COURT APPROVAL OF SETTLEMENTS INVOLVING MINORS OR INCOMPETENTS

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I. SETTLEMENTS INVOLVING MINORS

Settlements involving the claims of minors present several procedural and ethical issues for the attorney. Because your client is a minor, he or she cannot be bound by contracts such as releases, if the minor chooses to disavow the contract after the minor reaches the age of majority. As a result, procedures have developed as a result of a combination between various statutes and case law requiring that any settlement contract be approved by the court.

A. COURT APPROVED MINOR'S SETTLEMENTS

Settlements of claims involving minors should be approved by court order. This applies regardless of whether settlement is reached before or after filing suit. A minor cannot be bound by proposed compromise and settlement of a minor's personal injury claim unless it is properly approved by a judge. *Gillikan v. Gillikan*, 252 N.C. 1, 113 S.E.2d 38 (1960). The courts of this state have inherent authority over the property of infants and will exercise this jurisdiction whenever necessary to preserve and protect children's estates and interests, *Sternberger Foundation, Inc. v. Tannenbaum*, 273 N.C. 658, 161 S.E.2d 116 (1968), and will look closely into contracts or settlements materially affecting the rights of infants. *Redwine v. Clodfelter*, 226 N.C. 366, 38 S.E. 2d 203.

A court approved settlement and subsequent judgment issued thereon, and the satisfaction of that judgment by the settling defendant, is not the satisfaction of a judgment under North Carolina General Statute §1B-3(e) and does not operate to discharge the other tortfeasors. *Payseur v. Rudisill*, 15 N.C. App. 57, 189 S.E.2d 562, *cert. denied* 281 N.C. 758, 191 S.E.2d 356 (1972). The court in *Payseur*, citing §1B-4, held that "where a release or a covenant not to sue is given to one or more persons liable in tort for the same injury, it does not discharge any other tortfeasor from liability unless its terms so provide."

If a settlement is reached after the lawsuit has already been filed, the guardian *ad litem* or general guardian need only file a Petition for Approval of Minor's Settlement and obtain a judgment making sufficient Findings of Facts, Conclusions of Law and approving the settlement. (Examples of such a Petition and Judgment are included as part of the Appendix hereto.)

Frequently an agreement to settle is reached before any action is filed. In such a case there are two ways in which to proceed. A Special Proceeding may be instituted pursuant to North Carolina General Statute §1-400 seeking judicial approvement pursuant to §1-402. The use of a special proceeding for this purpose was expressly approved in *Gillikan v. Gillikan, supra.*

The more common procedure for obtaining court approval is to file a friendly civil action with the issuance of a Summons and Complaint in either District or Superior Court, depending upon the amount in controversy. In this situation, the procedural aspects of the case are greatly expedited since counsel for the defendant(s) cooperates in the process. The documents necessary to consummate the settlement of a minor's claim are as follows:

(1) Petition for Appointment of Guardian *Ad Litem* (see Appendix);

(2) Order Appointing Guardian *Ad Litem* (see Appendix);

(3) Summons and Complaint;

(4) Petition for the Approval of a Minor's Settlement (see Appendix);

(5) Judgment Approving the Minor's Settlement(see Appendix).

Depending on the method of investing and holding the minor's funds, there may be additional proceedings required as discussed hereinafter. It is not uncommon to have the Summons, Complaint, Acceptance of Service, Answer and Petition for Approval of Minor's Settlement to all be filed simultaneously. In the case of such a "friendly suit" all that remains is to schedule the hearing for purposes of obtaining the judge's signature on a Judgment approving the settlement.

Because of ethical considerations that arise when settlement offers are made, I suggest that you routinely appoint someone other than the parent to act as the guardian *ad litem* for the minor child, since the parent or parents have the claim for medical bills. Rule 17 requires the appointment of a guardian *ad litem* in order to file an action on behalf of a minor child.

The procedure to be followed by a particular judge in obtaining approval of a minor's settlement varies greatly. There are judges who will approve such settlements based upon a Consent Judgment signed by all parties having an interest in the matter. In such a case, the court is obviously giving great deference to the guardian *ad litem* or general guardian and their counsel in insuring that the interests of the minor are protected. Other judges require that the minor be present in court with a parent or parents. Additionally, there are an increasing number of judges who insist on any structured settlement being with an insurance company having the highest possible rating according to Standard & Poor's, or a surety bond from such an insurance company insuring the obligation of the company issuing the annuity contract.

Before you appear before a judge for the purpose of obtaining a minor's settlement, inquire as to what information the judge will want at the hearing and the people whose appearance she will require. By making that simple inquiry, you will save yourself and your client much time and potential embarrassment.

The procedure which Judge Gregory Weeks favors is set forth in a paper presented at a previous Academy seminar.[1] Borrowing liberally from Judge Weeks' remarks,

> The court must review the record in the case. It must weigh the strength of the plaintiff's case, and determine the existence of any viable defenses. All of this must be done on the record. The minor and his counsel must be present; the parent or parents should be present at the approval hearing. In determining the relative merits of the claim and defenses, the court should review all the pleadings, available discovery and any other documentation in the file... Evidence of the plaintiff's injuries must be received. Medical and hospital records must be used in this regard. The court must also determine the defendant's ability to pay. The judge should ascertain the limits of any insurance as well as the availability of any other assets. The court must question the minor's representative and the parents as to whether they think the settlement is fair

[1] *Court Approval of Damage Awards for Minors*, the Hon. Gregory Weeks. Personal Injury Law Seminar, NCATL 4-10-92.

and reasonable. The exact amount the minor will receive in his or her trust fund must be determined and the court must find this amount is fair and reasonable.

In the process of approving the settlement, the judge must also consider the reasonableness of any proposed payments from the settlement proceeds. For example, the proceeds that are payable to the minor cannot be used to pay the medical expenses of the minor. There arises from the injuries to the minor two distinct claims for relief, one for the minor and one for the parent. *Ellington v. Bradford*, 242 N.C. 159, 160, 86 S.E.2d 925 (1955). The parents are responsible for the minor child's medical bills and the minor's recovery is for such things as pain and suffering, disfigurement, future medical bills beyond the age of 18 and future lost wages.

The court should also consider the reasonableness of the attorney's fees. Again, since the minor is unable to enter into a binding contract, it is essential that the fees the attorney is to receive be approved by the court. In passing on the amount of the fees, the judge is not bound by any fee contract signed by the parents and the attorney. Rather, the court is required to make an independent inquiry. Generally, in a minor's claim, the attorney should maintain a record of the hours spent in handling the claim and be prepared to offer an Affidavit in support of the proposed fee, depending on the judge's requirements. In a case involving a substantial recovery, it is wise to obtain an Affidavit from another attorney supporting the proposed fee. Any such affidavit should address the various factors to be considered as outlined in Rule 1.5 of the Revised Rules of Professional Conduct.[2]

B. DISBURSEMENT OF THE MINOR'S SETTLEMENT PROCEEDS

The proceeds of settlement of the minor can be disbursed in the following three ways:

1. To the Clerk of Superior Court.

The simplest and most conservative approach to the disbursement of the settlement proceeds is to have them paid into the Clerk of Court for the county in which the Judgment was

[2]These factors include (1) the time and labor required, the novelty and difficulty of the question involved, and the skill requisite to perform the legal service properly; (2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer; (3) the fee customarily charged in the locality for similar legal services; (4) the amount involved and the results obtained; (5) the time limitations imposed by the client or by the circumstances; (6) the nature and length of the professional relationship with the client; (7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and (8) whether the fee is fixed or contingent.

approved. When this is done, the Clerk invests the funds for the benefit of the minor child in very secure conservative investments. A one-time fee in the amount of five percent of the amount deposited is subtracted from that amount. The investment then grows until the child reaches the age of 18, at which time the minor may apply for receipt of the funds upon proof that she has obtained the age of 18 years. The obvious benefits to this method of holding the minor's funds is the elimination of any bonding requirements, monitoring of investments and annual accounting as discussed hereinafter.

2. Invested in an annuity pursuant to a structured settlement.

When the settlement contemplates the purchase of an annuity, there are no funds to be deposited and the attorney for the minor will typically receive a copy of the annuity contract. Superior Court judges are becoming more active in withholding the approval of a structured settlement unless they are satisfied that the insurance company behind the annuity is sound, or that there is an additional surety behind the annuity contract. It is recommended that if the insurance company issuing the annuity is not a well-known insurance company, that counsel be prepared to provide the rating from Standard and Poor's. That rating can be found on the Internet at "www.standardandpoors.com/ratings/insurance/main.htm."

3. To a guardian of the child's estate.

If a parent or a financial advisor is to be the guardian of the minor's estate for the purpose of investing the funds, that person must be appointed by the Clerk of Court and bonded (N.C.G.S. §35A-1230-31). When the funds are paid to the guardian, I recommend that the Judgment Approving the Settlement reflect that the payment of the minor's proceeds be made directly into the Clerk of Court directing that the Clerk simply hold the funds for payment to the guardian. The Judgment may also direct that the funds be paid directly to the guardian if the person has been appointed. However, when the proceeds are given to the Clerk, advise that they are going to be disbursed to a guardian for the estate. The Clerk will not deduct the five percent fee in such a circumstance. Then, once the guardian for the estate of the minor has been duly appointed and bonded, the money is paid to the guardian of the child's estate.

Arrange to have the insurance company's agent appear with you and the guardian at the Clerk's office for the appointment of the guardian. That way the bond is in place and all of the paperwork can be accomplished at one meeting at the Clerk's office. The amount of the bond is 1.25 percent of the principal up to $100,000.00, and bond is reduced to 1.10 percent for amounts over $100,000.00. The premium for the bond can be paid from the minor's funds.

Pursuant to N.C.G.S. §35A-1232 (BILL CHECK THIS) if the principal has been or will be deposited in a bank in North Carolina or invested in an account in an insured savings and loan association, upon condition that the money or securities will not be withdrawn except upon authorization of the Clerk, the Clerk may, in its discretion, order that the money be so deposited or invested, and exclude that deposited amount from the computation of the amount necessary for the bond. This is called the receipt and agreement exemption from the bond requirement. The Clerk's office will have the required form for accomplishing this exemption.

Once the guardian of the minor's estate has been appointed, his or her powers are provided by statute. Generally, this includes investing the assets of the ward as a reasonably prudent business person would do. Also, this would include payment on the ward's behalf of necessary and reasonable expenses incurred in handling the funds. You must stress to the

guardian of the estate that the child's funds may not be used to pay for the child's ongoing needs, since that is a parental obligation. Court approval should always be obtained.

If the minor would otherwise be eligible for certain governmental benefits, placing the funds in the hands of the guardian may result in the loss of these benefits. Since there are other speakers addressing the creation of a special needs trust, to avoid the loss of governmental benefits, it is not discussed in this paper.

C. PROCEDURE IN FEDERAL COURT

The procedure followed in federal court is substantially the same as that outlined for state court. Always check the local rules. In the Middle District the local rule 17.1 (see Appendix) provides the procedure to be followed in great detail. Once the settlement is approved, the Judgment then directs that the payment of any funds due the minor would be paid to the Clerk of Court for the county in which the child resides or to a guardian. The use of the phrase in local rule 17.1(f), "the legal guardian of the minor or incompetent" means a duly appointed guardian under the procedures outlined above.

D. WAIVER OF COURT APPROVAL

In personal injury actions involving only mild or insignificant injury to the minor, insurance carriers will sometimes waive the requirement of court approval, taking the risk that the minor will not choose to renounce the settlement when he or she reaches the age of 18. In such a circumstance, the insurer will require the parent receiving the funds for the benefit of the minor to indemnify the defendant and carrier from any subsequent action by the minor.

This writer thinks that settling such claims is extremely risky and should be done only in very limited circumstances where the amount received by the minor is inconsequential. In settling such a case without court approval, the attorney is assisting in the resolution of the minor's claim in such a way that the minor does not have the safeguards mandated by law when the settlement is approved by the court.

E. AVOIDING ETHICAL CONFLICTS IN THE SETTLEMENT OF MINOR'S CLAIMS

A common factual scenario presents ethical considerations which you must be mindful of early in the representation. You are contacted by a parent of a minor child who has suffered serious personal injuries. The parent contacting you is not a potential defendant but has her own claim for the medical bills associated with her minor child's personal injury. She wants you to pursue all claims available to recover for her and the minor child. Those claims include her claim for medical bills and the child's claim for personal injury. You agree and proceed to file suit with her being the guardian *ad litem* and a plaintiff in her own capacity seeking compensation for medical expenses. You learn that the insurance proceeds available are $25,000.00. Obviously the insurance available is insufficient to pay the to claims. You have no agreement regarding the division of the proceeds. You receive an offer to settle the case for the available insurance. Under those facts, you would be required to terminate your relationship of both the parent and the child.

In 1992 the North Carolina State Bar issued an ethics opinion holding that a lawyer may not present parents as guardians *ad litem* for their injured child and as individuals concerning their related tort claim after receiving a joint settlement offer which is insufficient to fully satisfy all claims. In RPC 109, issued January 17, 1992, the State Bar ruled that there was an *irreconcilable* conflict between the parent acting as guardian *ad litem* and the parent pursuing

her personal claim. As the attorney any attempt you make to resolve that conflict would be benefitting one client at the expense of the other. The State Bar ruled that,

> Under the circumstances, Law Firm A must withdraw from representing both clients. The attorneys may not continue representing either of their clients unless their continuing participation is intelligently consented to by the other client, and this is impossible under the facts stated.

Fortunately, the State Bar issued RPC 123, which provides, "This Opinion is intended to address in a broader way the issues raised in RPC 109. It is offered for the general guidance of the bar and is not intended to contradict the advice given in response to the specific facts recited in RPC 109."

In RPC 123, the State Bar opined that an attorney could represent the parents on their individual claim for medical bills and the child under the circumstances outlined in the opinion. The attorney must insist upon the appointment of an independent guardian *ad litem* for the child. The State Bar ruled that since the interests of both the child and the parents are aligned to the extent of establishing negligence of the tortfeasor, it is unlikely that any actual conflict would arise until receipt of a settlement offer. The receipt of a single settlement offer to settle both claims does not *automatically disqualify* the attorney. The attorney may attempt to assist the clients in evaluating the claims and reaching an amicable agreement as to how to divide the proceeds, but under no circumstances may the attorney advocate for one client over the other. If such a dispute arises, the attorney would be permitted to withdraw from the representation of one client upon the consent of the other.

Therefore, whenever there is a potential for conflict between the parent and child, avoid any potential by having an independent guardian appointed. This writer routinely uses another attorney for such purposes. The application for the petition of a guardian *ad litem* included in this Appendix is for such an appointment.

II. THE SETTLEMENT OF AN INCOMPETENT'S CLAIM

Just as a minor is unable to enter into a binding contract, so is an incompetent adult. Therefore, proceeding on behalf of an incompetent adult raises many of the same ethical considerations and need for judicial approval.

Let's begin with the scenario in which you are asked by family members to represent a plaintiff and there is no dispute that the plaintiff is an incompetent adult. However, there has

not yet been an adjudication of incompetency and no appointment of a guardian *ad litem*, general guardian, guardian of the person or a guardian of the estate.[3]

In order to file the lawsuit, do you have to initiate an incompetency proceeding? No. Rule 17(b)(1) clearly provides that when a plaintiff is incompetent, they *must* appear by general guardian or by guardian *ad litem* appointed as provided in Rule 17. Rule 17(c) simply provides that a guardian *ad litem* shall be appointed, "At any time prior to or at the time of the commencement of the action, upon the written application of any relative or friend of said...incompetent person or by the court on it's own motion." Additionally, Rule 17(b)(3) provides that a guardian *ad litem* for an incompetent person,

> May be appointed in any case when it is deemed by the court in which the action is pending expedient to have the...incompetent person so represented, notwithstanding such person may have general or testamentary guardian.

Therefore, as a practical matter, you may initiate an action on behalf of an incompetent adult with the simple appointment of a guardian *ad litem* pursuant to Rule 17. However, it is important to be mindful of the fact that such an appointment is not an adjudication of incompetence pursuant to N.C.G.S. §35A-1101 *et. seq.* Therefore, before any proceeds could be paid in settlement of such an action, it will be necessary to have an adjudication of incompetency and the appointment of either a general guardian or a guardian of the estate, pursuant to §35A article 1 through article 5. (Article 1 sets for the procedure for a determination of incompetence and Article 5 sets forth the procedure for the appointment of a guardian of the incompetent person.)

If you represent a person for whom there can be no reasonable dispute as to their competence, there is no reason not to move forward early in the litigation with an adjudication of incompetence.

Rule 17 and case law provide that an action may proceed in the name of a guardian *ad litem* even if there is a general guardian. *Rutledge v. Rutledge*, 10 N.C. App. 427, 179 S.E.2d 163.

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[3]N.C.G.S. §35A-1202 defines the distinctions between the various types of guardian: Sub-section (7) provides, "'General guardian' means a guardian of both the estate and the person." Sub-section (8) provides, "'Guardian *ad litem*' means a guardian appointed pursuant to G.S. 1A-1, Rule 17, Rules of Civil Procedure." Sub-section (9) provides, "'Guardian of the estate' means a guardian appointed solely for the purpose of managing the property, estate and business affairs of a ward." Sub-section (10) provides, "'Guardian of the person' means a guardian appointed solely for the purpose of performing duties relating to the care, custody and control of the ward."

Once you have proceeded with an adjudication of incompetency and obtained the appointment of a guardian of the person for the plaintiff, you are then prepared to obtain judicial approval of any proposed settlement and able to disburse the proceeds. The procedure is very similar to that procedure followed in obtaining judicial approval of a minor. You must petition the court for approval of the settlement by presenting a summary of the settlement to the court having jurisdiction over the matter. The Petition should set forth the facts necessary to allow the court to evaluate the fairness of the settlement and the payment of any attorney's fees and expenses. The Judgment should direct that the net recovery of the incompetent plaintiff be held in an interest-bearing account established by plaintiff's counsel as an officer of the court, or by the Clerk of Court pending and Order establishing any limitations and restrictions upon the general guardian's or the guardian of the estate's ability to expend those funds.

If the funds to be handled by the general guardian are substantial, it is recommended that an Order be entered pursuant to 35A-1215 setting forth any limitations and restrictions of the guardian's use of the ward's settlement proceeds. Of course any such guardian is required to be bonded and to make annual reports to the Clerk. North Carolina General Statute §35A-1201 *et. seq.* gives the Clerk of Court broad powers in controlling the use of the ward's funds by the guardian. (An example of an Order establishing limitations and restrictions on a guardian's use of the funds is attached hereto as part of the Appendix.)

Let's assume that you have been engaged by a plaintiff whom you believe was competent and believe that a potential settlement is imminent. However, you have concluded, in large part based upon private confidential communications with your client, that the plaintiff is no longer competent to manage his affairs.[4] You attempt to discuss this with the plaintiff who is insistent that you not proceed to take any action for the appointment of a guardian or declaration of incompetence. Your conviction that the plaintiff is incompetent is not altered by your client's refusal to participate in such a proceeding. What should you do?

Fortunately, the North Carolina State Bar's revised Rules of Professional Conduct, Rule 1.14 give us some guidance. That rule provides as follows:

RULE 1.14 CLIENT UNDER A DISABILITY

[4]N.C.G.S. §35A-1101(7) defines "incompetent adult" as follows: "An adult...who lacks sufficient capacity to manage the adult's own affairs or to make or communicate important decisions concerning the adult's person, family, or property whether the lack of capacity is due to mental illness, mental retardation, epilepsy, cerebral palsy, autism, inebriety, senility, disease, injury or similar cause or condition."

> (a) When a client's ability to make adequately considered decisions in connection with the representation is impaired, whether because of minority, mental disability, or for some other reason, the lawyer shall, as far as reasonably possible, maintain a normal client-lawyer relationship with the client.
>
> (b) A lawyer may seek the appointment of a guardian or take other protective action with respect to a client only when the lawyer reasonably believes that the client cannot adequately act in the client's own interest.

Therefore, you must continue to involve your client in every way possible with all decisions in the case and treat the client as any other client without regard to their mental impairment. You are permitted to initiate the appointment of a guardian as provided in the Rule. RPC 157 specifically opines that a lawyer may seek the appointment of a guardian for a client the lawyer believes to be incompetent over the client's objection if reasonably necessary to protect the client's interest.

When faced with the dilemma contemplated by this hypothetical, the attorney must be mindful of Rule 1.6 regarding the attorney's duty to protect confidential information. The rule defines confidential information in Rule 1.6(a) as follows:

> Confidential information refers to information protected by the attorney-client privilege...and other information gained in the professional relationship that the client has requested be held inviolate or the disclosure of which would be embarrassing or would be likely to be detrimental to the client...

Therefore, if information that you have that you would be required to disclose as part of the initiation of any such proceeding is confidential under that definition, are you required to disclose it? Rule 1.6(c) expressly provides that a lawyer shall not knowingly reveal "confidential information," except as provided in paragraph (d). The only sub-paragraph of (d) which may apply is the one which states that you may reveal "(3) confidential information when permitted under the Rules of Professional Conduct are required by law or court order."

The lesson in all of this is if you are approaching a settlement with an incompetent adult, who resists the appointment of a guardian, you must tread very carefully. Any interested person may initiate the appointment of a guardianship in a declaration of incompetency. (See 35A-1106 and 35A-1210.) Hopefully a medical care provider or family member will have the same concerns and initiate such a procedure.

Suppose you are approached by the wife of an incompetent person. The incompetent plaintiff has a personal injury claim and the wife has what you consider to be a valuable loss of consortium and/or negligent infliction of emotional distress claim. Although there are no rulings which directly address this circumstance, it would appear that precisely the same considerations that gave rise to R.P.C. 109 and 123 would dictate your considerations and such a joint representation. It is our policy to only engage in such joint representation upon the appointment of someone other than the wife as the guardian *ad litem* or general guardian of the incompetent. Additionally, it is wise to discuss and anticipate the division of any proposed settlement by agreement before any such offer is made. If handled with a full disclosure and discussion of the potential conflicts, a written agreement between either a general guardian, a guardian *ad litem* and the wife will avoid many sleepless nights after the offer has been made.