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MARKETS

# Firms Help Settlement Holders Cash Out Payments Meant to Last a Lifetim

'Factoring' companies draw scrutiny as people with settlements sell them off

ByLESLIE SCISM

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After a childhood fire took Terrence Taylor's leg and many fingers in 1988, his lawyers crafted a multimillion-dollar legal settlement to ensure he had steady income for life. It didn't take much for him to lose it.

In 2012 at the age of 30, Mr. Taylor moved out of his parents' northern Virginia home and took over his finances. Then, in 11 rapid-fire transactions with five finance firms, he sold three decades of future payments for hundreds of thousands of dollars in cash that he promptly squandered, according to a lawsuit filed by Mr. Taylor and his parents against those firms last month in federal court in Alexandria, Va. He recently moved back in with his parents, who say they are struggling to pay his medical bills.

Michael Lafontant was turned down in New York courts but obtained approval in Florida to cash out a settlement granted after his mother's alleged wrongful death. He is now suing over the deal. *PHOTO: LESLIE SCISM/THE WALL STREET JOURNAL*

People like Mr. Taylor—those who have received settlements designed to provide income for many years—aren't supposed to be able to easily cash it out. Since the late 1990s, 48 states and the federal government have passed consumer-protection laws requiring a state judge to determine whether it is in a seller's best interest to do such deals.

But more firms are competing to buy the rights to future income from people with so-called structured settlements that pay out over time. The competition is leading to what some consumer advocates, state lawmakers and industry participants say is a pickup in questionable deals that have exposed soft spots in state and federal statutes. Now, lawmakers, consumer advocates and even some industry participants are pushing to strengthen laws.

More than two dozen firms compete for pieces of the roughly $140 billion in settlements that the industry estimates are in consumers' hands. The number of firms has nearly doubled since 2011, when industry leader J.G. Wentworth Co. merged with Peachtree Financial Solutions. That combination resulted in more than 100 layoffs, spawning new firms. They execute an estimated 7,000 to 9,000 transfers tied to consumers' future income annually, up 25% from five years ago, some industry experts say.

These so-called factoring firms say they provide a valuable service, allowing consumers to get lump sums to spend on things like houses and school tuition. But some of these firms also have joined the push for tighter laws, saying a rise in questionable transactions could tarnish the industry and make it harder to do deals that benefit the sellers.

Some firms and industry participants say they want laws strengthened to require, for instance, that all sellers appear in court and disclose prior transactions, among other changes. Most states don't require court appearances by the sellers; instead, judges rely on sworn affidavits detailing why selling future income is sensible. Most states also don't require factoring firms to detail to the court a person's prior transaction history.

"Could there be some improvement in the statutes? Absolutely," said Earl Nesbitt, general counsel of the National Association of Settlement Purchasers, a trade group representing about 20 factoring firms. "But overall I think the court approval process works pretty well."

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Illinois, Minnesota and Tennessee recently bolstered laws or are considering ways to do so. The industry also has caught the eye of the U.S. Consumer Financial Protection Bureau, which last year sent civil requests to Wentworth seeking documents about its factoring business. The firm says it is cooperating. The CFPB declined to comment.

Sally Greenberg, executive director of the National Consumers League, said her group is pushing for industrywide regulation by the CFPB, concerned about transactions in which "people with grievous injuries end up destitute" from repeated transactions.

The experience of Michael Lafontant illustrates how a patchwork of state approaches is allowing firms to push through deals that have since become the subject of lawsuits by the sellers.

Mr. Lafontant received a settlement after his mother's alleged wrongful death that had been providing him with regular monthly payments since he was a child. In 2011, the then-20-year-old, who was living in New York, wanted to sell future income for cash to finance a hip-hop artist representation business. But he failed to win approval on a transaction in appearances before a judge in New York, a state widely considered to have stiff standards for approvals of such deals.

A salesman from a then-unit of Imperial Holdings Inc. suggested he go to Florida, according to a lawsuit filed by Mr. Lafontant in federal court in Manhattan last year. The Imperial salesman allegedly arranged to fly Mr. Lafontant to Florida and sign a false lease that was used to obtain a Florida-issued identification card, according to the suit. Imperial then obtained deal approval in Sumter County, Fla., with no court appearance required of Mr. Lafontant. He spent some of the proceeds on his hip-hop business, a Maserati and a Davie, Fla., house, the last two of which were later sold at a loss, the suit says.

Mr. Lafontant's suit, which is pending, alleges the salesman committed fraud by cajoling him "into faking his relocation to Florida" from New York. In court filings, Imperial denies wrongdoing. In a statement to The Wall Street Journal, it said: "We are 100% compliant with all applicable laws." A spokesman for the Sumter County court said, "The Judge, as provided in the statute, relies heavily on the parties' submitted affidavits to make a determination."

The salesman "made me feel it was perfectly legal...that this was regular protocol," Mr. Lafontant said in an interview.

In Mr. Taylor's case, most of the factoring deals were filed for court approval in Portsmouth, Va. Under Virginia law, settlement owners don't have to appear in court or provide a history of their transactions, Portsmouth Circuit Court Judge James Hawks said in an interview.

Mr. Taylor's lawsuit alleges that the factoring firms "coached Terrence on how to submit false affidavits."

In an interview with the Journal, Mr. Taylor said one salesman "said it has to look good on paper for the judge."

The affidavits said he intended to use lump sums for purposes including starting a cellphone business, a vending-machine operation and a help group for burn victims, according to a lawyer for one of the factoring firms. In reality, the suit says, he spent "lavish sums of money on women and gambling."

Speaking generally, Judge Hawks said: "I accept these affidavits on their face. It is sworn testimony." He looks for "a genuine need or urgency for converting the payments" to a lump sum. "If the legislature would enact some sort of requirement that a history of prior [transactions] be included in the application, that would be beneficial."

The firms that dealt with Mr. Taylor said their transactions were proper. "That a customer's life has not improved [through transactions], that's a very unfortunate outcome," said Andrew Savysky, president of 123 Lump Sum LLC, which executed multiple transactions for Mr. Taylor. He said his firm will start to identify "serial filers and to scrutinize their stated reasons for each transfer."

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# What Is a Future Income Stream Really Worth?

ByKaren Damato

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When people are invited to swap a stream of future payments for an immediate lump sum, they are often sorely tempted to take the money and run.

The question may come up when an employer offers a one-time check in lieu of a future pension or when a company proposes to buy a series of payments awarded to a plaintiff in a lawsuit.

But taking the lump sum can be an unwise decision for a variety of reasons, including if the offer is unreasonably low in relation to the value of the future payments.

One big problem: most individuals have no idea how to evaluate a lump-sum offer.

The “structured settlements” awarded in lawsuits are typically complex to value because they are customized for the recipient. There can be a series of regular payments plus some five- or even six-figure dollar amounts sprinkled in to pay for college or a down payment on a home or other needs that the plaintiff’s lawyer anticipates at the point of settlement.

There are about $140 billion in structured settlements in consumers' hands, and competition has increased among firms that offer cash to recipients of these settlements in exchange for the future income.

To find out the lump sum that would be equivalent in value to a complex structured settlement, you would probably need to hire an actuary to do the analysis, says William Bernstein, co-founder of Efficient Frontier Advisors, an investment management firm based In Eastford, Conn. (Here is an online directory of these professionals.)

Meanwhile, retirement-plan participants given the option of choosing a lump-sum payment before or during retirement typically don't get the information they need to make an informed decision, the Government Accountability Office said in a recent report.

But there is a shortcut to estimate the lump-sum equivalent of a pension (or a similar lifetime income stream) that is recommended by Mr. Bernstein and by Bill Reichenstein, an investments professor at Baylor University in Waco, Texas: You can use a variety of websites to find the lump sum you would need today to buy an immediate annuity from an insurance company that would provide an income stream like the one you are considering giving up.

Say, for instance, you are a 60-year-old man in Illinois who is entitled to a steady $1,000 a month for life. A Fidelity Investments annuity calculator suggests you would need to invest about $200,000 to buy an annuity providing that income stream, while ImmediateAnnuities.com puts the cost at around $205,000.

You could also use sites such as these to get quotes for different types of income streams, such as those that also cover a spouse or include an inflation adjustment or guarantee payments for a set number of years even if the buyer dies sooner.

Checking annuity costs is "the easy answer" on what a stream of payments may be worth today, says Mr. Bernstein. In the one or two pension offers he has looked at, he says, the one-time payment "was a ridiculously low amount" —but it can seem "like a lot of money because it is all in one lump."

In the case of a corporate or municipal pension plan, the individual needs to consider the financial health of that employer and the risk it might not fulfill its promises to retirees, Mr. Reichenstein says. But consumers considering taking a lump sum also need to beware of financial advisers who may tout unrealistically high investment returns to be made by investing the money—and watch out for advisers who may take an imprudent amount of risk when handed a lump sum to manage, he says.