

SETTLEMENT ISSUES

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I. PRO TANTO SETTLEMENTS

Alabama law recognizes the validity of a pro tanto settlement whereby one or more joint tortfeasors can settle with and be released by a plaintiff while plaintiff proceeds against the remaining joint tortfeasors.¹ A couple of issues may arise, however, once the settlement is consummated and the plaintiff proceeds against the other parties.

A. Setoff Issues

A joint tortfeasor not released may place into evidence a pro tanto settlement the plaintiff reached with another joint tortfeasor, or it may ask that any amounts awarded against it be reduced by the amount of the settlement reached with the other tortfeasor. However, a defendant can not both present evidence of the pro tanto settlement and seek a setoff from the court.²

The issue of setoff can be addressed by the court in its charge to the jury by giving Alabama Pattern Jury Instruction 11.30, which provides as follows:

The plaintiff originally made claim against (party released) and (_____) the defendant(s) in this case for damages growing out of the (the occurrence made the basis of this suit). The plaintiff in consideration of the sum of \$_____ released (party released) and reserved (his) (her) right to proceed against the present defendant(s) _____. If you are reasonably satisfied from the evidence that the plaintiff is entitled to recover in this case then in arriving at the amount of damages to be awarded to the plaintiff you will determine from the evidence the total amount of damages suffered by the plaintiff and then give credit for the amount of \$_____ which the plaintiff has already been paid by (party released) and render a verdict for the plaintiff for the balance remaining.³

¹ See Steenhuis v. Holland, 115 So. 2 (Ala. 1927).

² See Dynasty Housing, Inc. v. McCollum, 2001 WL 699937 at *2 (Ala. June 22, 2001).

³ APJI 11.30 (2d Ed. 1993).

1. Must be joint tortfeasors to be entitled to setoff

In State Farm Fire & Casualty Co. v. Slade, 747 So. 2d 293 (Ala. 1999), plaintiffs sued their homeowners insurance carrier and several contractors involved in the construction of their home. Plaintiffs entered into a pro tanto settlement with the contractors and proceeded against State Farm alleging breach of contract, bad faith and fraud. The jury awarded the plaintiffs \$668,850 in compensatory damages but reduced that award by \$301,500, the amount of the pro tanto settlement with the other defendants.⁴ State Farm appealed and the plaintiffs cross-appealed. Plaintiffs argued, among other things, that the trial court should not have allowed evidence of the pro tanto settlement with the construction defendants or a setoff because those defendants and State Farm were not joint tortfeasors.⁵ The court agreed, holding that there was no “single, indivisible injury” caused by the construction defendants and State Farm, as is required for joint and several liability. The court reasoned that there were actually two injuries resulting from two separate tortious acts: “(1) damage caused by the alleged negligent and/or wanton construction that was done by the construction defendants and (2) damage caused by the alleged bad-faith refusal to pay an insurance claim.”⁶ Thus, the court concluded that because the construction defendants and State Farm were not joint tortfeasors, the trial court should not have allowed State Farm to introduce evidence of the pro tanto settlement and seek a setoff of the amount received from the construction defendants.⁷

⁴ See Slade, 747 So. 2d at 302.

⁵ Id. at 324.

⁶ Id. at 325.

⁷ Id.

2. Application in arbitration proceedings

A recent Alabama Court of Civil Appeals case illustrates that the rules relating to pro tanto settlements and setoffs apply equally in arbitration proceedings. In Dynasty Housing, Inc. v. McCollum, 2001 WL 699937 (Ala. Civ. App. June 22, 2001), plaintiffs sued both the manufacturer and seller of their mobile home. On the defendants' motion, the trial court ordered the case to arbitration.⁸ Before the arbitration hearing was held, the plaintiffs entered into a pro tanto settlement with the manufacturer for \$20,000 and the claims against the manufacturer were dismissed with prejudice. During the arbitration hearing, the remaining defendant introduced evidence of the plaintiffs' pro tanto settlement with the manufacturer. The arbitrators ordered as follows: "Majority of arbitrators find for plaintiffs on issue of negligence *and taking into account all sums previously recovered* award Plaintiffs the sum of \$25,000.00."⁹ The defendant moved for a setoff of the amount of the pro tanto settlement but the trial court denied the motion. On appeal, the Court of Civil Appeals held that a defendant may either present evidence of a pro tanto settlement or seek a setoff, but not both. The court pointed out that the arbitrators, pursuant to the arbitration agreement, had the power to award money damages, that their award was to be final and binding, and that the arbitrators clearly considered the pro tanto settlement in fashioning their award to the plaintiffs. Therefore, the defendant was not entitled to a setoff.¹⁰

3. Setoff allowed even where settling defendant found not liable.

The Alabama Supreme Court recently addressed an issue of first impression relating to a defendant's right to a setoff of amounts paid by another defendant pursuant to a pro tanto settlement. In Ex parte Goldsen, 783 So. 2d 53 (Ala. 2000), the plaintiff settled with one driver

⁸ McCollum, 2001 WL 699937 at *1.

⁹ Id.

¹⁰ Id. at *1-*2.

involved in a chain reaction automobile accident and then sued a second driver. The plaintiff also sued her own insurer for underinsured motorist benefits.¹¹ At trial, the jury awarded the plaintiff \$76,898.39 against the second driver. In addition to determining the liability of the second driver, the jury was also instructed to determine the liability of the first driver who had already settled with the plaintiff because of the issues involving underinsured motorist coverage. The jury found that the first driver had not been negligent.¹² The second driver moved to have the jury award set off by the amount of the settlement with the first driver but the trial court denied the motion. The Court of Civil Appeals affirmed the trial court's decision but the Alabama Supreme Court granted certiorari review.¹³ The court addressed, for the first time, the following issue: "Whether damages that a jury awards against a negligent defendant can be offset by a pro tanto settlement when the jury has found that the settling party was not negligent, and, therefore, would not be liable for the damage to the plaintiff."¹⁴ The court recognized a split among jurisdictions on the issue, but pointed out that the majority view holds that a setoff should be allowed, even where the party settling was not liable to the plaintiff.¹⁵ The court reasoned that this view is consistent with the general proposition that compensatory damages are designed to make the plaintiff whole and that a plaintiff is entitled to only one recovery for a single injury. Thus, the court concluded that the jury award should have been reduced by the amount of the pro tanto settlement.¹⁶

¹¹ See Goldsen, 783 So. 2d at 54.

¹² Id.

¹³ Id.

¹⁴ Id. at 55.

¹⁵ Id. at 55-56.

¹⁶ Id. at 56-57.

B. Cross-Claims or Third-Party Claims by Other Defendants

A defendant who enters into a pro tanto settlement with a plaintiff, where the plaintiff has claims remaining against one or more other defendants, is not necessarily out of the woods. Often one of the other defendants will attempt to bring the settling defendant back in by asserting a previously filed cross-claim or filing a third-party claim against the settling defendant. Of course, this defeats the purpose of settling a case as potential liability remains and litigation expenses continue to be incurred. The strongest defense to such a claim is that Alabama law as a general rule does not allow contribution among joint tortfeasors. That is, one party that is alleged to be guilty of wrongful conduct cannot require another party to contribute money to make the plaintiff whole.¹⁷ However, some remaining defendants may attempt to avoid the application of this rule by asserting their claim as a breach of contract claim rather than a tort claim if any type of contract exists. In order to protect itself against such a claim, a settling defendant will often include an indemnity provision in the release to be executed by the plaintiff, whereby plaintiff agrees to indemnify the settling defendant for any amounts recovered on cross-claims or third-party claims against the settling defendant by the other defendants. Such a provision offers some protection and peace of mind to a defendant entering into a pro tanto settlement.

¹⁷ See Crigler v. Salac, 438 So. 2d 1375 (Ala. 1983) (there is no contribution among joint tortfeasors).

II. PRO AMI SETTLEMENTS

While there have been few developments and no substantive changes in the law relating to pro ami settlements in recent years, it is worthwhile to review the requirements in order to ensure that settlements involving minors are approved and not subject to a challenge by the minor once he or she reaches the age of majority. Mere court approval of a settlement does not necessarily mean it can not be challenged. Courts must meet the requirements set forth by the Alabama Supreme Court to avoid the possibility of the settlement being set aside.

A. Substantive Hearing with Extensive Examination of the Facts

Perhaps the most informative and illustrative case on this issue is Large v. Hayes, 534 So. 2d 1101 (Ala. 1988). In Large, the Court confirmed that more than mere pro forma approval of a settlement is necessary, holding that “there must be a hearing, with an extensive examination of the facts, to determine whether the settlement is in the best interest of the minor.”¹⁸ The extensive examination of the facts should include testimony from the minor’s next friend, the guardian ad litem if one has been appointed, and the minor if possible. Each should testify as to the minor’s injuries, treatment and prognosis, as well as their understanding of the settlement terms and whether they believe it is in the minor’s best interest. While examination of these witnesses may be conducted by the attorneys involved, the court often prefers to question the parties in order to satisfy the court that no conflict of interest exists and that the settlement is in the best interest of the minor. It is also prudent to introduce the minor’s medical records, depositions taken in the case and any other evidence relevant to liability or the minor’s injuries. The minor’s attorney and the guardian ad litem should also testify regarding their respective fees and expenses, as the court must determine that the attorney’s fee is reasonable and must

¹⁸ Large, 534 So. 2d at 1105.

determine the amount of the guardian's fee.¹⁹ Finally, the parties should always insist that a court reporter be present during the hearing and that the proceedings be recorded. A complete record will be the best evidence that a substantive hearing and extensive examination of the facts was conducted if the settlement is ever challenged.

B. Guardian Ad Litem

Rule 17(c) of the Alabama Rules of Civil Procedures provides that “[t]he court shall appoint a guardian ad litem (1) for a minor *defendant*, or (2) for an incompetent person not otherwise represented in an action and may make any other orders it deems proper for the protection of the minor or incompetent person.” Similarly, Rule 17(c) of the Federal Rules of Civil Procedure provides that “[t]he court shall appoint a guardian ad litem for an infant or incompetent person not otherwise represented in an action or shall make such other order as it deems proper for the protection of the infant or incompetent person.” Thus, neither rule actually requires that a guardian ad litem be appointed for a minor plaintiff who is already represented in the suit by a “next friend.” However, it is nevertheless advisable to have a guardian ad litem appointed to ensure that no conflict of interest exists, as can be the case where the next friend is also a party plaintiff and has a claim being settled along with that of the minor. The guardian ad litem’s participation and testimony provides added protection of the legitimacy of a settlement if ever challenged.

C. Recent Case Law

One recent case has addressed and clarified the issues discussed herein. In Burke v. Smith, 252 F.3d 1260 (11th Cir. 2001), the Eleventh Circuit considered a challenge to an order approving a minor’s settlement by the district court. A deceased accident victim’s minor

¹⁹ See Peebles v. Miley, 439 So. 2d 137 (Ala. 1983) (setting out factors to be considered in determining reasonable of attorney’s fee).

daughter, by and through her mother, brought a wrongful death action against alleged tortfeasors. The mother was also a party plaintiff individually and as administratrix of her husband's estate.²⁰ The defendants settled the case and obtained a release of all claims. However, the release was signed only by the mother as administratrix of the estate and individually. The minor did not execute the release nor did the mother sign it on her behalf as next friend.²¹ The court did not appoint a guardian ad litem to represent the minor nor did it conduct a hearing regarding the settlement agreement. The court merely dismissed the case with prejudice upon receipt of a stipulation of dismissal.²²

After reaching the age of majority, the minor filed a Rule 60(b)(4) motion alleging that the judgment dismissing the case was void because (1) the court had not appointed a guardian ad litem and because (2) no hearing was held to determine the fairness of the settlement. The district court granted the motion and subsequently entered an order clarifying that the judgment of dismissal was set aside as to the minor plaintiff only, and not as to the other plaintiffs.²³

In addressing the minor's first argument, the court pointed out that Rule 17(c) does not require the appointment of a guardian ad litem if the minor is otherwise represented and the minor in this case was otherwise represented by her mother. The court refused to find that there had been a conflict of interest necessitating the appointment of a guardian ad litem, reasoning However, in addressing the minor's second argument, the court agreed that under clear Alabama

²⁰ Burke, 252 F.3d at 1262.

²¹ See Id.

²² Id. at 1262-63.

²³ Id. at 1263.

law²⁴ a hearing must be conducted in order to determine the fairness of a minor settlement for that settlement to be binding on the minor. The court therefore affirmed the district court's dismissal of the judgment.²⁵

Although the Eleventh Circuit agreed with the district court's dismissing the judgment, it ruled that the district court had erred in setting aside the judgment as to the minor plaintiff only. Reasoning that a judgment is either void or it is not, the court held that the judgment, which dismissed the entire action and did not distinguish the particular plaintiffs, must be set aside in its entirety.²⁶

D. Distributing Settlement Funds

The Alabama Uniform Guardianship and Protective Proceedings Act (AUGPPA) provide that settlement proceeds may be paid on behalf of a minor to:

- (1) Any person having the care and custody of the minor and with whom the minor resides;
- (2) A guardian of the minor; or
- (3) The judge of probate of the county in which the minor resides, if a resident of this state, or, if a non-resident, to the judge of probate or like officer of the county in which the debtor or creditor resides.²⁷

²⁴ The court concluded that the question of a fairness hearing and approving a minor settlement was a matter of state substantive law and applied in this diversity action.

²⁵ Id. at 1265.

²⁶ Id. at 1267.

²⁷ Ala. Code § 26-2A-6(a) (1992).

However, this can be done only if the payments do not exceed \$5,000 if payable as a single payment or \$3,000 per year if paid in a series of payments. Furthermore, the total amount of payments if the settlement is paid as a series of payments may not exceed \$25,000.²⁸ If the payment or payments to be made exceed these allowed amounts, a conservator must be appointed by a probate court and the proceeds paid to the conservator pursuant to the AUGPPA.

Another provision of Alabama law appears to provide an alternative method for payment of settlement proceeds. The Alabama Uniform Transfers to Minors Act (AUTMA) provides that one owing a debt to a minor not having a conservator “may make an irrevocable transfer to a custodian for the benefit of the minor” as long as the amount does not exceed \$10,000 at the time of the transfer.²⁹ Payment of minor settlement proceeds under this provision is accomplished by making the check payable to the minor’s parent “as custodian for (name of minor) under the Alabama Uniform Transfers to Minors Act.”³⁰ The comment to § 35-5A-8 of the AUTMA specifically states that a tort judgment debtor of a minor may create a custodianship under that section.

The AUTMA is a newer law than the AUGPPA, and courts tend to be more familiar with the provisions of the AUGPPA. Therefore, courts may object when an attempt is made to transfer an amount under the AUTMA that exceeds the limits of the AUGPPA. However, the law clearly seems to allow a tort debtor to proceed under either provision.

²⁸ *Id.* Also, the person making the payments must file a notice of such payment with the probate court.

²⁹ Ala. Code § 35-5A-8(a) (1991).

³⁰ Ala. Code §§ 35-5A-8(a); 35-5A-10 (1991). If a custodian other than the parent has already been nominated, payment must be made to that person rather than the parent.