); 735 ILL. COMP. STAT. § 5/2-1715 (same); MONT. CODE ANN. § 25-9-405 (same); N.Y. C.P.L.R. §§ 5038, 5048 (same); see also, e.g., J.G. Wentworth S.S.C. L.P. v. Ortega, Palm Beach Cty., Fla. Civ. No. CA-02-03013 AJ, July 2, 2002 Final Order ¶ 3 ("The proposed transfer of structured settlement payment rights from Ortega to Wentworth would 'contravene other applicable law' because it would . . . violate the provisions of New York Civil Practice Law and Rules § 5041 *et seq.* . . . which created and governs Ortega's payment rights and which . . . prohibits transfer of such rights").

54. Cf. N.Y. C.P.L.R. § 1206(c) ("the ability of an infant who has attained the age of eighteen years to accelerate the receipt of future installment payments pursuant to a structured settlement agreement shall be governed by the terms of such agreement").

55. See, e.g., J.G. Wentworth S.S.C. L.P. v. Callahan, 649 N.W.2d 694, 699 (Wis. Ct. App. 2002) and cases cited therein.

56. See, e.g., *In re Emerald Funding Corp.* (Brown), Monroe Cty., N.Y. Sup. Ct. Index No. 2003/3376, June 4, 2003, Mem. Decision at 7 ("If prior to the act [the New York SSPA] a clause

such as the one at issue here barred assignment . . . it should operate just as effectively afterwards."); *Lizotte*, 2004 WL 233327 at \*4; *Rapid Settlements, Ltd. v. SAFECO Nat. Life Ins. Co.* (Morgan), 2005 WL 246458, at \*2 (Conn. Super. Ct. Jan. 4, 2005) (disapproving application under Connecticut SSPA based on contravention of anti-assignment provisions); *In re Transfer by Raye Ann Brown*, Del. Cty., Ind. Cir. Ct. No. 18C03-0204-PL-11, July 3, 2002 Order (same, under Indiana SSPA); *In re Transfer [by] Vincent Zarbaugh*, Franklin Cty., Ohio Probate Ct. No. 484364, Jan. 14, 2002 Entry (same, under Ohio SSPA); *In re Transfer [by] Troy Walker*, Fayette Cty., Tenn. Cir. Ct. No. 4647, Feb. 23, 2005 Order (same, under Tennessee SSPA); cf. *Platt*, 2004 N.Y.S.2d 635, 639-40 (citing cases under New York SSPA in which insurers objected to transfers based on antiassignment provisions); but see also *Spinelli*, 803A.2d 172, 181 (approving transfer over insurer's objection; finding that antiassignment provision did not nullify the transfer); *Lundgren*, 646 N.W.2d 550, 554 ("the court is arguably empowered to override an antiassignment clause").

57. The SSPAs in the following states require a finding that the payee has actually received independent professional advice: AK, DE, FL, LA, ME, MD, MA, MI, MN, NC, and OH.

58. See, e.g., *In re Approval for Transfer of Structured Settlement by Reney Woodard*, Linn Cty., Iowa Dist. Ct. No. LACV 043227, Nov. 8 Order Denying Petition (attorney's letter "was in virtually identical form to those of attorneys' letters in similar proceedings reviewed by this Court. . . . [Attorney] further advised this Court that his name had been provided to Ms. Woodard on a list of attorneys suggested by [the factoring company]. . . . In light of the manner in which representation was provided to Ms. Woodard, a serious question arises as to how the attorneys on [the factoring company's] attorneys list are paid."); *Zarbaugh*, *supra* note 56, at 3 ("The Court notes that the [attorney's] letter is a pre-printed form . . . which [the factoring company] provided to [the attorney]. At the hearing, Counsel for [the factoring company] explained to the Court that [the attorney's] name appears on a list of attorneys that [the factoring company] provided to [the payee]. Additionally, the Court notes that at the bottom of the letter, [the attorney] advises [the factoring company] to 'send a \$300.00 check . . . this payment will represent payment in full of my legal fees for services rendered to [the payee] regarding this matter.'")

59. Many SSPAs define the term "independent professional advice" (or an equivalent term) in a manner that disqualifies advice rendered by anyone who is affiliated with or compensated by a transferee. Definitions of this kind appear in the SSPAs of the following states: AK, CA, DE, FL, LA, ME, MD, MA, MI, MN, MO, NY, NC, and OH.

60. See *Cunningham*, 761 N.Y.S.2d at 818 ("these applications should be treated as coming

without the independent advisor's endorsement unless the advisor submits an affidavit expressly stating that he or she endorses the transfer and gives specific reasons for doing so").

61. Unlike other SSPAs, the Indiana, Nevada, and West Virginia statutes do not specify the conditions under which they apply.

62. This combination of triggering conditions appears in the SSPAs of the following states: CT, IL, IA, MS, NJ, NY, OK, RI, SD, TX, UT, VA, and WA.

63. U.S. CONST. art IV, § 1 ("Full Faith and Credit shall be given in each State to the public Acts, Records, and Judicial Proceedings of every other State"); *see also* 28 U.S.C. § 1738 (implementing the Full Faith and Credit Clause).

64. *See* DEL. CODE ANN. tit. 10, § 6602(p)(2) (definition of "structured settlement payment rights"), § 6601(5)a.1-2 (requiring approvals).

65. Two courts have considered and rejected constitutional objections to application of the SSPA(s) of states other than the state in which a payee is domiciled. *See* Legal Asset Funding, LLC v. Travelers Cas. & Sur. Co., 155 F. Supp.

2d 90 (D.N.J. 2001) (confirming applicability of Connecticut SSPA to a transfer of payment rights by a Texas resident); Settlement Funding LLC v. Hunt, St. Louis Cty. Mo. Cir. Ct. Cause No. 01 CC-2247, Sept. 10, 2002 Judgment (finding Kentucky SSPA applicable to a transfer by a payee allegedly residing in Missouri).

66. The Louisiana SSPA provides for authorization of a transfer of structured settlement payment rights "in advance by ex parte order." LA. REV. STAT. ANN. § 2715.B(1). It is not clear how this procedure can be reconciled with due process. In practice, however, interested parties generally are notified of applications made under the Louisiana SSPA.

67. *In re* Katherine Campina, Benton Cty. Minn. Dist. Ct. No. C5-99-1177, Jan. 10, 2002 Order at 8 (vacating prior order under Minnesota SSPA approving transfer in the absence of notice to certain interested parties).

68. Courts should also be prepared to consider whether there are parties who may not fall within the applicable SSPA definition(s) of "interested parties" but may nevertheless be indispensable parties. If, for example, a payee

has been party to a previous factoring transaction, the transferee in that prior transaction may have (or claim to have) an interest that extends to payment rights that are the subject of a new application. Whether or not the prior transferee qualifies as an interested party under the applicable SSPA(s), it should nevertheless be made party to the new proceeding, based on applicable joinder rules because the prior transferee claims an interest in the subject payment rights. Disposition of the new application in the prior transferee's absence may impair its ability to protect its claimed interest and may leave the structured settlement obligor and annuity issuer subject to substantial risks of incurring double obligations. *Cf.* FED. R. CIV. P. 19(a).

69. Depending on the nature of the underlying settlement, structured settlement payment rights may qualify for exemption under any of a variety of federal and state laws, including, for example, § 522(d)(11) of the Bankruptcy Code, the Federal Employees' Compensation Act, 5 U.S.C. § 8130, state workers' compensation laws, and state insurance laws applicable to annuity contracts.