NATIONAL COUNCIL OF INSURANCE LEGISLATORS
FINANCIAL SERVICES & MULTI-LINES ISSUES COMMITTEE
2024 NCOIL SPRING MEETING – NASHVILLE, TENNESSEE
APRIL 13, 2024
DRAFT MINUTES

The National Council of Insurance Legislators (NCOIL) Financial Services & Multi-Lines Issues Committee met at The Sheraton Grand Nashville Downtown Hotel in Nashville, Tennessee on Saturday, April 13, 2024 at 1:45 p.m.

Senator Mary Felzkowski of Wisconsin, Chair of the Committee, presided.

Other members of the Committee present were:

Sen. Justin Boyd (AR)
Asm. Tim Grayson (CA)
Rep. Matt Lehman (IN)
Rep. Edmond Jordan (LA)
Rep. Brenda Carter (MI)
Sen. Paul Utke (MN)
Rep. Bob Titus (MO)
Rep. Nelly Nicol (MT)
Sen. Jerry Klein (ND)
Rep. Emily O'Brien (ND)
Rep. Tim Barhorst (OH)
Sen. Bob Hackett (OH)
Rep. Brian Lampton (OH)
Sen. George Lang (OH)
Rep. Forrest Bennett (OK)
Rep. Ellyn Hefner (OK)
Rep. Tom Oliverson, M.D. (TX)
Rep. Jim Dunnigan (UT)
Del. Steve Westfall (WV)

Other legislators present were:

Rep. Deborah Ferguson, DDS (AR)
Rep. Jeff Keicher (IL)
Sen. Mike Gaskill (IN)
Rep. Peggy Mayfield (IN)
Sen. Beverly Gossage (KS)
Sen. Mark Huizenga (MI)
Rep. Jerry Neyer (MI)
Sen. Natasha Marcus (NC)
Sen. Bill Gannon (NH)
Rep. Mark Tedford (OK)
Del. David Green (WV)
Del. Walter Hall (WV)

Also in attendance were:

Commissioner Tom Considine, NCOIL CEO
Will Melofchik, NCOIL General Counsel
Pat Gilbert, Director, Administration & Member Services, NCOIL Support Services, LLC

QUORUM

Upon a Motion made by Sen. Bob Hackett (OH), and seconded by Del. Steve Westfall (WV), the Committee voted without objection by way of a voice vote to waive the quorum requirement.

MINUTES

Upon a Motion made by Rep. Brenda Carter (MI) and seconded by Sen. Hackett, the Committee voted without objection by way of a voice vote to adopt the minutes of the Committee's November 17, 2023 meeting.

DISCUSSION ON NAIC'S "FRAMEWORK FOR REGULATION OF INSURER INVESTMENTS", INCLUDING PROPOSAL RELATING TO SVO'S RATINGS DISCRETION PROCESS

Sen. Felzkowski stated that we're going to start out discussing on National Association of Insurance Commissioners (NAIC's) "Framework for Regulation of Insurer Investments", including the proposal relating to the Securities Valuation Office (SVO's) ratings discretion process. We had a good update on this topic yesterday during the NCOIL-NAIC Dialogue and now we'll have a chance to discuss it in a little more detail. For those who weren't at the dialogue yesterday this topic has generated a significant amount of discussion throughout the past several months. And it deals with the NAIC's proposed "framework for regulation of insurance investments" which you can view in your binders on page 104. Within this framework, there's a specific 15 step process set forth that enables the SVO to review all filing exempt securities and to determine whether the rating is unreasonable for regulatory purposes. That 15 step process is on page 111 in your binders. All materials are on the website and app as well. Concerns have been raised by many regarding the framework, mainly focusing on the SVO's authority to overrule the decisions made by rating agencies. We do applaud the NAIC for making progress on the proposal and its willingness to engage in discussions and hear concerns. With us here today is the Insurance Commissioner from the great state of Wisconsin and Chair of the NAIC's Financial Condition "E" Committee, Nathan Houdek.

Cmsr. Houdek thanked everyone for the opportunity to speak and stated that I'm going to provide a little bit of background information before I dive into a little more of the substance of the framework. Some of this might be familiar for those of you who were here for Rhode Island Superintendent Beth Dwyers' presentation last fall when she talked about the investment framework. As state insurance regulators one of the key things we're charged with is ensuring the financial solvency of insurers and as part of that being able to properly analyze investments is really a key function of financial solvency oversight. And what we've really seen and I mentioned this yesterday during the dialogue is we've seen a material and observable shift in insurer investment strategies over the last decade or so, really since the great financial crisis. And we've seen a move towards more private assets, more structured assets, more complex assets. And from our standpoint as regulators just less transparency overall in terms of being able to analyze the risk associated with these newer investments. And so the framework is really we're trying to determine the most effective use of our regulatory resources in this new modern environment of these more complex and more challenging investments so that we feel comfortable that we understand the risks associated with them. And that's really what this project is focused on is how do we enhance the ability of us as regulators to do that financial solvency work and ultimately to protect policyholders and consumers?

The framework document was initially exposed at the NAIC Summer National Meeting last year. During that exposure period, we received comment letters from 17 different organizations, as well as oral comments that were presented by many of those same groups at the fall National Meeting in December. We then put together a small drafting group, which was comprised of regulators who really have subject matter expertise in this area. And they spent the winter months I would say kind of December, January, early February drafting three documents based on the comments we had received and just other information that has come to light since we initially exposed the framework. Those three documents were first a proposed work plan laying out I believe seven action items in terms of kind of next steps of how we move the framework project forward. Second was an update to the framework document itself, fairly minor revisions at this point, but a few changes that we thought were helpful. And then a third more substantive memo kind of generally to interested parties with responses to the comments that we had received during that initial comment period. We then exposed those three documents in February for a comment period that ended just this past week on April 8th. And we also had our spring national meeting last month that provided an opportunity for interested parties to provide verbal comments. I think we had five or six different groups that did that. And so, where we are now is essentially the drafting group members and the E Committee members are now going to go through those most recent comment letters that we had received and spend the rest of this month and next month with the idea then we will revise these documents that had been exposed earlier this year and determine if any additional documents or whatever additional information might be needed based on the comments and expose those for an additional comment period, likely in June. So, there will continue to be a lot of opportunity for all stakeholders and interested parties to have transparency into how we're doing this process and know the changes we're making and providing feedback and providing comments. That's something we've committed to and something that as the process continues we'll definitely adhere to.

So included in the work plan document that was exposed earlier this year were six core principles of the investment framework. The first being that the framework we're putting out there to settle long term strategic direction for really where investment regulation is going to go in the future given these changes that I talked about structured asset, private assets, more complex assets. And also to help ensure that both the current and future initiatives that are happening under the E Committee are coordinated and really supportive of this longer term direction. Second, we really want to ensure that insurance regulators have the appropriate tools, and that's something that you'll hear as I kind of talk through some components of the framework is it's' really about enhancing our resources, our tools and the policies that we have in place to ensure that we can have the appropriate oversight of these new investments. The third principle really restating and just reiterating the fact that the work that has been going on related to the framework will continue and there will not be a delay. We want to ensure that work and those work streams are directionally consistent with where we're going with the framework and we will continue to look at that work and make sure that is the case. But there is no intention to pause or to stop that work. And fourth and this is something that we've heard some concerns and criticisms about, we really want to reiterate that this work is being driven by regulators at the Commissioner level. Yes, we might be hiring consultants for some of the work which we will be transparent about. Yes, we rely on the SVO staff and NAIC staff. But it is really the regulators and Commissioners, E Committee in particular, that is really driving this work and who are benefiting at the end of the day from all of these enhancements and resources that we're developing. It's really about the fact when you have 56 different jurisdictions that oversee the regulation of insurance it's not practical for each of those jurisdictions to build out the full capabilities on their own from a cost standpoint to be able to do in depth analysis of investments. So, what we're trying to do is do this in a coordinated way where we have a centralized location, the SVO, or whatever the SVO will look like in the future, that benefits all of us as regulators in those 56 jurisdictions. The fifth principle is we're committed to being fully transparent and continuing to have multiple checkpoint exposure periods, comment periods throughout this process. And last, we really want to reiterate that while we're doing this work to bolster our resources, to improve oversight of the ratings from the credit rating providers (CRPs), at the end of the day it's the ultimate responsibility of the insurers to have prudent oversight of their investment. And the work that we're doing doesn't mean that that oversight should be outsourced to regulators. It just means we have to do this work from a regulatory standpoint so that we feel comfortable with the tools, resources and knowledge that we have.

So I'm going to dive in to kind of peel back the framework a little bit and talk about some of the specific proposals that are included in the framework and I'm trying to move through this quickly to provide time for questions at the end. So, the first proposal relates to the issue that we talked about this idea that right now as consumers of ratings from CRPs, the NAIC and insurance regulators really have to blindly rely on those ratings. And a big part of what we're trying to achieve here is to move from blind reliance to informed reliance. We really want to create both quantitative and qualitative parameters that the CRP's have to meet so that we feel comfortable with the ratings that are being provided to us again as consumers of those ratings that there is uniformity and consistency in the level of quality in the ratings that are being performed. And that's really a big part of what we're working through here when we talk about this idea of having more oversight of the ratings and how those track to our NAIC designations. Second, kind of related to that, we want to retain the ability of the SVO to perform assessments of individual securities and to utilize the discretion which we've talked about that is being developed so that when there is identified some concern or anomaly that the SVO has the proper tools to do that credit assessment and utilize the discretion process that has been laid out through those 15 steps. The third proposal - currently, the SVO is really set up to do credit assessments of individual securities and as we're looking to enhance the tools that we as regulators need to understand this more complex investment environment, we really need to look at enhancing the risk analysis capabilities of the SVO itself to move beyond individual credit assessment to look at company specific, company-wide portfolio assessment as well as looking at kind of risk assessments across the industry. This is really in line with the risk focused surveillance move that the regulatory community has been making over the last few years and ties in with broader macroprudential regulatory oversight efforts and responsibilities. So think about it as rather than waiting for some event to occur that leads to a problem, we're trying to develop the tools and build out the resources so that we can identify problems on the horizon and try to take steps to address those before they become a bigger problem. Fourth, we want to continue to build out the modeling capabilities. Again, these are all pieces of a broader whole so if there's a challenge to a particular rating based on the discretionary process we want to have the modeling capabilities to be able to do the proper assessment and analysis within the SVO. So, building out those additional resources and the governance associated with that is going to be a critical piece of that.

Fifth, we also want to add some policy advisory functions at the SVO. So, instead of just doing credit assessments of individual securities we want to add the ability to have some advisory services that could benefit all of us as regulators to really understand what are some of the emerging issues and potential problems that we need to be aware of as we continue to see the investment landscape shift in the coming years. This is something that's similar to how the American Academy of Actuaries supports the NAIC and state regulators right now in terms of our risk based capital (RBC) and reserving initiatives. This would be similar, but more focused on the investment side. Sixth, currently we have two regulator-only working groups that are really designed to provide a forum for discussion about confidential troubled company specific information. And those are referred to as the Financial Analysis Working Group (FAWG) and the Valuation Analysis Working Group (VAWG). Proposal six would have us develop a similar regulator-only working group that would provide a confidential forum where we could just discuss investment related risks and concerns in a way where we could bring in a broader regulatory group to really understand across states, across different subject matter experts what are issues that we as the broader regulatory community need to be aware of as it relates to the shifting investment landscape and the challenges that might be associated with that. And lastly, the seventh proposal relates to kind of some restructuring of the SVO and renaming the SVO and the Valuation of Securities Task Force (VOSTF) to better reflect the responsibilities that these groups should have based on all the changes that I just talked about as well as making sure the

SVO is empowered to utilize these new tools and resources that we intend to develop to support not just regulators across the country but the various working groups and other committees under the NAIC structural overall. And then also look at potentially reducing the size of the VOSTF membership to encourage more active participation and membership who have more of a subject matter expertise and really are willing and able to dive into these issues in a more substantive way.

So, in conclusion, there are four points I want to touch on. Again, these are really tools and resources that we're looking to develop to make sure that we as regulators can properly analyze the risks associated with these new investments to ensure that companies remain solvent. The ultimate goal is equal capital for equal risk. So, capital requirements, capital charges should be the same for similar types of investments and that's not always the case right now, and we're hoping with better tools, with better resources that we can do a better job of accomplishing this goal of equal capital for equal risk. Related to that, as the financial regulators, the more we can capture the accurate risk and assess the appropriate capital charge the more we can reduce the need and desire of companies to pursue regulatory arbitrage. So if we can get all these other parts right we should create an environment where we don't see companies trying to take advantage of loopholes and opportunities for regulatory arbitrage. And then the last point to make is the SVO and regulators overall are completely committed to continuing to rely on CRPs and the ratings that they provide for NAIC designations. There is no goal to have the SVO compete with the CRPs. There's no goal to put any of the CRPs out of business. The goal is again to ensure that right now we have to blindly rely on the ratings that come from CRPs that feed into our designation process which have an impact on capital requirements and accounting standards and a number of other functions for us as regulators. We want to shift that to being a system where we have informed reliance on those ratings. And ultimately that's the change that we're looking to do with regard to CRPs. There's no way that the SVO could take over or in any way compete with the work that the private CRPs do and we don't want that to happen from the E-committee standpoint. We're not pushing that. There are no task forces or working groups that are pushing that. So, that's something we always like to reinforce because I know there's some misinformation out there about that but there is no attempt to compete with or displace any of the CRPs.

Rep. Matt Lehman (IN) stated that we've been talking about the SVO for the last several meetings and even at some of our meetings with the NAIC. There are a couple of things that still may be a bit of a concern that I'm hearing. In the 15 step proposal, there's some language in here about, well we'll review, but if we're off three points we'll discard that rating and use our rating or we'll discard the rating, and then one of your bullet points there was to use the term "empower" the SVO. And whenever I see the word "empower" I just wonder where that's going to go. Because it does concern me that when you said we don't want to compete and it's just a resource. And so my only concern is I don't want to see that creep over into that becomes our rating service and we don't really need them anymore. So that'd be my only concern and as we keep moving forward on this, I think it needs to be something that we continue to have a dialogue about. Cmsr. Houdek stated that I appreciate that feedback and I know the discretion and oversight process is still in the process of being developed. I talked with the VOSTF Chair on Thursday and the plan is to take the most recent round of comment letters and take the rest of this month and into May and continue to refine and update the 15 step process. And the overall kind of process that's being laid out with regard to discretion, I don't know the details enough to speak to those issues but just know that there is additional analysis being done in initial kind of refining being done in terms of the feedback that we've been getting on some of these issues.

Sen. Bob Hackett (OH) stated that we went through 2008 and 2009 and we had a major crisis, not as much a crisis in our area, but a crisis in the financial markets. And the major mistake that was made was made by rating services with mortgage-backed bonds. The only thing that I worry about is, did we learn from the past? People made mistakes. That's the way those bonds were rated. They were rated tremendously different than they should have been under that scenario. And so I understand what you're trying to do and I commend you for what you're trying to do but in the same token, it still worries me that we might hit a crisis because we only look at the rating services and not other areas like the consultants and other things. Cmsr. Houdek stated that I know what you're saying and I think the tools and resources that we're talking about will hopefully identify those risks and potential problems. But I think to your point, it's then incumbent on us regulators to take action when we see problems. And I wasn't in a role at that time to have done anything but I think we need to continue to proactively identify where there are risks in the system, where there are potential problems and try to identify those and when necessary, take action to mitigate and prevent those risks from becoming bigger problems. So, I don't have an answer because all I can say is hopefully, we're doing the right thing and hopefully when that time comes these tools and resources that we've developed will serve us well and the right action will be taken to prevent those kinds of things from happening.

INTRODUCTION AND DISCUSSION OF NCOIL TRANSPARENCY IN THIRD PARTY LITIGATION FINANCING MODEL ACT (Model)

Rep. Lehman stated that I'm really privileged to be able to bring this Model before the Committee today and you can look at it on page 235 in your binder. For those of you that may have been around here awhile, this issue first hit NCOIL's radar screen in 2011 at our Annual Meeting in Santa Fe, NM and then over the next three years myself, Sen. Neil Breslin (NY), and Rep. Charles Curtiss (TN) worked on some language and came to a final vote at the Annual Meeting in 2014 and it failed 15 to 14. But there's been a lot of discussion as to what's changed since then. Well, it's been a decade and I'll tell you what's changed. I think we've seen a growth in the consumer space, we've seen some growing changes that I know in Indiana we've addressed and some other states have as well. The other thing is we've seen the influx now in the commercial space and I think that's what's really caught our attention as public policymakers because we're beginning to see more and more of these lawsuits turning into nuclear verdicts. And eventually we the policyholders bear the brunt of that. And what was troubling in a way I would say is we began to see or did not see who was behind the funding. Who's putting the money into this process? There was no transparency in that. We began to see cases where they were directing the case. They were directing the suit. The funder was. We began to see that some of these cases might be around not so much an investment to get a return on that money but simply I'm data mining. I'm going to sue Google because I want their mapping technology and as long as I can be a seat at that table maybe I'll get that data. These were coming from foreign investors. They were coming from foreign countries. And you saw articles after articles began to hit. And the one quote I really liked just said "our courtrooms have become a trading floor." And I'm a student of history. I've read The Federalist Papers multiple times. And never did I find anywhere there where our founders wrote the judicial branch to be set up as an investment tool. And so I think we have to be very careful when we get into this world of the judicial branch and litigation. Now that being the case, there's been some that have said "why don't we just get rid of this?" I think there's still a need for the product in certain cases because it would level the playing field and make sure people do have access to the courts. And in some cases we can't just say because I have more money than you, I win.

So, what I've tried to bring here now is a Model that addresses both of the issues that I think are before us as policymakers and that is the issue of consumer lending as well as commercial lending. From a consumer's perspective, I think these become very complicated and very troublesome in that we've seen some cases on the consumer side where the litigation went forward and they took the loan and walked away with less money than anybody else involved. And so again, I think that needs to be addressed. So, I'll briefly walk through a little bit of the Model and then turn it back over to the Chair. In the consumer space we do put in language around registration and making sure that we're regulating the industry that is doing this within your states. We put language around the limit on charges. I think this one has it at 36%. And then on the commercial side we prohibit the funding from the foreign entities of concern. I'll delve into that a little bit. But then what would apply to everybody is that issue around driving the litigation. You'll have no say in what the attorney and the clients decide they want to do on a case. If they want to settle or they want to continue, that's up to them and not up to you the funder. The other thing is you will not have access to proprietary data. If I sued somebody over something, a trademark, a lot of that information is disclosed. It's held in confidence by the court. But if I'm the funder sitting at that table, I've now got access to it. That needs to stop. And so that's in both sides of this. On the commercial side, what I attempted to do in Indiana, and I still lean that way but I understand where we ended up and where this is at, is we really want to focus on prohibiting those who are investing in our legal system who are not our friends. What passed out of the Indiana House was any foreign entity or country of concern which the federal government has a list of those. Those are China and Venezuela and Cuba, and countries like that. So, this Model does address the countries of concern and I'm going to now go to my philosophy at NCOIL has always been and always will be, we will never craft the perfect Model. There's no perfect Model and I think NCOIL's role, and I think we have 31 different states represented here, is you're always going to go back to your state and find it fits different in your state than it does in my state.

NCOIL's role really should be and my philosophy has always been that we build the foundation, we put the walls around it. Maybe we put a roof on it. We seal it up so it's nice and secure and a neat thing to look at and we get it as a good template. Go back to your state and fill in the blanks. We put it in the Model that the agreements are open to discovery. Now that's going to be a problem in some states because in some states, insurance policies and their limits are discoverable so then the contents of this should be discoverable. Other states don't allow that. So, maybe we have in here that the disclosure of the existence of it is mandated but not the contents of it. So, I think when you get back to your state there's always going to be a different path you may take. I'll wrap up with this and that is I think we're on the forefront of this issue in a big way. I know as we were going through our session, Florida had a bill and Georgia had a bill and at the end of the day the last two standing were us and West Virginia. So, I have talked to Del. Steve Westfall (WV) and asked him if he would be willing to be my co-sponsor on this. There is some language I know that came out of West Virginia that we would like to look at. And my path here would be to listen today and I want to hear you tell me what we need to change in this bill. And we'll take copious notes and I'd like to have an interim meeting of the Committee between now and Costa Mesa in July. If we can get it to the right place, then we'll move the Model. If not, we'll have another vigorous debate. We'll have another interim meeting and then hopefully in November we pass this out as states begin to draft their language for upcoming sessions. They can have a good Model to work with. And if I may, Chair Felzkowski, I'll defer to Del. Westfall and see if there's anything he would like to add to that before we open this up to the panel.

Del. Westfall thanked Rep. Lehman and Chair Felzkowski and stated that SB 850 was passed in West Virginia and it went a little bit farther than Indiana's bill and this Model we have here. So with no objection, I would like to be co-sponsor on this Model. The WV bill is not perfect but we had a lot of support for it and while there was some objection, we got it passed and the Governor signed it so it is law in West Virginia. Rep. Lehman and Chair Felzkowski had no objections to Del. Westfall being added as a co-sponsor.

Harrison Hosker, on behalf of the American Legal Finance Association (ALFA), thanked the Committee for the opportunity to speak and stated that ALFA is the oldest consumer litigation finance trade association consisting of the nation's largest and leading companies in this market. Our organization has long been an active attendee and participant at NCOIL. Most recently, we testified last November at the Columbus meeting discussing litigation finance. ALFA is not new to NCOIL's discussion of the subject. Ten years ago, ALFA proactively sought NCOIL's adoption of past NCOIL President NY Sen. Neil Breslin's model legislation to address oversight and regulation of this practice. Regrettably the model was not adopted at that time. However, I note that NCOIL members returned home to their States and adopted legislation modeled on the proposed language. We commend NCOIL and Rep. Lehman for taking up this issue again with his introduction of this model. I want to take a moment to discuss the unique distinctions between consumer and commercial litigation funding as both are captured under the proposed Model. These two transactions are distinctly different fundings that are often conflated creating significant confusion in the development of public policy.

Commercial litigation funding is a product that is used to fund the prosecution of litigation by funding the actual cost including attorney fees, the cost of discovery, research, deposition, witness fees, marketing and other expenses associated with the initiation and pursuit of a legal claim. Commercial litigation funders often include private equity large institutional investors and investment funds that become involved in the litigation before the legal action is actually filed and initial. Commercial fundings in many cases involve millions upon millions of dollars in effect investing into the pursuit of the litigation and its results. These sophisticated institutional investors and underwriters have numerous analysts and legal professionals to determine and underwrite the risk and value of the investment in large multi-million-dollar complex disputes involving amongst other things, intellectual property, product liability, bankruptcy and antitrust. This type of litigation often involves multiple jurisdictions resulting in hundreds of millions of dollars in settlements or judgments. Commercial litigation funding is distinctly different from the transactions that the members of ALFA provide. ALFA members provide consumer litigation funding transactions where a small amount of money, typically several thousand dollars is provided to personal injury plaintiffs to assist them with their personal life needs. Consumer litigation funding is only provided after the plaintiff has filed their case. Therefore, such funding has no role in the litigation being initiated. While pursuing a personal injury claim these funds were provided for life needs such as rent, car payments, mortgages, groceries and other personal financial needs. Consumer litigation funders do not provide funds to prosecute litigation. It is critical for the committee to know that the funds provided by ALFA members are contractually prohibited from being used for any cost, fees or expenses related to the prosecution of litigation. All ALFA members must adhere to this contractual standard and all other standards established in our best practices. ALFA's best practices include prohibiting any funds from being used for the cost of litigation, prohibiting the funding company from being involved in any decisions relating to the litigation, prohibiting funding companies from paying any referrals or kickbacks, and prohibiting funding companies from using false or misleading advertising. The model before you today contains many of the policies such as registration and reporting requirements, banning referrals and kickbacks, and mandating clear and easy to read contracts that ALFA has worked tirelessly to adopt in law across the country. We have several technical amendments that we'd like to see included before the Model is approved but it is our intent to be fully supportive of this model.

Eric Schuller, President of the Alliance for Responsible Consumer Legal Funding (Alliance) thanked the Committee for the opportunity to speak and that the Alliance is the trade association that does represent the companies that do offer this product. Currently, we have 46 members in our association. I won't repeat a lot of the stuff that Mr. Hosker stated because I agree with a lot of his statements. But there are a couple things I just wanted to maybe reiterate on. One is, we respectfully request that this piece of legislation be divided into two pieces of legislation. One dealing with the consumer side and one dealing with the commercial side. I can tell you I’ve been dealing with this issue for about 17 years now across the country and I can tell you the two issues get conflated all the time. When you have someone talking about funding of litigation, they think it's a consumer getting $400,000 to bring a class action lawsuit. Our average funding to a consumer is about $3,000 to $5,000 and that's used for specifically household needs. As Mr. Hosker stated, the roof over their head and food on table. As was stated by one of the largest funds that offer this, Burford Capital, in the 60 Minutes piece I'm sure a lot of you have seen, their minimums serve about $3 million dollars, so just a couple of zeros difference between the two. One of the things we want to make sure about too in this is that by having two pieces of legislation you're not going to conflate it. The Alliance, like ALFA, welcomes regulation on the industry. Unfortunately, it has been stated a lot of times that the commercial folks don't want regulation on the industry. That's their issue. That's not ours. And my concern is by putting this all into one piece of legislation is you're going to have people within the space that are going to be divided on it. The equating of this is that we're both fruit but we're an apple and they're an orange.

One of the other things we'd like to address is the issue on the rates that are currently in the piece of legislation. Our recommendation and suggestion would be to take a specific rate out of the bill and let each individual state determine that. We have some states like Missouri last year that didn't have rate restrictions, but we have other states like we worked with Rep. Lehman in putting in a rate restriction in Indiana. And just let each individual state address that issue. One of the other issues that we'd like to address respectfully with this is on the disclosure of the product. What was initiated years ago and in last few years was automatic disclosure of the product. We don't agree with that. What we've come to kind of agree to is kind of what we worked with Rep. Lehman on in Indiana last year where there's an acknowledgement that the consumer has one of these transactions but if you want any more information on it, it goes to the discovery process, but the normal discovery process of that state. It should not be more discoverable or less discoverable than any other financial product that the consumer has. So, if you need access to their bank accounts or whatever it is, this should not be treated any differently. And then finally, it should be inadmissible against the consumer, it cannot be used against them in any way. And then finally, what we'd like to do is work with the members of this committee and anybody else that has interest in this in making sure that there is a piece of legislation out there. As I stated before we like to have this industry regulated, but also we want to make sure that it’s good for the consumer and good for the legal system and also good for our companies.

Daniel Hinkle, Senior Counsel for Policy and State Affairs at the American Association for Justice (AAJ), thanked the Committee for the opportunity to speak and stated that AAJ is the largest plaintiff’s trial bar in the country. I'm here today to be helpful to the committee. Each individual state has their own state trial lawyer association that speaks for their state association. So, I can't speak for them. I am in communication with them. I will talk to them. I can explain things to them. But they make their own decisions. Similarly, AAJ works on federal policy, not on state policy. That's our state associations. So, I am a man who speaks from nowhere right now. But hopefully I can be helpful to the committee and to you all and sort of understanding where the trial bar comes down and sort of thinks about this issue and understands it. So from a big picture perspective I agree with both Mr. Hosker and Mr. Schuller. Commercial litigation financing and consumer litigation financing are two separate issues. I think of it as commercial real estate versus title loans. They're just different products that are thought of differently and addressing them both in the five minutes that I have is going to be complicated but I'm going to try to keep them separate, as I talked about. When you talk about this though, there is one similarity between them. And the access to these products can be either useful or smart. It is useful for the family that cannot put food on their table to have access to some financial product that lets them get to the point that the insurance company finally decides to pay on a valid legal claim. They need help during that interim period so they can put food on their table because they can't work. Having access is helpful. Similarly, the small business that's been exploited by a giant corporation whose only shot at maintaining their business is access to commercial litigation financing so that they can maintain their profitable business. It's important for them to have access to it. On the smart side of it, this is kind of like reinsurance. It's probably not a perfect analogy. But it can be a risk mitigation tool, particularly on the commercial side of this for sophisticated players working on some sophisticated issues. With that said, the biggest issue that we have with the model and what you're going to find from trial lawyers across the country is the automatic disclosure provision that's in the bill. I appreciate that it's narrow. We have seen automatic disclosure requirements that go so far as trying to get at partnership agreements within law firms and trying to really dig into the finances of every single person who might be involved on the plaintiff's side of the issue here.

This is a much narrower provision and I appreciate that. And I specifically appreciate that it already carves out the issue of entities of concern. That is a serious problem and I completely agree with you. Those sort of entities should have no place in the legal finances in this country. The one thing I would add though is that they should not have any place in it on either side. Currently, this bill is drafted so that it's only entities of concern who are providing litigation finance on the plaintiff side are carved out. Which is great. But it should be expanded to cover when that litigation financing is provided to defense firms for after the event insurance and other things like that. There are lots of financial products that are in this area that don't just cover the plaintiff side but also cover people on the defense side and I think that the committee should take a look at that when they're thinking about this policy. The other thing about the automatic disclosure that a lot of our members have is that most people do not use these products. Especially on the commercial litigation funding side as Mr. Schuller mentioned. It is a very narrow group of some cases and some firms that will potentially use these products. The vast majority of the time, this is not an issue at all in the litigation. But by forcing automatic disclosure, you make it a part of every single case. Because whether someone does or does not have litigation financing provides a tactical advantage to the defendant in a particular litigation, on the consumer side as well. So, whether a consumer needs to take a loan out so that they have the ability to put food on their table is wholly irrelevant to the case. But if we have to disclose that to the insurance defendant on the other side they have a duty to represent their client as thoroughly as possible. They can drag out that litigation process knowing that the client will eventually need to take a lowball settlement just to make sure their family has food on the table.

On the commercial side, similarly, the issue isn't necessarily that you disclosed there is litigation financing but did you disclose that you don't have litigation financing. Because if the defendant in a high stakes bet the company case does not have litigation financing, the defendant, who already has more resources than they do, knows that if they drag this out, they have a much better shot at either forcing this company to fold before the end of litigation or they're going to have to take a lowball settlement just to get some money in the door so that they can repay their other investors so that they can dissolve the company later. They just won't have the money to pull this out. So, that automatic disclosure provision is a problem. I do want to point out two more things - it gives negotiation leverage to the other side as well to know what position the plaintiff is in. And then the last thing is the public relations pressure. That's obviously part of this conversation across the board. We're already seeing this issue of litigation finance being used to delegitimize the civil justice system in general which I think is wildly hypocritical in certain circumstances that we're talking about a litigation finance measure around litigation when that's what the insurance industry is in the business of to a large extent. And I think that there needs to be sort of a general ratcheting down of the sort of rhetoric and understanding around this tool so that we can have a much more common sense, straightforward discussion about what exactly this industry is and what the pain points and what the issues are in terms of some of these proposals and I'm happy to do that. There are some good parts of this bill and I'm more than happy to work with the Committee on figuring out the best way to draft this policy.

Robert Gordon, Senior VP, Policy, Research & International at the American Property Casualty Insurance Association (APCIA), thanked the Committee for the opportunity to speak and stated that APCIA represents the majority of the property casualty industry. We greatly appreciate the Chair and the committee's consideration of the model legislation to protect our civil justice system from the hidden funders seeking to tip the scales of justice for their profit. And I particularly commend Rep. Lehman for advancing solutions to provide more consumer protection and more transparency into these hidden practices. And I want to strongly endorse and agree with Rep. Lehman's comments about how much has changed since he earlier identified the need for more sunlight in this area and the potential harm of shadow financing by third-party litigation funders. And one of the things that changed is the Government Accountability Office (GAO), which is a federal agency and not a public relations operation, did an investigation of third-party litigation financing published just last year. And they found it is expensive and they deter plaintiffs from accepting the settlement offer because they want to make up the amount they will have to repay the funder. The GAO also cited the warnings that sovereign wealth funds may be involved in third-party litigation funding to further foreign policy or military goals. There's been a lot of discussion about sovereign wealth funds pouring billions of dollars into encouraging lawsuits in the United States and five of the largest ten sovereign wealth funds are in China or Singapore and another four from the Middle East.

Secret third-party interests are now funding tens of billions of dollars into increasing litigation in United States. An estimated 30% of intellectual property claims now have hidden third-party dark money involved and not only are large funders being increasingly shown to control litigation, but again, we're uncovering that foreign actors and a number of our adversaries are essentially weaponizing the third-party litigation funding in our U.S. litigation. Fortunately, the policymaker reforms to create more transparency in third-party litigation funding are already starting to help. So, just last month, the Wall Street Journal uncovered that Abu Dhabi conglomerate owned the company, Forest Investment, a litigation financier that owned VLSI Technologies. That's a former chip manufacturer, been defunct for decades it but filed a multibillion-dollar litigation against Intel in Delaware. But when the Delaware judge told VLSI they would actually have to disclose its litigation funding origins it actually dismissed its suit rather than reveal its true master. And then only a week later, on March 28th of this year Bloomberg Law exposed that Putin's billionaires dodged sanctions by financing lawsuits and Bloomberg revealed that billionaire founders of a Russian conglomerate evaded both U.S. and European sanctions after Russia's invasion of Ukraine through third-party litigation funding around the world including in New York in London. So we now see state and federal policymakers and courts very much waking up to the dangers of this hidden money, they're actively investigating the third-party manipulation of the justice system. Just this last week in Congress, the Deputy United States Treasury Secretary discussed with the Senate Banking Committee the national security implications of illicit third-party financing and the challenges of foreign adversaries investing in U.S. legal system abuse.

And the Deputy Secretary agreed before Congress that there needed to be more transparency of the shadow funding system and supported working together to address the problem including potentially through litigation. Although this legislation and oversight is being done so far primarily through the states which is why NCOIL's efforts are so critical. We saw just recently four states adopting statutory requirements for disclosure of both consumer and commercial litigation funding. I'm a little surprised others on this panel think legislators can't draft legislation dealing with two colors of essentially the same fruit. They suffer the same damages and defects, especially when the focus is more sunlight to help detect and limit that abuse. And Indiana and Montana, West Virginia, and Wisconsin have already done the right thing and what we're now seeing in these cases is with the third-party litigation funding a majority of expenditures are going to the funders and the lawyers. And the funders have no fiduciary duty like the lawyers do to act in the victim's best interest. So, a lot has changed since Rep. Lehman had the foresight to identify this issue as a problem. It's something very important to deal with. States and the federal government are waking up for the need for more oversight. It's beginning to gain traction and it's very good timing for the Chair to consider model legislation and for the Committee to consider its adoption. We strongly support proceeding with the model. We look forward very much to working with you on it to make sure it achieves the intent and very much the need for additional transparency.

Jon Schnautz, VP of State Affairs at the National Association of Mutual Insurance Companies (NAMIC), thanked the Committee for the opportunity to speak and stated that the model that's before you, there are several fairly small pieces of a much bigger issue. And the bigger issue is like it or not, litigation is becoming an investment market in a lot of different ways. And we don't know all the repercussions of that. It is still a fairly early thing. But I think probably one of the things that everybody up here would probably agree to is it's not going away and it has grown over the years. So, I would start with that and then just point out this is looking at some fairly narrow pieces of that much broader issue. So, a couple of aspects of the model that I think are very positive and I'll speak to one and this seemed to be a point of agreement is that the model clearly prohibits control of litigation by a funder. I think that's a really important thing and a good piece of the Indiana bill. We think the model needs to reflect that throughout and we'll have some suggestions on how to make that more clear. I will speak to you since it was raised about how the model does include a limitation on the consumer side on the amount that can be charged. Because it's not obvious in the model, I'll just tell you the rate that is being referred to there is a 36% interest rate. So, in terms of what the committee might want to do there I would just advise that's what's on the table so you may want to consider whether you think that's a reasonable limit or not but I think that is an important issue to at least have be part of this conversation. There may be better ways to structure it but I wanted to bring your attention to what specifically is included there. On the disclosure point, I think that the model needs to be viewed carefully in light of what the Indiana situation was on the ground there. Rep. Lehman and I have had several conversations about this. Many states have different provisions on disclosure and discovery. In our view the way that the bill ended up treating these agreements is very similar to how insurance policies are treated in the discovery process and we think that is well justified. The analogy is not perfect but in terms of what ought to be disclosed we think it is a very strong one across both sides of the v as to what the disclosure ought to be and we look forward to thinking about other ways that that might be made more clear. Maybe it's the West Virginia approach, maybe it's something a little more modular but we want to be part of that conversation.

I have a couple of other responses to other points that have been made and then I'll stop. First, on the issue that there ought to be two models. I guess I would just point out this is already a fairly bifurcated model. It's got one set of rules for consumer. It's got one set of rules for commercial. They don't overlap a great deal. The one thing that's in for both and that we think is the most important part of the model is disclosure. That's the commonality. Otherwise, I guess they could be on two different sets of paper but other than that the model already recognizes some very key distinctions so that's already done to some extent. Finally, one of the previous speakers talked about kind of this leverage argument on disclosure and if I understood him right, he was arguing that in certain circumstances the opposite things are true. The argument that I've heard most often on disclosure is well, if the plaintiff' has to disclose it they're going to disclose that they're in financial dire straits. That's kind of a strange argument to me because it's sort of like saying "well I would have been in financial dire straits but guess what I got this funding and now I'm not." So, I don't really understand how that disadvantages the plaintiff from a leverage standpoint, it would seem if anything the opposite. On the other hand, the fact that the plaintiff doesn't have funding I think tells you almost nothing about why they don't have funding. Maybe they don't have funding because they don't need funding. There's no real inference you can draw there that the plaintiff is in financially some sort of destitute state just because they don't have funding as part of the case. So, those are the points I'll make for now. We look forward to continue to be part of this process.

Rep. Brenda Carter (MI) stated that I'm glad you brought this situation to light because I think it's very similar to payday lending. Regarding the 36% interest, who can afford that? I'd like to know what's the difference between what you're proposing and payday lending? Mr. Schuller stated that there's a big difference. Payday lending creates a cycle of debt for the consumer and consumer legal funding does not create debt. The Internal Revenue Service (IRS) has even weighed in on this and says if a transaction is consumer legal funding is done as a loan and the company gets back less than contracted amount, meaning the case settled short and there's not enough money to pay, then that funding company has to 1099 that individual because it is a forgiveness of debt. But if it's done as a funding like we have in the states where we pass it like Indiana and Missouri and several others, that is not debt. So, we do not put consumers in the situation of debt. It's also the only financial product out there that you only have to meet your obligation if a third-party gives you money, meaning you win a settlement. If that that third-party does not give you money, then you're not contractually obligated to make it. Whereas in payday lending, car title loans, home mortgage, credit cards, the person that provides you those funds, they don't care where you got your money from. They just want your money. We want to make sure you get it from your settlement and then secondarily if there's enough money to pay us back that's the process. The way we have a draft in the states is attorneys, medical liens, statutorily they all get paid first. Then we get paid. So, it may sound the same as payday lending, but it's a whole lot of difference between the two. Finally, this is the only transaction that I'm aware of anywhere that's offered and your attorney has to sign off on it. If the consumer's attorney looks over that contract and says this is not in the good interest of my client, it doesn't happen. In fact, we've put that in statute that if the attorney doesn't sign off on that, it doesn't happen. In most states you can go and get a $500,000 mortgage and you don't have to have an attorney at closing but just getting $500 from any one of our companies, the consumer's attorney has to look over the transaction and say this is okay for them to do.

Del. Westfall asked Mr. Hosker when and why do people seek your type of funding you were talking about? Mr. Hosker stated that to reiterate some of what Mr. Hinkle said, it's just a way of while they are pursuing justice after they've already filed their claim. So, this is not initiating any litigation in any form. But let's say for example someone gets in a car accident through no fault of their own and while they're awaiting the settlement from their claim they have no way to fix their car. They have no way to get to work. And so this allows someone to come in and fill that gap for them or put food on their table or any other life need that they would want to spend it on.

Rep. Jeff Keicher (IL) stated that I wanted to go back to the story that we started out with that just caught my ear. Does the financing company have access to the discovery documents through the course of the trial or the discovery process? Mr. Schuller replied no, we don't. And in fact, we're very clear that we do not request privileged information. Rep. Keicher asked what about the other side where we're financing on the business end of the Intel example if you will? Mr. Hinkle stated that I'm not aware of that being a condition or a part of any of this. I'm not opposed to that provision being included in this bill or being a model policy. I would think that's protected already. Rep. Keicher stated that he hopes so. I just think about the nature of some of the more expensive ones that are going out there and the more detail that needs to be there and I think that should be a consideration. And out of curiosity what's the most common setup for interest or a range of interest that is assessed on these fees that are lent? Mr. Schuller stated that a lot of it is risk assessment in states like Indiana where we have rate restrictions in place. Some states don't. I can tell you that two examples I point to are Oklahoma and Utah. There are no rate restrictions in either state. I can tell you for a fact those two states have probably the lowest rates in the country because the market is dictating the rate and in both those states companies have started up that were not there before the statute went into place and they're all local companies and they are giving the national players a run for their money because they are right there in Oklahoma City and in Tulsa and in Salt Lake and they're going to the attorneys who they deal with on a regular basis and saying, "hey, if you got a problem, I'm right down the street here from you. You don't need to deal with that guy in New York or the guy in Los Angeles or the guy in Chicago."

Rep. Keicher stated let me ask it this way - what is the lowest to highest range during your career that you've heard assessed on these dollars on an annual basis? Mr. Schuller stated that I'd say probably in the mid-30% to the mid-40% range. And I think a lot of times it is they're also risk assessed meaning that the case is more riskier. Just like in insurance, if a driver has a very poor driving record, they are going to pay more for it. Rep. Keicher stated that and I'm not trying to mitigate the risk, but I want to understand that the average typical rate is between 30% to 40% per annum on the monies lent? Mr. Schuller replied yes, typically.

Sen. Beverly Gossage (KS) stated that this issue came up in our legislature last year and what's interesting to me is I had to have them come into my office several times, and I was asking "what am I missing?" I don't quite get this. So, I was trying to understand it because what we heard was "we just to level the playing field." And I'm like, but if somebody is suing someone you typically assume the person doing the suing is the one that was harmed and they're trying to say maybe they don't have the money to come against this person. And so they've got somebody who's invested in them and what was shared with me is that we're not trying to stop that. We're just trying to say disclosure - they should just be able to disclose that they have that. Could someone address the difference? Mr. Hinkle stated that I can try to address what you're talking about. So, I assume you talking about the consumer side and not on the commercial side? Or are you talking about the commercial side? Sen. Gossage stated that typically what they tell me is commercial.

Mr. Hinkle stated that with the commercial side, I guess I'm not quite sure where they're coming from in terms of the issue too in one regard and so maybe we'll talk about that but I do want to talk about the remedy that they've proposed here which is disclosure. And so even if you assume that there's something problematic maybe I guess with where the money is coming from, which despite the fact that it is completely covered in this bill seems to still be the basis of their testimony here today, that somehow the disclosure needs to come from the lawyer to the opposing side and this side. I can tell you from my conversation with our members, they are working with a firm, a reputable U.S. based, commercially regulated firm that's providing sort of litigation funding in a handful of cases where this sort of thing is available. They don't know where that firm got their money. And so, the idea that the lawyer is going to be the one who's going to know to disclose it to the other side is I don't know how we get to that. They're not the ones there. But even if you assume that there's something problematic with this and that the lawyer might know about it, what does disclosure do other than provide the sort of tactical advantage that are already laid out here? I think if there's a problem with the funding then you can ban the funding and that's what this bill does for the sort of funding that we've identified from foreign entities of concern. If you have a problem with litigation funding in the commercial space, regulate the problem you have with funding in the commercial litigation space. The disclosure doesn't really do anything from that perspective. But even if you assumed the disclosure somehow did do something in these cases and that disclosure was an appropriate remedy in some way, why is the disclosure not to the Attorney General or the Secretary of State or some sort of entity within the State that could somehow do something with that information to regulate whatever the problem is with that? Maybe the Bar Association -- somebody who could do something with that would be a much more appropriate sort of target for that disclosure. But even if you assume that somehow there is a problem with third-party litigation disclosure in the commercial space and that the lawyer is the one who should know about it and should be the one that's disclosing and that the litigation funding should be disclosed in the context of a particular piece of litigation, why is the insurance defense counsel the appropriate party to be disclosing that to? Why not to the judge who could do something about it in camera if there's a problem, which I have yet to see. And so, I think that that's kind of the chain that you're probably maybe sort of correctly intuiting that it doesn't really make any sense as to why it is that the insurance defense is the particular party that needs to know about this.

Sen. Gossage stated that I've been told that on one side the one being sued has to disclose how much insurance they have. And so they're saying that this kind of equalizes that by you have to disclose how much money somebody has invested in your case. Mr. Hinkle stated that I apologize for misunderstanding. The reason why is because it's relevant and proportionate to the issues that are before the court. It goes to the standard rules of discovery generally. And the reason why you'd want to know if they have insurance or not is you want to know if you have the ability to satisfy a judgment against them. There is no corresponding need to know if the plaintiff has the capacity to bring the litigation. That's just sort of implied by the fact that they sued.

Rep. Tom Oliverson, M.D. (TX), NCOIL President, stated that this is all new to me and I'm learning a lot here. My question is more simple and that is, I've heard this number 36% finance charge thrown out. I'm sure that's not the case in all cases but that does sound like a large number to me. Assuming they're also lawyers that are representing these clients that don't have the money, are they getting their legal fees paid on top of that? And if so, if there is a judgment in their favor, what are they left with in these circumstances where an attorney may claim 20% to 40%, right? And then there's a 36% finance charge. So, in that case, what's left for the plaintiff? Mr. Schuller stated that we typically fund no more than about 10% of what we think the value of the client is to make sure there is money leftover for the consumer on it. You have to remember, at the end of the day, the consumer is not going to settle the case unless they're comfortable with the money that they're going to get in the end of it. The number that has been offered is 36% and everybody thinks "oh my God that's high." Just because the company charges a rate doesn't mean they make that rate. You have to remember too, there's a lot of costs associated with this. Right now, the cost of capital for some of the companies, especially the smaller companies, is 15% to 20%.

Rep. Oliverson stated that, related to what you just said, obviously most of the attorney's fees in these situations are probably contingency based. Mr. Schuller replied, yes. Rep. Oliverson asked what about the financing company - if their judgment doesn't go their way do they lose all their principle? Mr. Schuller replied then we get absolutely nothing even in the case, and it does happen on occasion, where the consumer drops the claim. So let's say they're living in northern Minnesota and say I'm done with cold weather and I'm moving to Maimi and they drop the case, we can't do anything about it. The only time we can go after a consumer is if there's fraud involved and in order for fraud to be involved, because we have the attorney sign off on it, their attorney would have to be involved with it. I don't know many attorneys that would lose a law license for $3,000 that somebody else got. Rep. Oliverson stated that it is fair to say then there's parity in that for both the attorneys as well as the financiers, it's high risk, high reward essentially. Mr. Schuller replied correct. And just to give you some quick numbers, when we polled our members last year, 30% to 40% of the time they get less than the contracted amount and about 10% of the time they get absolutely zero. That could be caused by a lot of things, they lost the case or they dropped the claim or there wasn't enough money left over even if there's a verdict. Let's say we projected the case would settle at $50,000 but it settled for $10,000. After everybody's paid, there's nothing there. I've seen transactions where the consumer, because they got legal funding, in the end got more money than anybody else. That does happen.

Rep. Lehman thanked everyone for their comments and stated that I think I've narrowed this down to two issues that probably need to be tweaked or at least looked at and those are separating the two issues, and disclosure. And so, with that, I look forward to working with everybody moving forward to get this to a place where hopefully we can have something to vote on. Sen. Felzkowski thanked Rep. Lehman and stated that I look forward to discussing this throughout the year and if anyone has any comments or questions please reach out to me, Rep. Lehman or the NCOIL staff.

DISCUSSION ON DEVELOPMENT OF NCOIL EARNED WAGE ACCESS MODEL ACT

Sen. Felzkowski stated that next on our agenda is a discussion on the development of an NCOIL Earn Wage Access Model Act (Model). As a reminder we had a discussion on this topic at our last meeting in November and you may have heard of this in your state where these types of providers grant workers access to wages that have already been earned before their scheduled payday. A few states have taken action and enacted laws with licensing and other provisions. After the discussion in November, NCOIL Vice President, New York Asw. Pam Hunter expressed an intent to develop a model law on this issue. Unfortunately, Asw. Hunter couldn't be here today as there was some last-minute schedule changes relating to New York's budget adoption. But she did convey that before introducing a first draft of a model she wanted to get some feedback on whether it should follow the direction of Nevada which was the first state to enact a law on this issue, or follow other states such as a bill that has been introduced in her home state of New York. You can view the Nevada law and New York bill on the website and app and some material comparing and contrasting the laws has also been distributed before you.

Matt Smith, Director of Gov't Relations and Consumer Affairs at the Connecticut Department of Banking thanked the Committee for the opportunity to speak and stated that I'd like to start off a little bit talking about Connecticut's small loan and related activities law. Under this law, it allows lenders to lend up to $50,000 beyond the 12% usury rate in Connecticut. The interest rate cap for this is 36%. Under this Act a license is required for companies that are leading beyond the 12% for a variety of activities. But particularly for our discussion it does define as licensable activity advances of money on a borrower's future income or advance of pay. And I think that that's important here today. So, again under this law your annual percentage rate (APR) cannot exceed 36%. So last year, the Connecticut Legislature at the request of the Department made some modifications that included that tips, subscription fees, and expedited transfer fees are now treated as “finance charges” when calculating the APR on a loan or advance. This was a proposal the Department had placed publicly back in January of last year. There were public hearings on it by the legislature as well as the opportunity for public testimony on this bill. The legislature passed the bill and then on September 11th of 2023, the Department issued industry guidance that captured not only earned wage advances but litigation settlement and some peer to peer lending companies as well both of whom had reached out to the Department during the last legislative session to talk about the department’s proposal. It’s important to note that one of the reasons that earned wage advances should be subject to oversight and licensure is we've already seen some bad actors in this space, particularly a class action lawsuit that resulted in a $3 million return of monies to consumers that were harmed and $9.5 million in forgiveness. That was EarnIn. And then Brigit, another earned wage access direct to consumer model, was fined $18 million by the Federal Trade Commission because of unfair and deceptive practices.

So, with that, earned wage advances are indeed loans captured under the Connecticut small loan and related activities act. And I know that there are a lot of insurance people here, but if you were to ask any banker, what is it when you give somebody money and you expect payment in return for a fee? They would call it a loan. And that’s exactly what these are, small loans. It’s another iteration of a payday loan that we've seen consistently over the years designed to prey upon vulnerable consumers, to circumvent lending laws. We’ve seen this with storefront payday lending in Connecticut and tribal lending. This is just a high-tech innovative way because you can use your smartphone to make it easier for you to have access to cash at an APR that exceeds 300%. When considering the Model Law I think it's important that it requires: unfettered access to company records for the regulator; thorough examinations; the vetting of ownership and control people in the organization; the need to have a surety bond; as well as a disclosure to the consumer on the actual cost of the money in the form of an APR calculation. It is something consumers are familiar with. It’s how you buy your car. It's how you find a rate for your mortgage. While they may not understand exactly what an APR is, they generally know that the lower the APR is the better it is for them. And then finally, there should be no exemption for any money transmission exemptions in any model law. Money transmission is a very different space through the small loan lending. One can imagine that as this business model evolves, you're going to see, and this is only me conjecturing, the possible movement of money between the consumer and another friend of theirs. Or paying a bill or something like that. And I think that it’s important that as non-bank services begin to move into the spaces of traditional banks which do not have the proper supervision that we can expect or essentially a deregulating of the financial services space. And when you're deregulating non-banks when banks have such strong regulation on safety and soundness then more services move over to the deregulated space. Small ripples in that space can have larger consequences for the entire financial system as a whole. So, I think that’s important as we look at this to think about what kind of regulation we want. We want regulations that protect consumers and also balance that with a healthy financial services system.

Ben LaRocco, Senior Director of Gov’t Relations at EarnIn thanked the Committee for the opportunity to speak and stated that I’m going to start with a little bit of a recap from what we talked about a couple of months ago. When you earn your money, you have a legal right to that money. If you are working and living paycheck to paycheck, you might only have $50 in your bank account but have hundreds or even thousands of dollars that’s legally yours. And you should have access to it. So, we provide that service with no mandatory fees and no recourse if somebody doesn’t get paid back. So EarnIn, we have about two million customers and we estimate there's about five million customers across the country that use this service so every elected official has earned wage access customers in their district. Who uses this service? Amazon and Walmart employees are generally always our top two employers but some other surprising top employers are postal workers are always in the top ten. Hospitals and school districts are also often in the top ten. So, folks where it's very human capital intense. And a lot of people are making an hourly wage. We don't sell any data. The only way that we make money is by voluntary fees or tips. We say, "hey, if you like the service, give us some money." If you need this money immediately you can pay a fee for that but nobody ever has to pay anything and many of our customers never pay anything. There's no late fees. There's no interest. So, as we're talking about the model policy here, the first eight bills came about four or five years ago. They were not really very well thought out. We've done a lot of work in the interim. Last year, the Council of State Governments (CSG) adopted the Nevada bill as their model bill, which was the first EWA bill that passed. Three other states have passed that bill. Missouri and Wisconsin have both been signed into law. In Kansas, the bill is sitting on the Governor's desk. So, that'll be the fourth state. California did a law by rule. It's sort of interesting. They consider it a loan but exempted it from the lending statue and said you don't need to become a lender, you can get registered under this other statute. So, I think there's maybe 15 or so other states that have considered this kind of legislation in one way or another.

So, I'm gonn do a little pre-buttal to the Center for Responsible Lending (CRL) presentation and then I'm going to respond to Mr. Smith a little bit as well. For CRL, why do they care about this so much? They generally don't disclose this but CRL is a subsidiary of a multibillion-dollar credit union that essentially has almost no capacity to compete with digital first financial services. You can see if anybody is on their phones. You can look at their app in the App Store and you can see some of their ratings. You know 3.3 stars compared to 4.7 stars. So, they have a model where they claim to be an impartial actor but then they essentially just attack anything that is new and innovative. And it is frustrating. So, my apologies that it's a little bit negative but I want to talk a little bit about some of the data that they have put out recently which I'm sure they will talk about. So they put out this report that basically claims that if you use earned wage access you get more overdrafts. But correlation is not causation. You know, it'd be like saying we followed nursing home patients for six months and we found that anybody that went to a hospital had more stitches afterwards, therefore hospitals are very dangerous. There's just a ton of reasons why the data that they disclose about this industry is misleading at best. One question that's going to come up a bit in all presentations and you already heard from Mr. Smith is a question of APR and fees. Basically, the Connecticut Department of Banking changed the way that APRs are calculated. It is not the way that APRs are calculated under federal law that everybody has been abiding by for 70 years. There's also a number of other fees that most financial services companies can use. You can see here our fees compared to some of the fees that Self Help Credit Unions use. So $45 if you lose your PIN for your ATM and you need it soon, that's a lot.

Comparing EWA to credit cards. The average earning customer spends about $60 a year using EarnIn. The credit card user spends $1,000 on late fees and interest. That's from the Consumer Financial Protection Bureau (CFPB). And just to give you an example of what happens if you don't pay EarnIn back. If you get $100 from EarnIn and you don't pay us back, you never owe us more than that $100. If you take $100 on a credit card, specifically the Self Help Credit Union credit card, a year from now you're going to owe $182 even though the APR for that is only 16% but once you compound that monthly and you add in the late fees that really adds up quickly. So the fees are quite high and the APR is pretty misleading. So, that's the next thing I want to about, APR. The Truth in Lending Act (TILA) is about a seven year old federal law that governs how APR is calculated. So, there's a number of transactions that technically have 0% APRs the way the law is calculated. But essentially, what the CT Dep't of Banking did and what CRL has done to attack this industry is said well, we want to redefine APR differently to essentially scare people about this product. And so using their claim we have about a 200% APR with our $3.99 fee but the late fee for their credit card is higher than that at 300%. An ATM fee would be 700%

and an overdraft is 1,800% So, all of those things are 0% APR but if you recalculate it differently there are high numbers that you could scare people with. But even at that, ours is still lowest.

So, what happened in Connecticut? The first quote up here is from Mr. Smith's testimony on this CT bill. The change in the bill from his testimony was about income share agreements. Earned wage access never came up in any of the testimony, in any of the discussions. It doesn't appear in the bill. It doesn't appear in any of the materials. We've asked dozens of legislators, "how'd this happen? Have you ever heard of earned wage access?" Zero people had ever heard of earned wage access before they voted on it that we've talked to. We had a conversation with the Department asking "how'd this happen?" When we first talked to them they said "Oh this was a misunderstanding, this wasn't our intention." And then as time went on they said "Oh yeah this has always been this way." So we put in a Freedom of Information Act (FOIA) request for their emails and we asked, "tell us about all of the earned wage access conversations you had with legislators." There were none. They never talked to legislators about them. So, as legislators I think you should be very wary of regulators that come to you and say a bill does one thing and then it does something very different. And in this particular instance it was very harmful to our customers. And I heard stories from our customers about this. We had to pull out of the state on basically two weeks notice because of the Department's guidance and people were just devastated. We followed folks in Connecticut and compared them to folks in New York and we found the folks in Connecticut had 10% more overdrafts compared to similar people in New York. Thousands of dollars in overdrafts that they shouldn't have had to get. They're very stressed out. So there was a lot of financial stress that happened to these people because a financial service that they had been relying on for years was taken away from them because of the change of this law.

Elyse Hicks, Gov't Relations Manager at DailyPay thanked the Committee for the opportunity to speak and stated that I am just going to highlight some things that I think you went over at the last meeting and tell you a little bit more about DailyPay. At DailyPay, our model is employer integrated which means we actually contract with the Targets of the world or the employer to integrate into their time and attendance and payroll systems. And that data updates four times a day. So, we get fairly close to the net amount that people are able to access and transfer to their accounts. Companies run payroll about once or twice a month. My husband was a teacher and he got paid once a month. So, you can just kind of think about how much he had to budget. He was also in the military and he got paid semi-monthly so twice a month and at that point we were living in California on his income. So 11% of companies run payroll monthly and 36% of companies run payroll bi-weekly and 32% of companies run payroll weekly and 0% of companies run it daily. I want to take a look at some strategies that our customers used before DailyPay: 57% paid a bill late and 49% borrowed money from family and friends and 39% overdrew their bank accounts and 21% took out payday loans and 21% made a loan payment late. DailyPay likes to say that we are overdraft fee eliminators. So, 38% of people that were surveyed overdrew their accounts before DailyPay and 97% rarely or never overdrew their accounts after DailyPay. And 75% of those people attributed that savings to DailyPay's use. We also like to say we're payday loan pillars. So, 28% of people that were surveyed took out a payday loan at least once a month. After DailyPay's access, 95% stopped using payday loans and then 88% of those people attributed that to the use of DailyPay.

Here we can see that 39% missed a loan payment or they paid the bill late. After DailyPay, 88% had less trouble paying their bills late. DailyPay has partnered with 970 employers. We have 1.6 million enrolled users and a 36% adoption rate which means the employees that are employed by the employers that we contract with have access but they don't adopt it. So, 36% of people that have access adopt or start using DailyPay. The average transfer amount is $108 and 49%

of platform users make no transfer, but they kind of use it to see what their net earnings are. This is also important, 66% of all platform users each month then take a three month to one year break after using our platform for the first time. There is probably trepidation about overuse or high frequency. This is what we're seeing when we are surveying our customers. Regarding our fee structure, there's no employer fee. If someone wants to use DailyPay and their employer has given them access to use DailyPay we have two free options. One is a standard Automated Clearing House (ACH) delivery so they can wait about a day to three days. It's usually a day to get that if they want to transfer to their bank. We have an instant transfer fee to our Friday card which is our prepaid debit card if they would like to use that. If they would like to get that money instantly to their bank account there is a $2.99 to $3.49 instant transfer fee. We all know that we do not live in a real time payment system so it does take money to move money. And that is a flat fee. So, depending on when the employer signed up with us their fee is either $2.99 or $3.49. We also have a financial wellness platform and people do use this as a financial wellness tool. One thing that I'd like to point out is 93% of DailyPay users check the app for their earnings to make spending decisions and 83% of DailyPay users say DailyPay helps them make better choices because they know their earning from day to day. We're also good for businesses. We lessen the turnover rate by 45%. My neighbor noted that I worked for DailyPay and she told me that she actually took her job because DailyPay was offered. People like having access to their earned wages when they need them most. So, that goes to my next point of the product being 52% in faster recruiting for businesses and three times more engagement for businesses and it lowers absenteeism for workers. I want to focus on the three states that have already signed and passed laws on this: Neveda, Missouri and Wisconsin. And there were over 10 state bills that were introduced in this legislative session. In six states the bill passed at least one chamber and in two states it passed both chambers. And within the laws that are already on the books and those that were presented we do as an industry advocate for strong consumer protections and these are the lists of consumer protections and hopefully my slides are available for you to look at those consumer protections and I don't have to go through all of them and I'll stop there.

Monica Burks, Policy Council at CRL thanked the Committee for the opportunity to speak and stated that CRL is a non-partisan, non-profit, policy advocacy organization. It was started in North Carolina in Durham and its initial mission was to shut down payday lending in the state of North Carolina because we came to recognize a pattern of the debt cycle, patterns of harm and patterns of usage that prevented people who access payday loans to build true wealth and stability for themselves. And I found it interesting that one of our speakers today mentioned how folks have been relying on their products for years and when it was taken there was this fallout. And that is the exact type of harm that we recognize in payday lending and similarly in earned wage advanced products that our research is affirming. And so, I just want to talk about that a little bit. And so the report that was mentioned was an analysis of over 14 million transactions from consumers. From that report, nearly 2,000 customers completed over 37,000 earned wage advanced products and we took a snapshot of an 18 month period of them using this product. And 75% of the users took out an additional advance the next day or the same day that they repaid the other one. So, that cycle of reborrowing that is signature to payday loans continues with the use of this product and I find it interesting because we heard that when folks switch over to DailyPay they stopped using payday loans because it was replacing the same exact purpose they were using the payday loans for. We also saw from this study that 48% of users use multiple earned wage access apps in one pay period and that's probably because as you see on the next slide, most of the earned wage advance aps limit the amount that you take out to $100. I'm a single mother with two children. When I go to the grocery store I'm praying that it comes in at $100 these days. It's such a small amount of money that folks are stacking the apps against their same paycheck that they're hoping to try to make ends meet between those periods.

Those small frequent transactions result in high fees for users. Just like payday loans you can see on the screen here the APRs are astronomical. What that means is if I didn't have $80 to get groceries and gas before my payday, when I have to repay that loan on payday I need to take it back because I still don't have the money. I took it away from money that I was anticipating and as soon as I get that money I have to pay it back. So, what's happening with the companies is they're giving you that same $80 and repeating the fees that you pay on that same amount of money and that is why it's so profitable. That is why some of these industries are looking toward going public. Because they're bringing such a healthy amount of return on the funds that they're lending. And to note this term "access" is misleading because they're not facilitating access to wages from their employer to the employee. They're third-party companies giving their own money from their own capital to facilitate these transactions and that's an important distinction because you can't do that for free. And they don't want to hear us talk about APR because APR illuminates the finance charge to access this money. It's telling the consumer how much it costs compared to other options to handle the financial issue that they're facing. But when you conceal that, when you defuse it for tips and fees and subscription it makes it harder to compare. It makes it almost impossible to know exactly how your money is being drained. And so, as you can see from the research, and I encourage you all to take a deeper look at the full report, these markers of payday lending are the exact reason why we think there's some essential protections that need to be included in any model law. And clearly from the research it's clear that these products are more harmful than helpful to consumers. But even if you as a policymaker sincerely want to make sure this product is available to consumers in your state, guardrails are essential. I mean, even if you have a vehicle, cars are useful but we still mandate seatbelts. So, regardless of how amazing and life changing some folks believe these products are, as regulators and as policymakers there's a powerful opportunity to make sure consumers who do see a need in these products have appropriate protections. Those minimum protections include and I think one thing that's really wonderful about the New York bill is the tips that these lenders can solicit are a part of the total cost and it does contemplate a cap on those sort of costs. That's great. However, it doesn't state what that cap is and it leaves it to the regulator to decide. And then paired up with that provision it says that if you are offering earned wage access under this bill then you're not subject to the state usury cap. And what that does is it kind of allows the regulator to allow fees that would exceed the state cap. And in a state like New York, like Connecticut, like Vermont where they have already put in comfortable, reasonable limits on APR, we don't want to allow these payday-like products to get a carve out from those strong protections.

Rep. Ellyn Hefner (OK) thanked everyone for their presentations and stated that I recall hearing this at the last NCOIL meeting and my first initial thought was that the thing that we do is we forget about the education on financial literacy first. I did have that in high school but I know that I had to teach it to my kids because they don't teach it. And even if I think it's a good idea that we could get the money that we earned earlier, you know that but they don't even know really what that is all about and what the next steps are. I remember when I was young my Mom said you need to have good credit so you can buy a house. Well, I bought a house when I was 20, I have great credit, but it's not possible for young kids to buy houses these days. So that's not even one of those scare tactics to have good credit. So, I'm just wondering in each of your presentations I didn't hear a lot about that where we should start that earlier. I know education in my state is something that we're really talking about and related requirements. And you all can talk about the use of this and I said this and he said that but the only thing that I know is that we're talking to a big culture of people who have no understanding about what those missteps are with saving. I did like in a previous presentation talking about putting money in a place for later. Maybe we start out and look at a different model when you go check and you take $5 away and put it into an account and it grows and if there's an emergency we use it. I don't know.

But right now we're not really teaching all the things that you are referencing like lending and comparing it to your credit card or bank drafts – there is still a huge population that has no idea. So, I'd just like to hear where financial literacy comes into all this and if that's being something that you push also instead of just talking about these products.

Ms. Burks stated that I appreciate you raising that issue and I spent most of my time in law school trying to understand how to increase literacy in the exact frame that you mention. And during my time I was honored to hear a distinguished Professor who spent his career and his research focusing on this exact issue. And one of the things that his research actually revealed is that financial literacy, while it is important and powerful, actually has a much smaller impact on the wealth gap that we're witnessing in our country. And the main thing is an ongoing gap between living expenses and reasonable wages. And so you can understand everything about how to manage your money but if you're constantly trying to take care of yourself or your family on a salary that just does not cut it, that's an issue. And a lot of times you'll hear folks or certain industry people say there's no other solution and that's why we have this product but there are solutions. But in the meantime, it's important to recognize we don't want to overburden people with fees they can't afford in the absence of real viable solutions for that gap.

Mr. Smith stated that the Connecticut Department of Banking does have a fairly robust financial literacy program and we were very supportive of the bill that finally got passed last year that made financial literacy, wellness and education part of a requirement to graduate high school. So, to answer your question we are making some strides in that regard.

Sen. Felzkowski thanked everyone and stated that Asw. Hunter is going to be introducing a first draft of a Model for discussion at our summer meeting. And in the meantime if you have any questions or comments please reach out to myself, Asw. Hunter, or the NCOIL staff.

ANY OTHER BUSINESS

Sen. Felzkowski stated that I have one last piece of business to raise. Our Workers Compensation Insurance Committee has jurisdiction over a model law dealing with structured settlements. It was brought to our attention that some folks who have an interest in structured settlements weren't aware that the model was in the Committee as it does also have an annuity aspect to it as well. So, starting now and going forward this Committee will provide notice to everyone when that model is being discussed by the Work Comp Committee. For those who may have missed the Workers Comp Committee, yesterday morning there was a presentation on structured settlements for those that may not be familiar with this product and the laws surrounding them. It hasn't been decided yet as to whether the model or structured settlements in general will be put back on the Work Comp Committee's agenda for the next meeting. If you have questions or comments, reach out to the Chair, Sen. Lana Theis (MI), or the NCOIL staff.

ADJOURNMENT

Hearing no further business, upon a motion made by Del. Westfall and seconded by Rep. Lehman, the Committee adjourned at 3:30 p.m.