



A minor compromise

Where the funds go when resolving a minor's claim requires due consideration



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The lawyer sat with his client's parents in the mediation room. They discussed the final offer and determined it was acceptable. Time to settle their minor child's case. The parents turned to the lawyer. "That's a lot of money for a 12-year-old. Can you tell us more about that structure thing you were talking about?"

"Sure," said the lawyer, "We should talk about it and the process we now need to go through. The court has to review and approve a minor's settlement. There are restrictions on what can be done with the money."

Petition to compromise

Settling a minor's case requires court approval. The formal method for doing this is a petition to compromise (a minors' comp). Major changes were made to this process in 2010. These changes were designed to standardize the fees and approval process. Prior to this, some counties had local rules that artificially limited attorneys' fees – some as low as 10 percent. Doing away with these arbitrary local fee limits is the plus. The minus is a mandatory Judicial Council form that is nearly as fun as an IRS 1040. Just like the 1040EZ, there's a short form for simple cases that can be submitted without hearing.

Why all the hoops? The court wants to protect minors. This includes making sure the settlement amount is appropriate, the attorneys' fees and costs are not excessive, and the money is protected from nefarious friends and family.

It's about the money

As part of the compromise, the court reviews how the minor's settlement funds will be set up. The typical methods are blocked accounts and structured settlements. Courts are also agreeable to certain 529 plans – savings plans for college tuition.

•Blocked accounts

A blocked account requires court approval to release bank funds. These accounts require little effort on a lawyer's part for upfront planning. But blocked accounts are unusual. It can be frustrating for a parent – unfamiliar with bank rules – to try to get one set up with a bank manager – unfamiliar with court rules. Additionally, the lawyer will often get a call when the minor turns 18 and needs the account unblocked. Interest on blocked accounts also tends to be awful.

•Structures

A structured settlement is another useful tool. This allows the funds to be placed in a tax-free annuity that can be tailored to the child's anticipated needs. While settlements are not taxable, interest generated is. The structure avoids this. Assuming it starts paying out after the child turns 18, one avoids blocked account protocol. The downside is that planning a child's needs that far out can be difficult. Once structures are set up, they are difficult to undo without huge financial impact. Factoring companies will purchase a structure for upfront cash but the losses are significant. The rate at which structured money grows (\$100,000 now being overall \$150,000 in structure payments 10 years from now, for example) is directly impacted by interest rates. Low interest rates mean structures may not always be the best option.

•529 Plans

The IRS created a tax-advantaged method to save for college, known as a 529 plan. The interest earned is not taxable, one advantage over a blocked account. The interest rate tends to be better than blocked accounts and many structures as well. The funds can be disbursed as one sees fit instead of a rigid structure schedule. But the funds can only be used for certain educational expenses. If using this tool for a minor, one will need a special tool known as a California Uniform Transfer to Minors Act (CUTMA) 529. Not difficult, but a nuance. Otherwise the parent technically owns and controls the 529 (and could theoretically gift it to someone else.)

Earn your keep

The court also determines whether the attorneys' fees requested and costs are appropriate for the work performed. Don't be shy about outlining the risk, expense, and time spent handling the case – some courts are not shy about cutting fees. This goes into the supporting declaration. If the case is particularly difficult and one will be seeking a higher fee than usual, consider making a motion to approve the fee at the beginning. A good settlement looks easier at the end than at the beginning.

By law, costs in minors' cases are deducted before fees are taken. In cases where both the parent and child are receiving funds, make sure they understand that the more money allocated to the minor, the lower the overall fee. Courts are more likely to approve the compromise, appreciate that the clients were counseled on it, and it is in accord with one's ethical duties (even if it is not in one's own financial interest).



Outro

The lawyer and family discussed the various options available. After a few days reviewing various structure proposals and 529 plans, the family decided on what was right for their child. The court approved the petition a couple months later.

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