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Crafting an enforceable settlement agreement

Taking the time to include key provisions in drafting settlement agreements can prevent lost clients, lost money, and even malpractice suits.

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Enforceability of settlement agreements is an important consideration for all of us. Whether you are plaintiff or defense counsel or mediator, our common goal is securing a settlement that satisfies you and your clients. None of us likes the idea of spending the time, money and effort to reach and draft agreements on what we think are the important settlement terms only to realize afterward that key terms were left out or left uncertain. And we shudder to think that the settlement agreements we have drafted might be held unenforceable if challenged, possibly resulting in lost clients, lost money and malpractice suits.

The California Supreme Court has wisely cautioned counsel to "be wary of 'overly broad, loose terms in release agreements'" stating that "'(A)ttorneys' energies are better spent making sure that release agreements accurately reflect their clients' intentions than in litigating what their clients really intended when they signed agreements.'" (*Hess v. Ford Motor Co.* (2002) 27 Cal.4th 516, 530).

So what can counsel do to craft complete and durable agreements which will stand up to challenge and which eliminate uncertainties between parties and counsel?

First, have a draft settlement agreement to take with you to *each* mediation or settlement discussion.

Second, remember that some "general" provisions we might not always think of as being valuable negotiation items may in fact be of value to one or more parties and may significantly impact the overall agreement or outcome.

Third, have a solid understanding of the laws regarding settlement agreement enforcement before approving a settlement agreement.

Settlement agreement provisions

The following is a comprehensive outline of settlement provisions to be considered and discussed with clients and included in a draft settlement agreement before mediation. It is helpful to refer to the draft agreement as a checklist during mediation to make the best use of the many provisions which may be used as leverage. These provisions are in addition to any specific provisions which may be required pursuant to the circumstances and laws governing each individual case.

Recitals or Introduction

Recite information here that is not part of the terms of the agreement but which provides the necessary context for the forthcoming material terms:

- Identify the parties to be bound by the agreement. Include full names, d.b.a.'s, or relevant aliases, and indicate how each party will be referred to throughout the agreement.
- Identify the legal counsel involved and who each attorney represents.
- For corporate parties, identify the individuals who have authority to bind the corporation.
- Identify the court case number or indicate that no case is pending in any court.
- Identify the nature of the dispute or the claims alleged.
- Identify the purpose of the settlement (*e.g.*, to resolve the parties' conflicting claims efficiently, informally and without the costs associated with lengthy litigation).
- Identify the purpose of the settlement agreement itself (*e.g.*, to settle all claims and causes of action arising out of the action).

Material terms of the agreement

***For settlements involving the provision of money, counsel should*:**

- Identify the specific sum of money to be produced.
- Clearly identify each party to provide the funds and each party to receive the funds, including specific allocations in cases with multiple plaintiffs or defendants. (See, *Gauss v. GAF Corp* (2002) 103 Cal.App.4th 1110, 1123.)

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• Identify the specific method of payment (check, cashier's check, wire transfer).

• Determine whether issuance will be from an out-of-state bank delaying availability of settlement monies.

• Identify the number of checks to be produced and identify the payee *and* recipient of each check (*e.g.*, one check to counsel to make disbursements? Separate checks for counsel and clients sent separately or all sent to one recipient?).

• Identify whether taxes should or should not be withheld based on the specific circumstances and applicable laws and indicate whether IRS 1099 forms will be issued and to whom.

• Determine whether an apportionment of settlement funds as to the type of injuries or damages will be included by considering the circumstances and potential ramifications for taxes and child/spousal support. (See, *In re Marriage of Heiner* (2006) 136 Cal.App.4th 1514.)

• Identify whether payment will be a one-time lump sum or a structured settlement with a payment schedule which might allow parties to reach a settlement that would otherwise be impossible.

• Identify the specific timing of the payments to be made including the number of days or months as well as the method of calculating (business days or calendar days); check the calendar to confirm that payment is due on a date that actually works for the parties.

• Identify the rate of interest which will apply if payment is not made within the time specified (*e.g.*, 10 percent for unsatisfied money judgments per Civ.Code, § 685.010, but this can be negotiated).

• Identify any other provisions or penalties for nonpayment such as liquidated damages. (See, Civ. Code, §1671 on validity of liquidated damages.)

• Don't forget the liens. Attorneys risk personal liability if they settle around known liens (*Kaiser Found. Health Plan, Inc. v. Aguiluz* (1996) 47 Cal.App.4th 302, 305) and the State Bar may discipline an attorney who purposely disregards a known lien. (*Matter of Respondent P.* (Rev.Dept. 1993) 2 Cal. State Bar Ct. Rprtr. 622).

For settlements involving non-monetary "performance" terms, counsel should:

• Identify specifically what is going to happen (*e.g.*, adopt new policies; make repairs; post warning signs; issue public apology or private letter of apology, etc.).

• Identify with as much specificity how it is going to happen.

• Identify who is responsible for performing the item or making it happen, including specific allocations of responsibilities in multi-defendant and multi-plaintiff cases.

• Identify when the performance is going to occur, including specific time frames to avoid uncertainty and avoiding the subjective "ASAP."

• Identify specific penalties if the performance deadline or agreed specifications are not met.

Release of claims

• Identify who is being released. If the agreement is intended to be binding on the heirs and assigns of the parties or releasees, include that information.

• Identify the specific claims released – from what are the releasees being released?

• Consider negotiating and including specific claims *not* to be released by the agreement.

• Identify whether a Civil Code section 1542 general release of all known and unknown claims is appropriate or inappropriate for each case.

• Identify whether the specific and general releases are mutual and consider whether a mutual release is truly appropriate in each case.

• Include any indemnification or "hold harmless" provisions, identifying who will be responsible for future claims brought by third parties.

• Consider and identify any other third-party issues to be negotiated, including assignment of claims against third parties.

Not-so-general "general" provisions for negotiations

Some of these provisions are often overlooked by counsel and parties on both sides without much consideration for the key role these issues could play in the settlement outcome. Counsel should discuss each of these issues with clients before and during the mediation:

• Identify who is paying for each party's attorneys' fees. Settlement agreements which are silent as to costs and fees do not create a bar to either a cost bill or a motion for attorney's fees. (*Folsom v. Butte County Assn. of Governments* (1982) 32 Cal.3d 668, 671.) Fees and costs can be valuable leverage.

• Consider the practicality, ethicality and enforceability of including a confidentiality clause before agreeing to include such a provision which may be held unenforceable.

• Consider the enforceability and potential ramifications to your clients of a non-disparagement clause and include specific enforcement procedures if such a provision is included.

• A no-fault provision indicating the agreement is not an admission of liability or fault is likely to be included in any compromised agreement. Prepare your client ahead of time to help minimize their surprise and anger that can derail a fair settlement.

• Where multiple claims have been negotiated, identify whether one claim's settlement is conditioned on another claim settling. Consider any other conditions which may affect settlement.

• Identify the timing of filing any dismissals. (See, California Rule of Court 3.1385.)

• Include a provision evidencing all parties' voluntary and informed consent, including an agreement that each party has performed their own investigation of the facts, has fully disclosed all known material facts and has consulted with in-

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dependent counsel. (See, *Levy v. Superior Court* (1995) 10 Cal.4th 578, 583; Civ. Code, §1565.)

• If settlement is based on representations by one party which have not been independently verified, either condition the settlement on proof of the facts relied on and/or include a warranty by the party making the representations and a severe remedy for breach of the warranty.

• Consider including an attorney's fees provision for an action to enforce the agreement (*e.g.*, parties to bear their own fees/costs or prevailing party to have fees paid by the other party).

True general provisions

The following provisions are truly "general" as they are typically not subject to negotiation but are important to include in most, if not all, settlements to increase certainty as well as enforceability:

• If settlement is the result of mediation, a limited waiver of the mediation confidentiality privilege is required, including the parties' intention that the written agreement is to be binding, enforceable and admissible once fully signed. (See Evid. Code, §1123; *Fair v. Bakhtiari* (2006) 40 Cal.4th 189, 199-200). A clear statement of the parties' intention to be bound by the agreement is advisable even in non-mediated agreements.

• For pending litigation, do not forget the very important provision continuing the court's jurisdiction for settlement enforcement under Code of Civil Procedure section 664.6.

Include a "good faith settlement" provision if settling with one of multiple defendants (Code Civ. Proc., § 877.6).

• If the settlement agreement document constitutes the entire agreement of the parties and supersedes oral agreements and any prior written agreements, include that information. Otherwise identify any additional documents, which taken together, constitute the full agreement of the parties.

• Include a provision requiring the cooperation of all parties in implementing the agreement. If documents are to be signed at a later date, consider including a provision allowing the court to appoint a signer in the absence of the party's cooperation.

• Include a provision allowing severability of invalid clauses, keeping the remaining valid clauses enforceable.

• Include specific provisions for modifying the agreement in the future.

• Include a governing law provision but keep in mind that only parties to certain contracts may agree that California law will govern if performance is not to take place in California (Civ. Code, §1646).

• Define the effective date of the agreement (*e.g.*, Date of signing by the last party to do so).

• If the settlement agreement is the result of true negotiations, consider a provision stating the parties' intention that in the event of a dispute, each contract provision will be interpreted fairly and not strictly for or against any party. (See, Civ. Code, §1654.)

• Include the statutory time for consideration and revocation in settlements including a waiver or release of an employee's claim under the Age Discrimination in Employment Act (29 U.S.C. § 626(f)).

• Include dispute resolution mechanisms to prevent future litigation in case of uncertainties, including multi-tiered procedures including mediation and/or arbitration.

• Include a provision allowing execution of the contract in counterparts or by fax, if needed. If all signatories are at the mediation, this provision is unnecessary.

Signing the written agreement

An agreement to be enforced under Code of Civil Procedure section 664.6 must be in writing and must be signed by the parties. There are exceptions to the writing requirement (see, Evid. Code, §§ 250 and 1118; *Marriage of Assemi* (1994) 7 Cal.4th 896, 909; *City of Fresno v. Maroot* (1987) 189 Cal.App.3d 755, 761), but counsel should err on the side of caution. Put any agreement in writing as soon as possible to avoid the difficulties of proving the terms of an unwritten agreement or trying to fit your situation into one of the narrow exceptions. All "material terms" are more likely to be included in a predrafted comprehensive settlement agreement rather than an abbreviated term sheet.

To be enforceable under Code of Civil Procedure section 664.6, the written agreement must also be signed by the party seeking to enforce the agreement as well as the party against whom enforcement is sought. Counsel or other agent's signatures are not a sufficient replacement for the client's signature in settlement agreements. "The litigants' *direct participation* tends to ensure that the settlement is the result of their mature reflection and deliberate assent. This protects the parties against hasty and improvident settlement agreements by impressing upon them the seriousness and finality of the decision to settle, and minimizes the possibility of conflicting interpretations of the settlement." (*Levy v. Superior Court (Golant)* (1995) 10 Cal.4th 578, 585.) (Emphasis added).

If third parties are to be bound by certain or all of the provisions of the settlement agreement, have the third parties sign the agreement or a separate agreement incorporated into the settlement agreement. Alternatively, include a clear indemnification or other appropriate provision to ensure protection or an avenue of recourse if the third party does not act pursuant to the agreement.

Requirements for a verbal agreement made at mediation

If the parties enter into an oral agreement at mediation, in order to be enforceable under Code of Civil Procedure section 664.6 and Evidence Code section 1118 it must:

• Be recorded (tape recording or court reporter);

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• Include a recitation of the terms of the agreement evidencing a "meeting of the minds has occurred on the material terms." (*Weddington Productions, Inc. v. Flick* (1998) 60 Cal.App.4th 793, 797);

• Include the parties' verbal consent on the record;

• Include the parties' express consent that the agreement is to be binding and enforceable; and

• Be put into a signed writing within 72 hours.

Requirements for written "term sheets" prepared at mediation

Term sheets may seem more convenient at the time settlement is reached, particularly when it is late in the day and everyone is eager to leave. But "[i]f no meeting of the minds has occurred on the material terms of a contract, basic contract law provides that no contract formation has occurred. If no contract formation has occurred, there is no settlement agreement to enforce." (*Weddington Productions, Inc. v. Flick* (1998) 60 Cal.App.4th 793, 797.)

Moreover, the California Supreme Court recently noted: "The aim of [Evid. Code, § 1123(b)] is to allow parties in mediation to draft enforceable agreements without requiring the use of a formulaic phrase. However, the writing must make clear that it reflects an agreement and is not simply a memorandum of terms for inclusion in a future agreement. The writing need not be in finished form to be admissible under section 1123(b), but it must be signed by the parties and include a direct statement to the effect that it is enforceable or binding." (*Fair v. Bakhtiari* (2006) 40 Cal.4th 189, 192.)

Therefore, if the parties prepare a written memorandum at the mediation, in order to be enforceable under Code of Civil Procedure section 664.6 as an exception to the mediation confidentiality protections pursuant to Evidence Code section 1123, it must:

• Include the material terms of the agreement. (See, *Weddington Productions, Inc. v. Flick* (1998) 60 Cal.App.4th 793, 797);

• Include a "direct statement to the effect that it is enforceable or binding" or subject to disclosure (*Fair v. Bakhtiari* (2006) 40 Cal.4th 189, 192; Evid. Code, §1123);

• Include a provision in the written document (or a separate written agreement) providing that the court retains jurisdiction to enforce the settlement agreement under Code of Civil Procedure section 664.6; and

• Include the signatures of the parties themselves evidencing their intention to be bound to the terms of the document. (*Levy v. Superior Court (Golant)* (1995) 10 Cal.4th 578, 585.)

Enforcing the settlement

A motion to enforce settlement or motion for judgment may be needed where another party seeks to back out of an agreement or simply fails to comply with the terms of the agreement. Settlement agreement enforcement is primarily governed by Code of Civil Procedure section 664.6, which provides a "summary, expedited procedure to enforce settlement agreements when certain requirements that decrease the likelihood of misunderstandings are met." (*Levy v. Superior Court* (1995) 10 Cal.4th 578, 585.)

This remedy is *only* available to:

• Parties engaged in pending litigation (not pre-litigation settlements);

• Parties who have expressly agreed to have the court retain jurisdiction to enforce their settlement; and

• Settlement agreements which are in writing (or comply with Evid. Code, §1118) and which are signed by the parties themselves.

Although Code of Civil Procedure section 664.6 provides the most efficient method of enforcing settlement in a pending lawsuit, there are other formal options for enforcing settlement that do not have the same strict requirements and which were the only options available prior to the enactment of Code of Civil Procedure section 664.6 in 1981. Those options (including amending the pleadings to include the settlement as an affirmative defense or claim and then moving for summary judgment or filing a separate breach of contract action) were considered inadequate prior to 1981, with uncertain procedures and even more uncertain results.

Code of Civil Procedure section 664.6 is not an available remedy to enforce a pre-litigation settlement. In such cases, a breach of contract action may be needed to enforce a settlement or the settlement can be pleaded as a claim or defense once the case is filed.

Overturning the settlement

While it is possible to overturn a settlement agreement by filing a motion for relief from settlement under the excusable mistake, neglect or surprise provisions of Code of Civil Procedure section 473, it is unlikely "in the absence of a showing of fraud or undue influence…" (*Folsom v. Butte County Association of Governments* (1982) 32 Cal.3d 668, 677). This is due to California's strong public policy of encouraging voluntary settlements. (See, *e.g.*, *Osumi v. Sutton* (2007) 151 Cal.App.4th 1355, 1359; *Tower Acton Holdings, LLC v. Los Angeles County Waterworks* (2002) 105 Cal.App.4th 590, 602.)

Additionally, "The trial court's factual findings on a motion to enforce a settlement pursuant to Section 664.6 'are subject to limited appellate review and will not be disturbed if supported by substantial evidence.'[citation omitted]." (*Osumi v. Sutton* (2007) 151 Cal.App.4th at 1360.)

Nevertheless, settlement agreements which contain provisions in violation of the law or public policy will not be endorsed or enforced by the court regardless of whether there was a meeting of the minds and regardless of the public policy in favor settlements. (See, *Timney*

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v. Lin (2006) 106 Cal.App.4th 1121, 1127.)

Doing it right the first time

Counsel can minimize the likelihood of enforcement challenges to settlement agreements by taking the time to prepare in advance. Counsel should always:

- Prepare a draft settlement agreement before each mediation.
- Discuss each provision with clients to increase their understanding, ensure their voluntary and informed consent with all terms and to determine valuable negotiation items.
- Refer often to the draft agreement as a checklist of negotiable provisions during negotiations.
- Re-check your list of enforcement requirements before the agreement is signed and before everyone leaves the mediation.

The additional time spent *after* mediation trying to re-negotiate or enforce a vague or incomplete agreement is unnecessary when planned for in advance. Barbri's advertising slogan applies equally to the bar exam as it does to crafting settlement agreements: "Do it once. Do it right. Never do it again."

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