

Outside Counsel

Expert Analysis

A Best Practices Primer For Drafting Settlement Agreements

Most cases settle. A trial lawyer's last act, therefore, often is preparing a settlement agreement. While a settlement agreement is not always necessary (sometimes making payment, exchanging releases and filing a voluntary dismissal suffice), it remains the norm. So, a well-crafted settlement agreement should be in every litigator's toolbox. Nonetheless, we have all received from opposing counsel a proposed agreement that is inadequate. And there are countless cases where a settlement agreement itself becomes the basis for a lawsuit, resulting in the parties' litigating over an agreement that had "settled" their dispute.

Although drafting a settlement agreement should be standard fare for every litigator, a "checklist" of terms doesn't cut it. For every case, one needs to think through the provisions to be set forth. A suggested "best practices" approach for a straightforward commercial case is described below.¹

Remember the Basics

A settlement agreement, like any contract, should be about the performance of mutually agreed upon terms. Before drafting, ask: What are the basic "deal terms" of the settlement? How do I best ensure performance of the terms? And how do I best protect my client if performance issues arise? The objective is twofold: accomplish certainty of the resolution by carefully spelling out

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what needs to be done, while also preparing for uncertainties if the steps to resolution hit a roadblock. As a consequence, while both lawyer and client want the settlement agreement to be "the end," it is necessary to consider "next steps" should enforcement of the bargain become an issue.

As with most legal writing, use clear language. Excessive "legalese" is difficult to penetrate and can obfuscate the parties' intent. Some provisions, such as releases, tend toward formalistic terminology, but mainly the agreement should use straightforward language that a non-lawyer can readily understand and apply. Your client, and particularly the business people at a corporate client, should be comfortable with the language.

The provisions often fall into two camps. First, there are the terms specific to this deal. What is the basic consideration for resolution, and how is it to be exchanged? Are there other negotiated promises to the deal? Indeed, myriad terms can become important for reaching peace in any given context. (For example, in a contract case, there might be terms involving other business dealings among the parties; in an employment case, a job reference for the former employee might be an issue; or in a business

tort case, there can be provisions related to future competitive practices). Are there limitations on the scope of the releases? Are there any concerns or carve-outs relating to dismissal of the litigation? What about the parties' relationship—do they still expect to do business together, or are they entirely antagonistic? The particulars of the deal terms come from the specific circumstances of the lawsuit being resolved.

Second, there are the "procedural," "usual and customary" or "boilerplate" terms. Some are addressed below. Most litigators have their standard list. But solid draftsmanship should tailor these terms to the settlement at hand. At times, the "usual and customary" terms can create unanticipated issues when performance problems arise. Understand their purpose, and avoid using them haphazardly.

Common Provisions

A typical agreement will have: (i) an introduction (useful for defining the parties and adopting short-forms); (ii) recitals (sometimes followed by "definitions"); (iii) the key deal terms (such as consideration/payment, releases, dismissal); and (iv) the procedural and usual/customary terms. Good draftsmanship should consider the following issues for some of the common provisions.

Recitals. A settlement agreement typically includes recitals. They help to frame the settlement. "Whereas, so-and-so entered into a contract, a dispute arose over the contract, one of the parties sued..." etc. Recitals may prove useful in informing the parties' intent if disputes arise over specific

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terms or their performance. In drafting recitals, think about how you would explain the settlement in court in the event of a dispute over the agreement—this would be the core information setting the stage for the terms to follow. You want to include what is necessary for this purpose, without overdoing it. Although recitals are not essential, using them generally makes sense.

Payment/Consideration Terms. The provisions for exchanging consideration are sometimes very simple—“X agrees to pay \$1,000 to Y upon execution and delivery of this agreement”—but often detailed provisions are necessary. In the simpler scenario, payment is made “on the spot”—for example, one side pays the full amount upon delivery of the executed agreement, and the other side gives a release and commits to dismiss the lawsuit. The deal is done. Drafting can be straightforward.

But many settlements involve payments over time, or “installment” payments. In this scenario, the party to be paid does not want to give a release and dismiss the lawsuit before receiving full payment, which might be years away. The common way to handle the installment-payment settlement in New York is to require a confession of judgment through an affidavit from the party making payment.²

By an affidavit confessing to judgment, a party admits to liability on a debt or obligation, such as the total amount due in installments under a settlement agreement. If the paying party defaults, the affidavit can be filed in the clerk’s office for the county of the affiant’s residence (or for a non-resident, in a county where the affiant authorized entry) to obtain a judgment by confession. (Often the affidavit is referred to as a “confession of judgment”). Thus, the agreement should require the party making payment to give an affidavit for a confession of judgment; the affidavit should be an exhibit to the agreement; and the affidavit itself should be executed with the agreement, to be held in escrow (under the agreement) by the other party during the payment period. The party holding the affidavit files it if there is a default, and the clerk is authorized by statute to enter judgment for the amount confessed. That judgment then may be enforced like any judgment issued in an

action in New York State Supreme Court.³

What if the payor defaults after making some, but not all, of the payments? By the New York statute, execution on a confessed judgment can only be for the amount then due.⁴ Again, best practice is to spell this out in the documents: if there is a default, the creditor-party holding the affidavit is entitled only to judgment for the unpaid balance, with the payments made being credited against the debt. Additionally, the agreement should require that, in conjunction with filing the debtor’s affidavit, the creditor or its counsel must file its own affidavit attesting to the default and the amount still owed. (Likewise, the affidavit for the confession of judgment should condition its filing on the creditor’s separate affidavit). In other words, the payee should only be able to obtain a judgment on confession by proving the settlement default.

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Where the case is settled with payments over time, it is also sound practice (at least for the paying party) to include a provision requiring the creditor to give the payor notice and an opportunity to cure the default. Likewise, the creditor’s affidavit for enforcing the confession should have to attest to compliance with this notice/cure provision. This gives some leeway if a default arises.

Both sides should carefully review the statutory requirements for a confession of judgment when going that route. For example, in addition to stating the sum for which judgment may be entered and the county for entry, a confession for an amount to become due (such as per an installments settlement) must concisely state the facts out of which the debt arose and show that the sum confessed is properly to become due. Reciting the settlement obligation as the debt being confessed is typical. A failure to describe the

basis for the confessed debt in the affidavit might present a problem if the need arises to obtain a confession judgment. Furthermore, entry of judgment is authorized under the statute only within three years after execution of the affidavit confessing to judgment; for a settlement payout covering a longer period, additional security arrangements might be necessary.

The payee might also want the confession of judgment to be greater than the full settlement amount. The concern is that the debtor could decide to renege on the late-stage payments, hoping that the payee might not go to the expense or bother to file for a confession of judgment when only a small amount is outstanding. An obligation beyond the full amount due under the settlement is a disincentive to this gamesmanship.

Sometimes parties settle even after the plaintiff has won a money judgment. The plaintiff might conclude that the judgment will not be fully collectible, that prevailing on appeal will be problematic, or that it makes sense to compromise to end the litigation. In these situations, the judgment-debtor should make sure that the settlement agreement requires the plaintiff to file a satisfaction of judgment (known as a “satisfaction-piece” in state practice) upon payment of the settlement amount.⁵ Sometimes that obvious provision is omitted, even though a satisfaction is necessary to remove a judgment as a lien on record.

Where a plaintiff holds a judgment, can the parties still structure a settlement on installment payments? The judgment-debtor might be unable to pay the judgment, and the judgment-creditor—realizing that collection proceedings will be unproductive—agrees to settle for payments over time. However, in this scenario, the judgment-debtor wants the judgment to be extinguished as a lien “on the books,” while the judgment-creditor is, understandably, reluctant to give up the judgment. Again, properly crafted provisions in the agreement, with the confession-of-judgment approach, can solve this standoff. The judgment-debtor can give the affidavit for a confession judgment, and the judgment-creditor then can agree to file a satisfaction of judgment to extinguish the existing judgment. This structure, in effect, substitutes the confession of

judgment for the filed judgment. It avoids the more cumbersome approach of requiring periodic filings of partial satisfactions of judgment and can enable parties to reach a payout-over-time resolution even where the creditor holds a judgment.

Releases and Dismissal. The release is a key provision. A basic question will be between a general or specific release. Do the parties want to extinguish (i) the claims arising from the lawsuit only; (ii) any and all claims that exist, or might exist, between them generally, going beyond the lawsuit's assertions; or perhaps (iii) a "hybrid" or carve-out of claims from litigation and related matters but not the full-blown general release of "everything in the world that might exist"? Where the lawsuit involves a single transaction between one plaintiff and one defendant, settling with general releases is often preferred. But if the parties have had various dealings over time, or if the case involves multiple parties, more defined releases might be appropriate.

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Again, careful attention to the litigants' relationships, their past interactions, any connections to other parties or lawsuits, and other circumstances in a particular case is significant for the scope of a release. Reciprocal releases—releases with mirror-image language—are the norm, although some circumstances might produce settlement without exact congruence. Remember to include appropriate language (particularly where the releases are general) to preserve obligations under the settlement agreement itself. (For example: "...except

that this Release shall not release, relieve or discharge X from the obligations provided for by this Agreement.")

The agreement should provide for dismissal (usually "with prejudice," but a "without prejudice" dismissal might be warranted where, for example, the parties agree that a claim is revived upon failure of a condition); and it should refer to the appropriate dismissal document (usually a stipulation but sometimes a notice) to be signed by the parties or the plaintiff, and then filed with the court.⁶

Attention must be given to the statutory or rule requirements for voluntary dismissal, whether by stipulation, notice or on court order. I prefer (i) to reference and attach the dismissal document as an exhibit to the agreement; and (ii) to have the document executed as a standalone instrument from the exhibit version and delivered with the executed settlement agreement, so that filing for dismissal can be accomplished promptly.

Confidentiality. Typically, there is no reason for the terms resolving a business dispute among private parties to be aired publicly, so a confidentiality provision is common. But carve-outs are usually necessary—a party will need or want to disclose the settlement to its accountant, financial/tax advisor, attorneys, and others with a need to know to render professional services. Also, the fact of the settlement, as distinct from terms, is something that parties often do not want (and likely cannot keep) confidential, so frequently that is spelled out as well. The agreement also should provide that confidentiality is not required if a party must enforce the agreement.

No Admission of Wrongdoing and Non-Disparagement. To promote resolution of litigation, settlement offers, negotiations and related matters are generally inadmissible,⁷ but it remains good practice to specify that neither side admits to wrongdoing or liability by settling and that the settlement cannot be used against a party. Relatedly, and especially when the parties' dealings have been highly contentious, a provision forbidding negative statements about the other side might be appropriate. But draft a non-disparagement obligation with specificity,

because too-loose non-disparagement language can be fertile grounds for alleging breach in a new lawsuit.

Forum Selection. Settlement agreements frequently state a jurisdiction for litigating disputes involving the agreement. For a settlement involving New York City parties or a lawsuit here, it is common to specify "the Supreme Court of the State of New York, County of New York, or in the event that federal court subject matter jurisdiction exists, the U.S. District Court for the Southern District of New York." But avoid one common drafting misstep: There is a distinction between mandatory and permissive forum selection. If you want a particular jurisdiction to be the only available forum, the provision should designate it as the exclusive forum (and that the parties consent to personal jurisdiction there) for bringing an action under the agreement. Otherwise, the language might support only permissive jurisdiction, leading to litigation over the appropriate forum.

Conclusion

In the world of commercial litigation, most lawyers will prepare far more settlement agreements than jury summations. Every settlement is unique, but common drafting issues exist. Focus on the specific "deal terms" of the settlement, spell them out clearly, and steer clear of often overlooked pitfalls—and your settlement agreement is more likely to do the trick.



1. This article discusses some basics in settling business litigation among commercial parties. Numerous kinds of cases, such as class actions, shareholder derivative lawsuits and government enforcement proceedings, typically require court approval for settlement. These cases, as well as more complicated commercial disputes and securities fraud cases, often involve multiple parties and may require complex settlement arrangements, implicating issues concerning non-settling parties and insurance coverage. These more complex settlement matters are beyond the scope of this article.

2. C.P.L.R. §3218(a).

3. *Id.*, §3218(b).

4. *Id.*, §3218(c).

5. *Id.*, §5020.

6. Fed. R. Civ. Pro. 41; C.P.L.R. 3217.

7. Fed. R. Evid. 408; C.P.L.R. §4547.v