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HEADLINE: #15 2010 TNT 41-15 UNOFFICIAL TRANSCRIPT OF IRS HEARING ON EXCLUSION FOR PHYSICAL HARM AWARDS NOW AVAILABLE. (Section 104 -- Damage Awards/Sick Pay) (Release Date: FEBRUARY 23, 2010) (Doc 2010-4501)

CODE: *Section 104* -- Damage Awards/Sick Pay;
Section 468B -- Designated Settlement Funds

ABSTRACT: The unofficial transcript is available of a February 23 IRS hearing on proposed regulations on damages received on account of personal physical injuries or physical sickness; the focus of the hearing was on insurance companies' practices in negotiating settlements with plaintiffs.

SUMMARY: Published by Tax Analysts(R)

The unofficial transcript is available of a February 23 IRS hearing on proposed regulations (REG-127270-06) on damages received on account of personal physical injuries or physical sickness; the focus of the hearing was on insurance companies' practices in negotiating settlements with plaintiffs.

Richard B. Risk Jr. of the Risk Law Firm asked the IRS to use the proposed regs as an opportunity to clarify that *section 468B* qualified settlement funds remain tax free regardless of whether a plaintiff is aware of the amount of the settlement or is the only beneficiary of the fund.

Jack L. Meligan of Settlement Professionals Inc., representing the Society of Settlement Planners, agreed with Risk's comments. The threat of making settlement amounts taxable to the plaintiff under a constructive receipt theory has been used by insurers to discourage the use of qualified settlement funds (QSFs), Meligan said.

John S. Stanton of Hogan & Hartson LLP, representing the National Structured Settlement Trade Association, argued only that the *section 104* regs are not an appropriate place for a revision of the QSF rules.

Speakers also addressed other possible changes to the proposed regulations, including per se exclusions for amounts received for sex abuse or long-term wrongful imprisonment.
Internal Revenue Service

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For related coverage, see *Doc 2010-3949* or *2010 TNT 36-4*.

TEXT:

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UNITED STATES DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE

PUBLIC HEARING ON PROPOSED REGULATIONS
26 CFR PART 301
"DAMAGES RECEIVED ON ACCOUNT OF PERSONAL PHYSICAL
INJURIES OR PHYSICAL SICKNESS"
[REG-127270-06]
Washington, D.C.
Tuesday, February 23, 2010

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* * * * *

PROCEEDINGS
(10:00 a.m.)

MR. MONTEMURRO: Good morning, ladies and gentlemen. I'd like to welcome you this morning to this hearing on proposed amendments to the final regulations under *Section 10482* of the code. The proposed amendments would update the final regulations to reflect the changes made by Section 1605 of the Small Business Job Protection Act of 1996. It would also delete the tort type rights test in the current regulations. The reg project number is REG 127270-06.

The next thing I'd like to do is let the panel members introduce themselves, starting at the opposite end of the table.

MS. ROSS: I'm Jeanne Ross, I'm with the Treasury Department.

MS. CRISALLI: Donna Crisalli, with Income Tax and Accounting.

MR. ISKOW: Sheldon Iskow, Income Tax and Accounting.

MR. MONTEMURRO: Mike Montemurro, Income Tax and Accounting. Okay. We have a little bit about -- some of the rules about speaking. We have three scheduled speakers today, but after I'm done with the scheduled speakers, anybody else who wants to speak will have an opportunity to speak, as well. Each speaker gets ten minutes to speak, and there's a little timer here, hopefully you can see it, you get ten minutes. I think the way the lights work is, there's a -- you start with a green light, with three minutes to go, a yellow light comes on, and then the red light comes on, sort of like traffic signals when the time is up.

I will stop the clock if one of the members of the panel has a question for the speaker, and then, you know, and that will stop the clock until that conversation is over, then we'll resume the countdown on the clock, and that's sort of what we'll do, that's the way that sort of works. I've got a beeper on, if you want a beeper on, you want the beeper on, we can figure that out, okay.

So we also have two services here transcribing the hearing, one, the Federal News Service, and one, Tax Analysts, and I think that sort of takes care of all the preliminary matters. What we'll do is, at the end of the three scheduled speakers, other people who want to speak will also have the opportunity to speak, OK. Go ahead, you have a question.

MR. MILLIGAN: I have a question. And I spoke to Mr. Iskow earlier, I had asked for 15 minutes and heard nothing to the contrary, and I've timed my presentation for that, so do I just hand over my script?

MR. MONTEMURRO: Well, I think it's ten -- I think we've said it was ten minutes, so I think that's where we are, you know. It's always a ten-minute presentation, so I think that's sort of what it is.

MR. MILLIGAN: Okay.

MR. MONTEMURRO: So I guess we'll start with the first speaker.

MR. ISKOW: Our first speaker is John McCulloch, representing Integrated Financial Settlements.

MR. MCCULLOCH: Thank you for letting me appear today. Again, my name is John McCulloch, I work for IFS. We're a large structured settlement brokerage. We provide tax-free periodic payments for plaintiffs and defendants. Every year thousands --

MS. CRISALLI: Can you speak louder because your back is to the audience and they're not --

MR. MCCULLOCH: Do I get time out for that?

MS. CRISALLI: Yes, time out.

MR. MCCULLOCH: Every year we encounter thousands of plaintiffs who we put in tax restructured settlements, but every year we encounter groups of plaintiffs that we are not able to assist because their injuries do not fall under the strict definition of an observable physical harm, a personal physical injury or sickness under 104A2. I'm here today talking about two of those groups, victims of sex abuse and molestation and victims of long-term wrongful imprisonment.

The 1996 Act, which changed 104A2, was never meant to affect these two groups, but because of a lack of clarity, we're really not in a position to help them, and that's what we're seeking here today, is to get some clarity surrounding these two groups of claimants.

When the Small Business Job Protection Act was signed in the law on August 20 of '96, it created -- it imported that requirement that the injuries be physical to be excludable from harm. The conference committee report at 104737 at 301 specified that emotional distress injuries, even those manifesting in a physical injury, were taxable unless they originated in a physical injury or physical sickness. Therefore, the Act elevated being -- an injury being physical to a new level, but neither the Act nor the legislative history went into any detail on how do you define what a personal physical injury or personal physical sickness was.

Throughout the existence of *Section 104*, the taxation of settlements has been interpreted by the Service and the courts to reflect the character of the claim and the damages the recovery is meant to replace or compensate for.

It stands to reason that the Act, which that provision was aimed at employment damages, made those taxable. Since wage loss represents a large component, those recoveries should be taxable. Conversely, an injury settlement to replace a lost limb or the loss of a loved one, those were never items of income, and it stands to reason those are not taxable.

So was congressional intent to exclude certain types of claims or rather that the injury be distinctly physical either in its origin or its result? The conference committee report states that this provision originated in differing views the courts had on employment discrimination -- decision on age discrimination, and the Service's suspension of guidance on the tax treatment of employment discrimination claims. A direct quote from the House bill said that the intent was to change *Section 104A2* so that it did not apply to damages received based on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress. So while a line was drawn between physical and emotional injuries, the Act didn't define what types of claims -- what constituted physical injuries.

Nowhere in the bill or the legislative history will you find anything stating a congressional intent to tax sex abuse, molestation, or long-term wrongful imprisonment. We're now 13 years post the Act and we don't have any sort of formal guidance on what constitutes a personal physical injury.

We only have informal guidance in the form of *PLR 2041022*, which gave us the observable harm standard. So to qualify under that PLR for exemption, the injury had to have direct or unwanted or uninvited physical contact resulting in observable bodily harms such as bruises, cuts, swelling and bleeding.

So while this standard may work for some claims, there's many claims that this standard cannot work for and shouldn't be universally applied. For example, pneumoconiosis is a physical sickness without an observable harm, you can't even see the symptoms until the latter stages of the disease, and yet no one would deny that black lung is a serious physical sickness or illness.

Similarly, tort litigation surrounding some physical sicknesses, such as the cases against Johns-Manville for asbestosis, or the diabetes cases against Eli Lilly from Zyprexa, none of those are observable harms, in fact, the symptoms aren't observable until shortly before death in some cases.

Taken to an extreme, consider a rear end collision with only soft tissue injuries, those harms are not observable, you can't even measure soft tissue injuries under x-ray or MRI, and yet those are consistently considered personal physical injuries.

So if an observable harm is not workable for those, it should not be workable and cannot be workable for sex abuse and wrongful imprisonment claims. For example, a study of 893 sex abused victims reported in the American Journal of Obstetrics and Gynecology, Volume 190, titled Physical Injury After Sexual Assault, was an analysis of urban emergency room sex assault victims. And while bruises and abrasions were the most common injury, they only represented 15 percent. Only seven percent had lacerations. Some 48 percent did not have what could be categorized as an observable trauma. Genital trauma in particular can be very difficult to document even when seen by a physician right away, which is typically not the case in these types of circumstances because of what goes on with the victim, embarrassment, shame, just the overall trauma.

So clearly, you know, we have 48 percent on average of these victims without an observable harm. I would submit to you it is improper to call these purely emotional or nonphysical injuries simply because there's not an observable harm.

The long term effects of both sex abuse, molestation, and wrongful imprisonment are well documented and long lasting. A study in the Journal of Interpersonal Violence, Volume 18, 2003, showed that victims of abuse were four times likely to commit suicide, four times likely to self-mutilate. A study of drug users showed that 42 percent had been abused as children.

A report from the Population Information Program showed that rape and childhood abuse were among the most common causes of post traumatic stress disorder, a disorder which is well understood and well documented in the medical communities, having long term physical and mental effects. Turning to long term wrongful imprisonment, according to the Innocence Project, of the 249 people they've exonerated, the average time spent in prison was 13 years.

Department of Justice study of women's prison showed that virtually every female inmate had been subjected to various levels of sexual aggression, from lewd remarks to rape, while a similar study conducted on men showed the percentage at 22 percent.

The Journal of Epidemiology reports that the long term effects of imprisonment include mental health problems, increased rates of poverty, smoking, poor eating habits, and substance abuse. A 2000 study showed that those in prison exhibited high rates of depression, chronic mental health problems, and substance abuse. The worst outbreaks in recent history from tuberculosis and HIV originated in prison populations.

I think it's without question that there are long term observable effects from both of these types of injuries. These cases were not meant to fall within the scope of the '96 Act. In deference to the very difficult tasks faced by Service and Treasury in attempting to define what is a physical injury, I would submit that for these two specific types of injuries, rather than relying upon an observable harm standard, we create a standard that would fit these cases, that the physical act of abuse or the physical act of deprivation of freedom is in itself a direct manifestation of a physical injury.

While purely mental or emotional damages are one thing, the act of being deprived of freedom or the act of being abused is, by definition itself, an observable harm.

Turning back to the legislation intent of the Act in '96, Congress did not say that an injury needed to be observable, but what they were trying to do was raise injury claims to a certain threshold, a physical threshold, in order to distinguish it from transitory emotional distress damages, the type of which typically accompany age discrimination or wrongful termination claims.

It is interesting to note that Congress decided that once you reached that threshold, then emotional distress damages became tax free. In the past, we've seen that it's been congressional intent to create tax exemption for wrongful imprisonment with the Civil Liberties Act of 1998. Treasury has ruled in the past, in revenue rulings 56462 and 58370, that victims of -- prisoners of war, that their reparations were tax free, and the Service, in one ruling, post the '96 Act, 199906004, relied upon these rulings to rule that compensation for deprivation of civil rights and freedom was not income. Very distinguishable from short-term wrongful detainment, as we saw in the Stadnyk case, where the detainment only lasted eight hours, and the injuries were no greater than being photographed in a prison jumpsuit.

In terms of the sex abuse cases, the Service itself, a Chief Counsel advisory letter from Mr. Montemurro acknowledged the difficulties found in these cases. In CCA 2009 09001, the Service acknowledged the difficulty in showing an observable harm, the lack of medical records, and acknowledged that absent an observable harm or medical records, that they would assume that an observable harm existed, and it was exempt. And I would submit that all sex abuse cases fall and receive the same type of treatment, no less and no difference from a broken toe or a bruised leg.

Thank you.

MR. MONTEMURRO: I just will make one comment, the thing about --

MR. MCCULLOCH: -- taken your Chief Counsel advisory in vain?

MR. MONTEMURRO: No, that would be observable -- observable harm is a standard. Of course, that was, you know, in the context of one PLR, and you know, sometimes I read a lot that, you know, this is like somehow -- you have to -- in order to get 104A2, you have to be able to observe the harm currently. I would assume that, you know, if somebody were physically injured, were sick, and then they sued later, and the harm had disappeared over that course of time, I would think that that -- that's still a personal physical injury.

I mean I think we were dealing with, you know, a particular factual situation, so to extrapolate that the letter will set some sort of black letter rule, it's just a statement in the --

MR. ISKOW: It's broader.

MR. MONTEMURRO: -- in the, you know, as facts in the letter ruling that we had presented there, that's all I'd say.

MR. MCCULLOCH: Absolutely; the thing we're faced without -- in the field, so to speak, when we're dealing with injury victims, with plaintiff attorneys, with the annuity issuers that provide the structured settlements, they take an extremely conservative view, and while we know PLR's are not presidential, they certainly look at it as to what would the Service do in this situation, and they tend to err on the side of caution. But even if we set the observable harm rule advisory letter aside, it's a gray area. And insurance companies are notoriously conservative.

And, you know, absent a clear definition that sex abuse and molestation is, per se, a physical injury, as we have submitted, or that long term wrongful imprisonment is a physical injury, as we have submitted, there have been err on

the side of caution and not take these.

And when you look at people who have been abused and people who have been wrongfully incarcerated, those are groups of people who desperately need long term financial planning, they're two groups that are the least capable of doing financial planning, they're dealing with a multitude of mental and emotional issues, the last thing they need is the added burden of trying to, you know, manage bills and invest, things that confound even the best of us.

MR. MONTEMURRO: Thank you.

MS. CRISALLI: I have some questions.

I'm trying to understand exactly what it is you're saying. Now, I assume you're not saying that someone who had a purely mental condition should be able to exclude damages --

MR. MCCULLOCH: No.

MS. CRISALLI: -- because that's not physical, but you seem to be saying that, in certain situations, we should presume that there's physical injury, for example, someone who's suffering from PTSD or somebody who's been wrongly imprisoned; is that what you're saying?

MR. MCCULLOCH: Yes; you know, rather than try and come up with a broad rule, which I would think is impossible, quite frankly, we're looking at two very, very narrow groups. So if you've been molested or abused, even though there's -- there may not be any proof of a physical injury, and, in fact, the statistics show that there is not in most cases, or if you've been in prison for a long duration as opposed to just a short transitory detainment, that those are, per se, physical injuries, with or without an observable harm.

We're not looking for exclusion on any kind of broad basis for non-physical or emotional injuries, it's those two very specific, very narrow groups of people, fortunately very small groups. On average, there's probably several hundred to maybe, at peak, 1,000 people exonerated a year. When you look at a report from the Presbyterian Church, they assume there's about 50 abuse cases annually, which is why I think this has sort of slipped under the radar. These are very small groups of folks; however, we run into them, whether on the plaintiff or the defense side. And it's incredibly difficult to sit across the table from someone whose child has been molested in a daycare and tell them that the life insurance companies that issue the -- annuities won't take this case because they're not sure it's tax free. And we're looking for relief for just those two groups.

MS. CRISALLI: Okay. Is it difficult for plaintiffs, injured people in these groups, to obtain some kind of medical documentation that there is a physical injury that's resulted from this?

MR. MCCULLOCH: Yes.

MS. CRISALLI: Even if it's like high blood pressure?

MR. MCCULLOCH: That wouldn't satisfy the life -- again, the life companies will look --

MS. CRISALLI: Okay. I'm not talking about the life companies, I'm talking about the Service. I mean if the Service said, you know, they would presumably accept it?

MR. MCCULLOCH: The problem, though, is a lot of times people don't seek medical treatment. And in the case of wrongful imprisonment, there is, you know, ultimately not going to be a treating physician for all of the impact for being wrongfully imprisoned. You can seek things later, but tying it back to the wrongful incarceration is not going to

be successful.

A lot of times, particularly with molestation cases in schools, you'll find an incredibly low rate of physicians treating these folks, and the physicians are not going to just write up something that says you're injured for tax purposes.

MS. CRISALLI: Do you have any indication that these kinds of issues are being raised by the field, by the Service level? You're more concerned about how the insurance companies are adjusting?

MR. MCCULLOCH: We're more concerned about -- in the field, what ultimately leads up to the insurance companies and whether they can accept it. But whether you can do a structure is almost secondary to the issues -- whether these -- are these tax free or are these taxable situations. And often times when you tell a party that it's taxable, it changes the entire dynamic of the settlement negotiation. Do you have to withhold to pay taxes on what your attorneys are being paid? On these cases, if they are taxable, ANT could potentially apply, so the parties have to plan accordingly.

But the problem is not so much being raised in the field offices. Again, I think because these are small numbers of folks, fortunately, I think it would be, in one dimension, terrible if we had, you know, rampant sex abuse cases and wrongful incarceration. But there are a few hundred folks a year, but I don't think that makes it any less important.

MS. CRISALLI: The last question, do you -- can you comment on whether you think we could include a rule like this in a final regulation and be compliant with the Administrative Procedure Act that requires notice and opportunity for public comment?

MR. MCCULLOCH: I believe we could. I think this is an issue --

MS. CRISALLI: Of course you do.

MR. MCCULLOCH: Well, you asked me, and I thought there was sort of a softball, you know, pitch for me to --

MS. CRISALLI: No, it's not, it's a hardball actually.

MR. MCCULLOCH: I do, I think it's an issue that you would find a lot of support on. I don't think administratively or procedurally there would be any objections to including these as, per se, definitions of physical injury, you know, nothing would make me happier than to see that.

MS. CRISALLI: Okay. So we could do it because nobody would care?

MR. MCCULLOCH: No, I think you would do it because you would find that a lot of people care and you would not find objection?

MS. CRISALLI: Nobody would object?

MR. MONTEMURRO: Let me just ask you a question. So you set it at one year, so the guy who is in prison for 11 months, if we say that that's -- if we say that one is a physical injury -- implication going to be that the one 11 months is not a physical injury. Right now no one says that it is or isn't, so that guy is going to be, you know, potentially in a worst position, right?

MR. MCCULLOCH: Potentially, but you have to draw the line somewhere, and it's not an enviable task.

MR. MONTEMURRO: That sort of goes back to Donna's question, that guy with 11 months, he's going to be reading that reg saying, wait a second, I didn't have an opportunity to say get it down to six months, or three months, or two

months or --

MR. MCCULLOCH: Possibly, but when you look at the -- again, turning back to the data that is available from the Innocence Project, these are not people on death row for 11 months, these are people on death row for over a decade. And I tried to draw the line, as the Service has in other circumstances, capital gains, for example, the difference between short term and long term is a year, it seemed like a good place to draw it.

MR. MONTEMURRO: Congress drew that line, though.

MS. CRISALLI: Well, that kind of gets to my -- well, I said that was my final question, I found another one. Have you talked to them up on the Hill about this?

MR. MCCULLOCH: No, not yet.

MS. CRISALLI: You might think about it.

MR. MCCULLOCH: I will.

MR. MONTEMURRO: Okay.

MS. ROSS: I have a question. I mean you're proposing that we draw the line around the sexual abuse cases and these wrongful termination cases.

MR. MCCULLOCH: Wrongful imprisonment.

MS. ROSS: Wrongful imprisonment, thank you. And I think you said at the beginning of your testimony that it's hard to make the distinction between physical and non-physical, and you think, correct me if I'm mischaracterizing what you're saying, but I think you said that you don't think that distinction can be made and that's why you are proposing to carve out these two groups here; can you say more about why you don't think we could clarify what we mean by physical injury?

MR. MCCULLOCH: Well, in looking back to the employment cases that led to the '96 Act that changed 104A2, you are looking at a lot of emotional distress, mental anguish claims and suits being brought, you know, being incorporated into wrongful termination type suits, and as I look at those, it's hard to know where to draw the line on the emotional distress, mental anguish issue in terms of just overall what you would call non-physical injuries. You know, certainly, if the Service wanted to make non-physical injuries excludable as they were back in the pre-'96 days, you know, that would be beneficial to a lot of folks, but I think you run up against congressional intent, which was to close the door on excludability for employment cases.

So in trying to be consistent with congressional intent and understanding that it is a very difficult task, you know, you would face in trying to carve out or trying to define physical injury, you know, we looked at, you know, one of the two most egregious instances of where we're just unable to help folks, or that there's just big questions of whether they're taxable or tax free.

So that's why we drew the line around these two particular types of cases. These are the sets of taxpayers most in need. You know, I think, looking at what Congress was doing, they wanted to make sure it wasn't transitory, that these injuries rose to a specific threshold so that they weren't just added in to get exclusion from taxation.

And I think with molestation abuse cases and long term wrongful imprisonment cases, you know, these are not people that are adding emotional distress and mental anguish or non-physical elements to get excludability, two very distinct

groups of folks, you know, and those are the two I'm here arguing for. I mean if we were arguing about excluding all non-physical injuries, I think I would be making very different arguments today.

MR. MONTEMURRO: It has nothing -- in a narrow sense, what you're asking is, these folks who have suffered these injuries, I mean they're not reporting these as taxable income, I'd assume; the question is whether the insurance company will let them structure, rather than take it as a lump sum, whether they can take the money over, you know, 20 or 30 years.

Because I mean I don't know that the Service has ever gone to court on litigation, you know, I know the Service doesn't ever go to court on litigation, anybody who's been falsely imprisoned or anyone who's suffered any sex abuse, as far as asserted in a courtroom that those kinds of damages are taxable, I mean whatever the pure technical answers may be, but I'm saying I don't know that taxpayers are reporting these as taxable damages themselves, it's the matter of whether you go to the insurance company and they'd be willing to structure it, instead of the lump sum payment that comes over time.

MR. MCCULLOCH: That's a hard one to answer. The statistical data isn't there. All that you really have is anecdotal data. For example, the Dallas Star reported when David Pope was freed, you know, they gave him a lump sum, and he actually -- interviewed him, because nine months later he dissipated it all. And the interesting thing, there is a mention in there, almost cursory, about, you know, how it was taxed. It almost is like they were going in the direction of, look, the state with the left hand compensates you for throwing you in jail, and with the right hand, takes it back in the form of taxation, there's an inequity there.

I think the wrongful imprisonment cases are being reported as taxable income; the abuse cases may or may not. I looked, I've done exhaustive research, I could not find the data there.

The Catholic Church and the Presbyterian Church were understandably reluctant to share data about whether they're doing 1099 miscellaneous reporting on these settlements, for example. So, Mr. Montemurro, I tend to agree that they're probably not, but the issue is that these taxpayers shouldn't have to worry. It should not be a roll of the dice whether your settlement is tax free or taxable. You should know if your abuse case or your wrongful imprisonment case is going to be reported and taxed.

MS. ROSS: I just want to make sure I understand what you're saying.

MR. MCCULLOCH: I'm from Chicago, our goal is to dance around the question and talk as fast as possible.

MS. ROSS: You're asking for per se rules here. Is your position that they should -- that sexual abuse and wrongful imprisonment cases should come in because they are physical injuries?

MR. MCCULLOCH: Yes.

MS. ROSS: Or that they are non-physical injuries that are at the extreme end of the spectrum, and therefore, should be treated as if they were physical injuries?

MR. MCCULLOCH: I think in the case of wrongful imprisonment, the latter is true. I think in the case of sex abuse, they are -- it's the former. Just because you can't see the impacts of an abuse or a rape doesn't mean it's non-physical.

I think with the wrongful imprisonment, it is -- you're being confined, your civil rights have been deprived, that in itself is a physical act, but when you look at the statistical data from the Journal of Epidemiology, the World Health Organization, lots of long term repercussions that even now are not fully understood, but we know that these folks commit suicide at a high rate, drug abuse, substance abuse, mental health, personality disorders, and I think that is very

distinguishable from a transitory emotional distress from being fired, or detained in a department store for a few hours because somebody accused you of being a shoplifter or something like that.

I think, as you say, it's on the extreme end of -- and I hate to use the word non-physical, I don't think it's an accurate word, I just think it is a -- rather than having the physical injury itself be physical, the act itself is physical, and a lot of the repercussions and effects are physical.

MR. MONTEMURRO: I mean that's the sort of thing -- do we do a carve-out, because there will be other situations. You could have a stalker, you know, terrorizes somebody, it never touches them, calls them on the phone, takes pictures of their kids, I know where your kids are, and that person could suffer long term, you know, is that physical, never touched them, you know, just called them, but that, you know, I mean there's -- that's always been the problem with this statute. And you've got -- so I don't know whether we want to say, well, we'll treat these two because then other folks will say, wait a second, what about this situation, what about the nine month guy, what about the stalker, what about people who are, you know, falsely -- wrongfully imprisoned, not by the state, but by a kidnapper for three or four days, maybe that happens to a child or an adult --

MR. ISKOW: Hostage.

MR. MONTEMURRO: -- yeah, a hostage, maybe they're released and maybe they were treated well while they were a hostage, but they may be still in terror of their -- of dying or being killed, you know, and you know, well, that person, though, that guy -- his, you know, if we say this one, false imprisonment in a real prison required by state law because you're falsely imprisoned by the state, that's physical, but the guy who may be kidnapped or held hostage for a couple of days by some, you know, kidnapper, well, that guy is, you know, he gets the negative implication.

That's sort of the problem of sort of cutting out two nice little safe harbors, if you want to call it, and then the other folks are still there, and you know, we still may be faced with those as an administrative matter, may accelerate those questions or exacerbate those questions more than we have now.

MR. MCCULLOCH: You know, great points, you know, especially I think this week on -- you had a book about the long term hostages down in Colombia for the three independent contractors, but that's the problem, you know, that the service and Treasury faces, how do you open the door a little bit without throwing the barn doors wide open, which is why we went for these very narrow specific situations, but they tend to be the most frequent.

I mean we do, you know, we are the largest structured settlement, you know, group of brokerage companies, we run into thousands of situations every year, and these are the two that we see that are the most prevalent.

You know, I've been doing this about 15 years, and I've only run into one kidnapping case, but we were, you know, heavily involved in the LA Archdiocese, with some of the Presbyterian Church, we were involved with some of the folks wrongfully incarcerated in Texas, trying to set up taxable periodic payments.

You know, I think those other situations are more one -- and I think can, you know, be addressed by informal calls for guidance, for example, to the field or national office, even private letter rulings. But I think that there's a sufficient number of abuse molestation victims and wrongful incarceration victims that it warrants these two separate -- if you will.

MR. MONTEMURRO: Okay, very good. Thank you.

MR. MCCULLOCH: Thank you.

MR ISKOW: Our second speaker is Richard Risk, who is representing himself.

MR. RISK: Thank you. And as I -- before the clock starts, as I mentioned here, I had prepared comments for about 15 minutes, and I'm going to skip through a lot of this, and so if the -- is not correct, it's because I left out large blocks of what I had prepared to say, unless the Chair would grant the extra five minutes. Can't do?

MR. MONTEMURRO: No, I can't.

MR. RISK: Okay.

MR. MONTEMURRO: Everybody, you know, that was the, you know, the public announcement was ten, so --

MR. RISK: All right. Well, ladies and gentlemen, Mr. Chairman, thank you very much for the opportunity to appear. My name is Richard B. Risk, Jr., I reside in Tulsa, Oklahoma and St. Petersburg, Florida. I'm an attorney whose entire law practice focuses on the aspects of tort claim settlements. I've written documents to establish more than 250 qualified settlements funds and have administered the majority of them. I've been published extensively in legal journals and have chaired tax panels for professional associations, the Society of Settlement Planners, including guest panelists from Treasury and the Internal Revenue Service. I'm appearing today on my own.

Structured settlements are a very important tool in the resolution of satisfaction of claims originally asserted by injury victims against the tort -- after the liability for such claims has been transferred by novation to the qualified settlement fund. I'll get to the tax issues in a few minutes, but first I want to present a little background of the undercurrent within the structured settlement industry that may serve to explain why we may have differences of opinion among ourselves as to how the tax codes should be interpreted.

I first came into the structured settlement community in 1986 as a producer, and eventually joined the National Structured Settlements Trade Association because it was required of anyone who sought to be appointed by the major annuity markets. At the time I joined the Trade Association, the marketing orientation for structured settlements was almost entire from the defense side. Structured settlement producers worked with corporate risk managers and liability insurance claim adjusters to propose periodic payments to injury victims, along with the attractive tax subsidy, as a way the responsible party could save money and settle claims.

If a claimant or claimant's attorney wanted to know the cost of the funding asset, the annuity, the response was that knowledge of the amount that caused the claimant to be in constructive receipt of the funding asset, and thus would lose the tax benefits.

If the claimant felt uncomfortable, allowing the structured settlement producer engaged by the defendant to handle perhaps the biggest financial transaction of their life, and wanted to engage or consult with a fiduciary duty to the claimant, the response was, take the structure that we offer or take cash.

These were hardball tactics designed to keep control of the structured settlement process for the defendants and their insurers. Loss of control meant loss of money saving tool -- of the money saving tool for the defense, and in some cases it also meant the loss of profitable annuity business for insurance groups that had life insurance affiliates, because the liability insurer could control where significant amount of settlement dollars were spent. The National Association of Insurance Commissioners calls this practice steering and describes it as an inappropriate solicitation activity.

Loss of control of the structured settlement transaction also meant the loss of sales commissions paid by the life insurance companies to life insurance agents who like to call themselves brokers as a reward for their efforts on behalf of the defendants or the insurers.

When one thinks about it, the refusal by the defense to allow an injury victim the right to engage his or her own

structured settlement specialist to handle the periodic payment arrangement is morally indefensible. After all, the claimant is the ultimate consumer of the annuity even though the tax considerations prevent actual ownership.

By the mid 1990's, the defense canard that knowledge of an annuities cost causes constructive receipt have been revealed to the plaintiff's bar is untrue, and the amount of the proposed annuity premium to be spent by the defense then became integral to the settlement negotiations. The mediation paradigm had shifted from, "we offer you a cash lump sum and periodic payments as described in this proposal", to "let's settle on the total cost to the defense of settlement and then we'll decide how much will be spent on periodic payments."

With that paradigm shift, the commission for the annuity sale, which was bundled into the annuity premium, was now part of the gross settlement amount offered by the defense. Then the issue became which side had the right to pay a structured settlement specialist using the built-in commission.

Claimants began to assert that commission was part of the settlement offer, and therefore, they were entitled to engage the services of a structured settlement specialist loyal to them and to use the commission as compensation.

This notion upset the structured settlement agencies when they were in total control of structured settlements, and the battle over who gets the commission still rages today. The National Structured Settlements Trade Association, or NSSTA, fears the use of the qualified settlement fund because it gives the plaintiffs the opportunity of the structure without involvement of the defense. As early as 1997, NSSTA began to discourage the use of the CSF except in mass torts. It turned to its text counsel, the law firm of Hogan and Hartson, who came up with the theory that a qualified settlement fund created for a single claimant resulted in that claimant having the economic benefit and the funds.

In more than one instance, Hogan and Hartson claims that some officials at the Service, in this building, agree with their theory of economic benefit attaching when there is a single claimant. And details of that effort appear in my Virginia tax review article which is cited in my written comments, and I do have a hard copy of that that I can provide for the record, beginning at page 673.

So the economic benefit theory promulgated by the defense is the new canard to replace the old one. Remember, knowledge of the cost of the annuity is constructive receipt.

Well, the irony here is that NSSTA's stated mission is to promote the use of structured settlement, but in this case it was looking for a way to stop them from being arranged without the defense participation. They were, and still are, in effect, discouraging the use of structured settlements rather than promoting them. As soon as NSSTA discovered the request to Treasury in June of 2003, submitted by three distinguished alumni of the Internal Revenue Service, the request for published guidance on the single claimant issue, NSSTA wrote a letter urging that the guidance not be published. They did not advance any liable tax theory as to why a single claimant should be deemed or have economic benefit. They simply didn't want the guidance to be published, and that seems to be their mantra, just don't publish the guidance.

I note that John Stanton of Hogan and Hartson has submitted written comments for this hearing and is scheduled to appear right after me on behalf of NSSTA, and I believe he has submitted the 2003 NSSTA letter for the record of these proceedings. This is simply another way of saying don't publish the guidance.

His stated purpose, I understand, of being here today is to refute my suggestion, that the economic benefit issue be resolved -- can be resolved easily in the proposed revision, *Section 1.104 of the regulations*, on the basis that my suggestion exceeds the scope of the proposed revision. Of course, the scope should be whatever is needful, using a word from the statute, in order to clarify Code *Section 104*. I suppose I should be flattered that NSSTA used me as a threat to disrupting the status quo, and I hope that speaks for the credibility of my remarks today.

Now, let's get to the tax issues. I understand that branch four has limited the scope of the proposed revision to a couple

issues in order to avoid the type of controversy that has stalled this project in the past. But the scope of this project should be determined by the necessity for guidance related to the tax code, *Section 104*, and not limited for the convenience of staff.

This issue is primarily a Code *Section 104* issue, and the corresponding regulation is an appropriate place to clarify how the code will be interpreted. I sincerely hope you'll recognize the legitimate need to clarify and that the law requires such clarification, and I refer to *Section 7805D* of the code.

There's simply a duty to the taxpayer constituency, a statutory duty of that to provide the guidance. This need is compounded by the fact that certain people within this building reportedly have made comments being used by the defense community to promote fear among those who would otherwise employ the qualified settlement fund for the benefit of their clients. I'm not asking the Service to develop a new policy to clarify this issue. I submit that the policy is already in existence, except that one must go to several different sources to piece it together.

The proposed scope of the regulation, of the revision rather is to incorporate some legislative history dating back to 1996, that's 14 years ago. What about the legislative history from 1982 that never got included in the regulations? That's 28 years ago, twice as long.

I elaborated in my earlier written submission on the policy that already exists, and I won't repeat it here for the record.

So I urge this panel to consider the writings of Jeremy Babner, who submitted his article on the single claimant issue for the record. The point here is that all these events I've described above and in detail in my previous submission, as well as in my Virginia tax review article, demonstrate that Congress, Treasury, including the IRS, and the courts have spoken on the single claimant issue, confirming that economic benefit does not attach in periodic payment arrangements. The rule is still from all of these events to be appropriately inserted into the corresponding regulations for Code *Section 104*. I previously provided proposed text, one single paragraph, for your consideration. Is that it? That's it, okay. All I can say is, please don't forget, you're here to serve the people, not the other way around. Thank you.

MR. MONTEMURRO: Very good.

MS. CRISALLI: I have a couple questions. If the defendants have so much leverage that they can say, take this structured settlement or you get a lump sum, why don't they have leverage to say if you don't use a QSF, we offer X, but if you use a QSF, it's X minus Y?

MR. RISK: I've heard that, I've heard that that's employed.

MS. CRISALLI: So in that case, you know, if the plaintiff has enough leverage to counter that, wouldn't they have enough leverage to counter without using a QSF?

MR. RISK: I'm not quite sure I'm following you, and maybe I'm not the right person to try to answer that.

MS. CRISALLI: Well, you're suggesting that without a QSF, the defendant can impose its will in terms of the settlement --

MR. RISK: That's true.

MS. CRISALLI: -- and I'm saying that even with a QSF, if the defendant had that much -- I'm asking, I'm suggesting, I don't know, if the defendant had that much power, perhaps they could also --

MR. RISK: I used to be in that position.

MS. CRISALLI: -- undermine the use of a QSF?

MR. RISK: I used to be in that position. I would show up at mediations, and the defense person would literally scoff at me and say why are you here, this is my case, I am representing insurance company X, this is my case, you're going to go home with nothing, and at some point in the span of time, it was figured out that we could use the qualified settlement fund to replace that defendant. After all, the only thing the insurance company really should want is the release and the dismissal from the action, and so they could get that, they could get your tax deduction by the QSF, and that's an incentive.

And the courts will recognize this, too. The courts will recognize that if you create a qualified settlement fund and say to the court this is simply an entity to receive the settlement proceeds and give the plaintiffs then the time to make some informed financial decisions that they would otherwise be pressured into making at the time of the mediation. The defendant is out of the picture, and it would be a beneficial interest if they still wanted to impose their will and direct where the annuity goes. So I'm not sure that the carrot on the stick, so to speak, will give you a higher amount. I haven't really used it -- heard it used in that context, I've heard it used in -- you need to structure, and if you structure with us, we'll give you so much money, and if you don't structure, it'll be a cash lump sum of a lesser amount, which seems to suggest that there is a profit motive for the defendant.

MS. CRISALLI: Let me ask you the question I asked the last speaker, although I'll rephrase it. How do you think we could include a rule like this in a final reg under the APA without having proposed it first, a rule such as you suggest in your written comments?

MR. RISK: I'm not sure, I mean I don't understand the workings of the process as well as you do, but I assume that there's an opportunity for you to restate your proposal.

MS. CRISALLI: Well, we could repropose, yes, and then that would delay the effectiveness of the other rules that we have in there.

MR. RISK: Excuse me, but we're now 14 years into this.

MS. CRISALLI: Well, I understand.

MR. RISK: And maybe 28 years.

MS. CRISALLI: I understand.

MR. RISK: Okay. So time may be of the essence, but an additional six months.

MS. CRISALLI: Well, another possibility you might consider is suggesting, when it comes time to make comments on projects for the new business plan, that this be resurrected as a separate project, which would then allow us to propose something if it went out in a reg without delaying the other reg.

MR. RISK: Would it be appropriate to ask why it was terminated or removed from the plan after four and a half years?

MS. CRISALLI: You could ask that, but we won't answer.

MR. RISK: Okay. And I guess my response would be --

MS. CRISALLI: And nobody is supposed to know anything about that. So all these rumors you hear, you know, aren't

worth the paper they're not written on.

MR. RISK: Well, it's not on the plan. I guess my immediate reaction was that because of this project, that you were going to include the guidance and that's why it was removed from the "to do" list.

MS. CRISALLI: Okay. Well, obviously that wasn't the case.

MR. RISK: Okay.

MS. CRISALLI: So if you think that this warrants our attention, you might consider, when the notice goes out around April-ish timeframe, soliciting ideas from the public, submitting a letter suggesting that we resurrect it.

MR. RISK: Would the same consideration then apply, because there's some darn good recommendations here regarding the definition of physical injury --

MS. CRISALLI: Absolutely.

MR. RISK: -- and that's beyond the scope of your proposal.

MS. CRISALLI: Absolutely.

MR. RISK: So I guess what -- if I understand you correctly that -- you're saying we're going to go ahead with the proposal that we've made and then it would be a whole new ballgame then if we considered other things?

MS. CRISALLI: I'm not saying anything.

MR. RISK: Okay.

MS. CRISALLI: But I am saying that one possibility would be to finalize the reg without these new proposals and address them in a separate guidance project rather than hold everything up to repropose. In other words, there's no reason why your proposal or the proposal without defining physical injury has to be attached to this project; it could be a separate project.

MR. RISK: Okay. I would agree with that. I have a little familiarity with the way the bureaucracy works. I was in the -- I was an Air Force officer, a squadron commander and a staff officer and a general's aide for several years, and I also ran a federal agency, and I do know that there are sensitivities of stepping into somebody else's bailiwick and whatever, and I thought that maybe because this had been at Treasury for four and a half years, that maybe it was untouchable.

MS. CRISALLI: I don't think that there is any -- that it would be any easier to get us to revisit this issue by attaching it to this project than by creating a new project. I don't, you know, the issue is going to be what are the other priorities on the business plan, do we have the resources, you know, is this of significant importance or more important than other projects that are vying for attention, and that would be the case whether we repropose these regs and wrap it into that or do another project. So you have to convince us that this is of more importance than other projects, that's the key.

MR. RISK: I've done my very best.

MR. MONTEMURRO: I guess we're done.

MS. CRISALLI: Thank you.

MR. MONTEMURRO: The next speaker.

MR. ISKOW: The next speaker is John Stanton of the National Structured Settlements Trade Association.

MR. STANTON: Good morning. I'm John Stanton, I'm a partner with the Washington law firm of Hogan and Hartson. I represent the National Structured Settlement Trade Association and I'm here to continue the discussion about the dogs that didn't bark, but --

MR. MONTEMURRO: Maybe raise your voice a bit, a little louder.

MR. STANTON: On behalf of the Association, we would like a chance to respond. Some structured settlements have been invoked here. By way of background, the National Structured Settlement Trade Association, NSSTA, is the trade association of the structured settlement industry. It represents the entire industry, ranging from the plaintiff and defense brokers who work with the parties at the settlement table to develop, negotiate and implement the structured settlement, the life insurance companies who, under the congressional tax rules, create structured settlements, fund the structured settlements by way of annuities, the casualty companies that use structured settlements, participate in structured settlements to resolve their liability claims, plaintiff attorneys, defense attorneys, those that are active in the field.

You've got some important issues to address in this project, but our view is that structured settlements is not one of them. As you know, the project does not address structured settlements, and we see no reason to do so.

The suggestion has been made that the project be used as an opportunity to address this issue of a trust report to be created under *Section 468B* to -- for the benefit of a -- claim entered to a structured settlement. That issue is not addressed in the proposed regulations, it's beyond the scope of the proposed regulations, and we see no reason to address that issue by way of the vehicle of the project before you particularly since, as was noted, the guidance project regarding the single claimant, 468B, was dropped from the priority guidance plan.

Let me just say by way of background that structured settlements have been around for about 30 years and they work quite well. The structured settlement tax rules that were adopted by Congress in 1982 lay out a bright line path that's been followed in hundreds of thousands of structured settlements by claimants.

Structured settlements in which both sides today are represented by their own brokers, their own lawyers. Structured settlements enjoy broad support among the plaintiffs, by the defense, by the claims community, judges, mediators, the federal government.

The federal government engages in structured settlements quite lively to resolve federal -- cases, vaccine compensation cases, military hospitals. We see no reason to use the vehicle -- the project before you to reopen the structured settlement tax rules that have worked quite well over time. So, with that, I'd be pleased to answer any questions that you may have. I appreciate the opportunity to appear today.

MS. CRISALLI: Nope.

MR. MONTEMURRO: Okay, very good.

MR. STANTON: Thank you.

MR. ISKOW: Thank you.

MR. MONTEMURRO: That completes the list of scheduled speakers. So I'm just going to open up the floor. If anybody else wants to speak, raise your hand and come on down, introduce yourself and whether you're speaking on behalf of

yourself or an organization. You had your hand up first, so you go first.

MR. MILLIGAN: Thank you for this opportunity to be heard. My name is Jack Milligan, I live in Portland, Oregon, I am a cofounder and co-President of Settlement Professionals, Incorporated, a 23 office nationwide firm that specializes in settlement planning directly with and on behalf of the personal injury victim.

I have been actively involved in the structured settlement and settlement planning industry for 25 years. I am a founder of the Society of Settlement Planners, SSP, and served as that organization's first president for its first three years.

I am a former member of NSSTA, the National Structured Settlement Trade Association. The SSP's members take an oath of loyalty to personal injury claimants and devote 100 percent of their practices and efforts to assisting these unfortunate victims to plan their settlements and their entire financial futures. The SSP is a professional trade association as opposed to being an industry trade association. The SSP does not have voting membership categories for annuity life insurance companies, for casualty insurance companies, for personal injury plaintiff or defense attorneys, or claim adjusters. Only our professional practitioner members are allowed to vote or hold office.

The SSP Mission Statement is to promote and preserve the rights of personal injury claimants to choose their advisors and product providers as they plan their personal injury settlements.

I am here today representing the SSP, in support of the effort to make the much-needed changes to *Section 104A*, as expressed by Mr. McCulloch in his comments, and also by Mr. Higgins in his written comments to this panel, and to support Attorney Richard Risk's suggestion that this effort include simple language that will positively assure personal injury victims that the doctrine of economic benefit will not apply to a qualified assignment emanating from a single claimant, QSF. I am also here to refute certain statements made by Mr. Joseph Ricci, the Executive Director of NSSTA, in his letter to this panel, and also just now by Mr. Stanton. In his letter, and in Mr. Stanton's comments, both assert that the insurance industry organization, NSSTA, represents all professionals in the structured settlements industry, both defense and plaintiff, and that all are opposed to Mr. Risk's suggestion, this is -- false.

NSSTA does not represent me, nor the merely 50 members of the SSP which includes both financial as well as legal settlement planners from around the country, all of whom have a stake in *Section 104* on a daily basis, and all of whom join me in urging this Committee to consider Mr. Risk's suggestion including guidance.

Mr. Ricci also states that issuing positive guidance would have a detrimental effect on the usage of structured settlements. Mr. Ricci cites no authority or study for this position, and indeed, NSSTA's own data would seem to support an entirely different position, in conclusion.

NSSTA's annual measurement of the growth of the industry seems to coincide with the proliferation in QSFs as the structured settlement industry has seen premiums grow from approximately four billion in the mid '90s to over six billion in the year 2008. Now, admittedly, some of this growth can be attributed to inflation in the general economy as well as inflation in medical expenses for our injury victims.

However, over this same timeframe, we have seen a proliferation of QSF's, Qualified Settlement Funds. In my office, I have been involved in over 200. My associates and peers have been involved in many hundreds more. One would think that with this dramatic increase in the usage of QSF's, that the utilization of structured settlements would have dropped if Mr. Ricci is to be believed. To the contrary, their utilization has increased. Why is this?

I'd like to give a brief history of this industry as I have seen it. In 1985, when I entered nearly complete control of this industry, it was through the defense side. They selected their brokers, they dictated the annuity companies and trust companies that the plaintiff would use. Plaintiff specialists like myself were denied access to the annuity markets by life insurance companies. Defendants, in essence, held 104A captive; as Mr. Risk described it, the carrot at the end of the

stick. The plaintiffs could not give the benefits of 104 unless they accepted defense's choices of not only their brokers but the annuity companies, where they wanted the business to go. Also, most cases, no matter how large, were funded with a single annuity from one just -- from just one life insurance company. The plaintiffs at the time, many plaintiffs rejected structured settlements simply because they couldn't choose their own expert and they ultimately couldn't choose the companies that would be responsible to them. And they couldn't, in many cases, buy the fact that the people who caused their injuries would somehow profit from the settlement of their claim, and they could do nothing about that.

In 1988 through 1990, the Wild lawsuit occurred, and this, in essence, resulted in life insurance company appointments for people who worked on the plaintiff's side of the business. Up until that time, we couldn't even get access to the annuity markets with which to help these injury victims that we represented, a landmark situation for us.

In 1991, Executive Life of California went through a solvency crisis and entered conservatorship. First time in history that some personal injury victims suffer a partial loss of payment due to this insolvency. Diversification of annuity company risk becomes imperative from this time forward and plaintiffs begin to look for their own experts. 1992, regs regarding QSF's were issued; '96, the industry recognizes that QSF's have game changing potential as personal injury victims and no longer have to be subject to the disclosed or undisclosed financial agendas of the people who caused their injuries.

Defendants have sought to make all the choices for plaintiffs without remaining accountable or reliable for those choices. Instead, we see exactly what they were entitled to, a full, complete and irrevocable release from liability, nothing else.

Personal injury victims could now choose their own advisors and then select the companies. The annuity issuers and the trust companies would ultimately be responsible to them for their future payments. And they could diversify the risks in these transactions by selecting two or more companies as their guarantors.

2001, SSP is formed. Why? Because the NSSTA did everything in its power to marginalize those of us who work for plaintiffs, and NSSTA was perceived to be working against the rights of plaintiffs to choose who they wanted to work with. Also, the organization had become dominated by insurance companies, whose agendas included controlling commission flow from annuity policies so that portions of those commissions could be captured as profits. Also, the term "asset retention" became very popular at this time as insurance companies sought to capture claim dollars and transfer them to wholly owned insurance company annuity issuer affiliates. SSP believed that 104A2 was meant to benefit injury victims, not the --

2002, the use of QSF's explodes. NSSTA members pushed back, claiming that one or more language does not mean "one or more", and that economic benefit doctrine would apply. 2003, SSP submits request to Treasury for published guidance. IRS adds it to their business plan, 2004.

2008, financial meltdown. AIG and Hartford, big structured settlement annuity providers, both are in the forefront.

Interestingly, these two companies, along with the Department of Justice, are the two biggest or the three biggest perpetrators of forcing plaintiffs to follow their agenda and follow their will in where they want the settlement and claim dollars to go, with DOJ even denying claimants the right to have their own expert and to have that expert compensated out of the transaction that ultimately settled their case. So now here we are, and I on behalf of future personal injury victims, and the professionals that work with them, both financial and legal planners across the country, respectively ask you to consider adding positive guidance to 104A regarding single claimant QSF's: that economic benefit does not apply to disqualify a qualified assignment.

MS. CRISALLI: Do you think that plaintiffs really have no power to push back on defendants in terms of how they -- where they go for the structured settlement without using a QSF?

MR. MILLIGAN: Prior to --

MS. CRISALLI: I mean do they have people like you to support them and advocate for them?

MR. MILLIGAN: -- prior to the creation of Qualified Settlement Funds in 468 cap B, it was extremely difficult. The personal injury victim had to have an exceptionally strong legal advocate to gain any traction at all.

MS. CRISALLI: Well, how about now?

MR. MILLIGAN: Now we have the QSF.

MS. CRISALLI: Without the QSF, if you don't use a QSF.

MR. MILLIGAN: Well, that's like saying let's roll the ball back up the hill and imagine what the situation would be. If we didn't have QSF's, I imagine it would be the same as it was prior. But now, because of their existence, we can't really put that genie back in the bottle, and what has happened is that the mere fact that QSF's are available is enough to persuade many times the defense side of these cases that they should try to acquiesce to the plaintiff's demand.

MS. CRISALLI: Well, that's my point exactly.

MR. MILLIGAN: Okay.

MS. CRISALLI: Is it the mere threat of the QSF helpful?

MR. MILLIGAN: It is, except in the case where we now have companies and the Department of Justice who are, as part of the negotiations, telling the plaintiff, if you think you're going to use a Qualified Settlement Fund, think again, we will oppose it, it's a risky tax transaction, it's not proven, we believe economic benefit would apply, and the tax consequences would also come back to us on the defense side.

MS. CRISALLI: I assume then that plaintiffs that use QSF's are applying the 104A2 exclusion?

MR. MILLIGAN: Yes.

MS. CRISALLI: They're not treating it as taxable?

MR. MILLIGAN: Yes, that's true.

MS. CRISALLI: Okay.

MR. MILLIGAN: And single claimant QSF's are being used around the country for those brave enough to step out and say, my advisors have told me, explained what the code says, that these can be used for one or more claims, and I'm going to believe that the code says what it says.

MS. CRISALLI: Thank you.

MR. MONTEMURRO: Okay. Is there anybody else who would like to speak?

MR. LEYDEN: Good morning, Mr. Chairman, ma'am. I am Edward Leyden, I'm here -- I'm a partner at the law firm Hallwell Leyden, but I'm here today in my capacity as President of Consumers for Civil Justice. At Consumers for Civil

Justice, there's a *Section 501C6* trade association comprised of attorneys here in the metropolitan Washington, D.C., area who fight for the rights of people that have suffered harm from discrimination and from the wrongful acts and omissions of others, in short, the plaintiff spot, as we've heard described. We view the tax policies underlying *Section 104A2* to be both wise and well founded because the financial compensation that one may receive in a court of law or as the result of a legal settlement for physical harm and pain is certainly not an accretion of wealth by any measure. It is, thus, entirely fair and proper that such sums be statutorily excluded from income and not subject to taxation.

CCJ further applauds the clarification that the Service is linked to *Section 104A2* and that that -- since 1996, when Congress substantially modified the statute, and especially the thought and insight that went into the proposed regulations that are the subject of this hearing today.

However, we do echo the concerns expressed by Stuart Lewis in the American Bar Association section of taxation concerning the need to clarify that compensation, for physical injuries and sickness comes within the ambit of *Section 104A2*, even if such harm resulted from a wrongful act that did not encompass physical contact or touching. Such qualification will be manifestly consistent with the policy considerations underlying these proposed regulations and of a whole with the thoughtfulness and compassion that ultimately animates them. In the interest of full disclosure, I should point out that while I'm a currently serving officer of the ABA Section of taxation, at which I share the Committee for Employment Taxes, that's not the capacity that I'm here today, and I had no part in writing or preparing the comments that the ABA tax section itself submitted.

I thank you for this opportunity to testify on behalf of our Association, and, of course, would be delighted to answer any questions that I may.

MR. MONTEMURRO: Fine.

MR. LEYDEN: Thank you.

MR. MONTEMURRO: Very good. Okay. Is there anybody else who would like to speak this morning? Okay. Then I thank you all for coming this morning and setting forth your views, and we'll be working here on the regulations and trying to move them toward the final product, and I think you all for coming, and the hearing is adjourned.

(Whereupon, at 11:08 a.m., the HEARING was adjourned.)