

DENTONS

Drafting Effective Settlement Agreements

Speakers:

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Grow | Protect | Operate | Finance

Overview

1. Background – *Newbury v Sun Microsystems*
2. Why have settlement agreements?
3. Key terms in settlement agreements
4. Types of settlement offers
5. Ways to bring an end to legal proceedings
6. Tomlin Orders
7. Settlement agreements in employment relationships
8. Litigation after settlement
9. DOs and DON'Ts
10. Questions

Background – *Newbury v Sun Microsystems*

- Newbury, the Claimant, claimed unpaid commission from Sun Microsystems, the Defendant
- Company counterclaimed for recovery of an alleged overpayment
- 3 June 2013
 - Shortly before the trial, Newbury's solicitors wrote to the Company's solicitors



Background – *Newbury v Sun Microsystems*

Offer (Company's solicitors):

"To reach a compromise between the parties, our client has agreed to make a further offer of settlement to the Claimant ...

Our client is willing to settle the entire proceedings by paying the Claimant within 14 days of accepting this offer the sum of £601,464.98 (the "Settlement Sum") inclusive of interest by way of damages ... in full and final settlement of the Claim and counterclaim plus the sum of £180,000 in relation to his legal costs such settlement to be recorded in a suitably worded agreement.

This offer is open for acceptance until 5pm this evening after which it will be automatically withdrawn without further notice to you."

Background – *Newbury v Sun Microsystems*

Acceptance (Newbury's solicitors):

"We are instructed that the Claimant accepts the terms of your client's offer, being payment of the Settlement Sum of £601,464.98 plus £180,000.00 in relation to his legal costs.

We will forward a draft agreement for your approval on Tuesday 4 June."



Background – *Newbury v Sun Microsystems*

Subsequent events:

Newbury's solicitors sent a draft Tomlin Order to the Company's solicitors.

The Company's solicitor amended the draft order and referred to the claim being stayed on the terms set out in a separate waiver deed.

Draft waiver deed contained additional provisions:
confidentiality obligations, payment to be made within 14 days of the agreement, etc.

Issue: whether the letters of 3 June 2013 gave rise to a binding contract?

Essential to determine whether a binding agreement had been reached on the terms set out in the original offer letter and whether conduct after 3 June 2013 (e.g. the waiver deed) are admissible

Background – *Newbury v Sun Microsystems*

Outcome:

- Binding settlement agreement was **reached via the offer and acceptance** on 3 June 2013
 - no other terms could be added afterwards
- Reference to a "suitably worded agreement" was reference back to the terms set out in the offer, but **not to additional terms still to be negotiated or agreed**

Lesson:

- Importance of the words **"subject to contract"**
- To be used where
 - terms are not yet binding, or
 - not yet agreed until a formal contract is signed



Re MSB International Ltd [2023] 1 HKLRD 386

- Series of without prejudice written offers and counter-offers
- No good explanation had been given as to the absence of the words “subject to contract”
- Held:
 - Settlement upon acceptance of the final offer
 - The settlement was not subject to conditions
 - The fact that parties did not reach agreement on all the terms did not render the agreement uncertain or incomplete

Why have settlement agreements?

- Protect your own interests
- Ensure that your desired terms are included
- Reduce the risks of future disputes
- Record all essential terms **fully** and **clearly**

Practical tips (when writing a letter containing a settlement offer)

- Consider marking it “**subject to contract**”
 - Give yourself an opportunity to insert additional terms
 - Enable subsequent negotiations
- Can you make the payment on the date stipulated?



Key terms in settlement agreements

1. Without admission of liability
2. Full and final settlement
3. Costs and interest
4. Payment mechanism
5. Time is of the essence
6. Acceleration
7. Release
8. Indemnity
9. Mechanism to end proceedings
10. Confidentiality





Key terms in settlement agreements

1. Without admission of liability

- Settlement agreement generally not protected by “without prejudice”
 - Important to have a **confidentiality clause**
- State that the settlement is on an entirely **without admission of liability basis**

Key terms in settlement agreements

2. Full and final settlement

- A creditor cannot seek the balance of the debt if it chooses to settle for less
- Exception: the party was induced by fraudulent misrepresentation
- *Hayward v Zurich Insurance Company plc* [2016] UKSC 48
- There was deliberate exaggeration and the settlement agreement was set aside



Key terms in settlement agreements

3. Inclusive of costs and interest

- Interest on the amount in dispute
- Court allows cost-only proceedings if the issue of costs cannot be resolved
- Include this term to avoid disputes in relation to the issue of costs / separate costs proceedings



Key terms in settlement agreements

4. Payment mechanism

- In cleared funds
- Without set off or deductions
- Specify the currency
- Date and time in the particular place in which payment shall be received
- Also consider:
 - Payment to be made by solicitors' cheque
 - Payment by instalments



Key terms in settlement agreements

5. Time is of the essence clause

- Failure to adhere to deadline → **material breach of the contract**
- Repudiation → a party is allowed to terminate the contract
- Otherwise, default in making payment generally a **non-material breach**





Key terms in settlement agreements

6. Acceleration clause

- Instalment payment plan in place but default in payment
- Acceleration clause → in case of default, can accelerate all future payments
- Not an unenforceable penalty
 - *ZCCM Investments Holdings plc v Konkola Copper Mines plc* [2017] EWHC 3288 (Comm)

Key terms in settlement agreements

7. Release

- Scope of release needs to be carefully negotiated, clearly and carefully worded
- What a claimant wants?
 - Will not want to relinquish future rights regarding other claims that might arise against the same defendant
- What a defendant wants?
 - Widest possible release to cover all present and future claims, whether known and unknown to claimants, at the time of entering into the settlement
 - “irrevocably and unconditionally waive, release and discharge”
- Express words necessary to release unknown or fraud-based claims
- Mutual release

Key terms in settlement agreements

7. Release (continued)

- **General rule:** the release relates only to the subject matter of the settlement and not something else
- In *Satyam Computer Systems v Unpaid Systems*, release of claims re Service Agreement did not bar claims arising out of separate agreement
- In the absence of **express indication**, parties could not release rights to claim something that they were unaware of, and could not have been aware of at the time of entering into the settlement agreement
- Example of express indication

*“For the avoidance of doubt this applies to any past, present or future claims, actions, liabilities, costs or demands, **regardless of whether or not the Claimant is aware of them at the date of this agreement.**”*

- Also consider including the Claimant’s successors and assigns, staff and employees and associated companies

Key terms in settlement agreements

7. Release (continued)

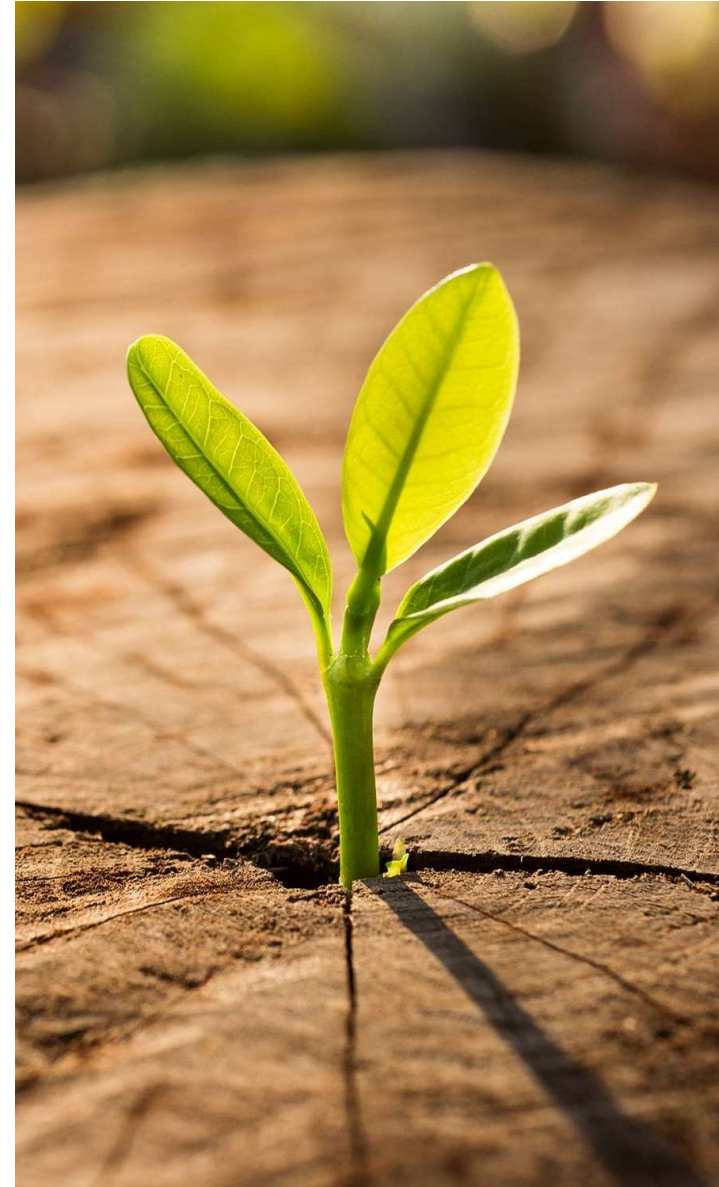
Bank of Credit and Commerce International v Ali

- Employee made redundant signed release in exchange for one month's additional salary
- One year later, bank went into liquidation
- Liquidators uncovered evidence of widespread corruption and dishonest practices at the bank
- Employee could not find another job because of stigma and brought claim against bank in liquidation
- Held: Court would be "slow to infer that a party intended to surrender rights and claims of which he was unaware and could not have been aware of at the time of signing."

Key terms in settlement agreements

8. Indemnity

- **General rule:** release of one concurrent tortfeasor does not have the effect in law of releasing another concurrent tortfeasor
- Important in professional liability claims involving multiple advisors
- For examples:
 - Settlement Agreement between A and B will not affect A's right against C
 - If A subsequently sues C, C may seek contribution from B
 - B should consider obtaining an indemnity from A, against any liability to which B may become subject



Key terms in settlement agreements

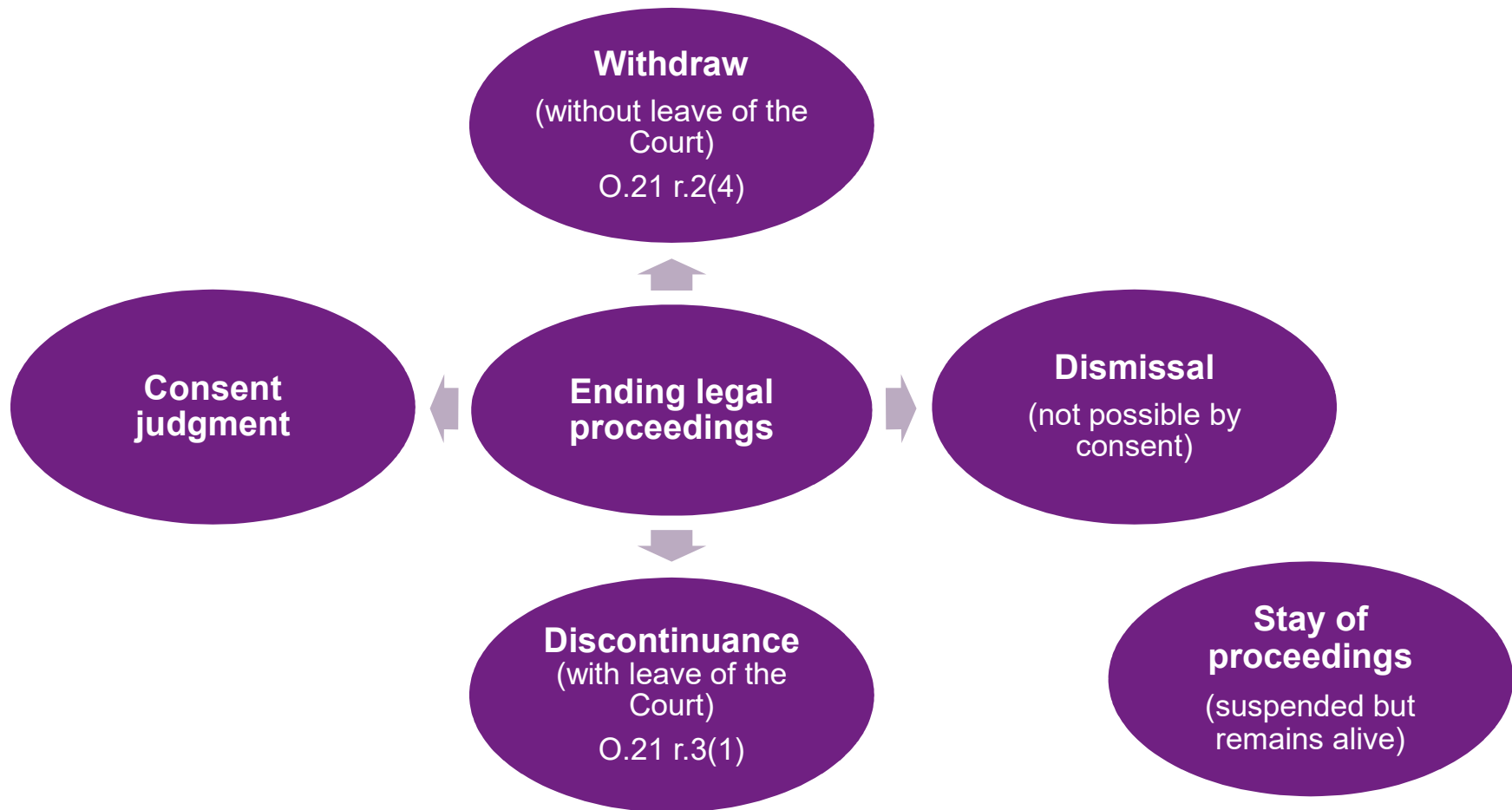
9. Mechanism to end proceedings

Always include a clause that stipulates

1. When parties must take steps to bring an end to legal proceedings
2. Who will do it
3. Who will bear the cost (e.g. negotiation, preparation and execution of settlement agreement)
4. Annex a form of the consent order / consent summons



Ways to bring an end to legal proceedings



Key terms in settlement agreements

10. Confidentiality

- One of the most important terms; sometimes known as a “gagging clause”
- May be extended to include covenants not to file complaints with regulators and professional bodies
- Parties may nevertheless be obliged to report
 - SFC Licensing Handbook and rolling bad apples
 - SFC Code of Conduct for Licensed Persons (para 12.5)
- Whistleblowers and public interest disclosures
- Remedies for breach of confidentiality obligations
 - Depends on whether it is a condition of the agreement or innominate term
 - Duchy Farm Kennels v Steels
- US: agreeing to a confidentiality clause any render settlement payment taxable

Key terms in settlement agreements

11. Third party rights

- Consider whether to exclude the operation of the Contracts (Rights of Third Parties) Ordinance
- Describe the third parties as clearly as possible

12. Non-disparagement

13. Law and jurisdiction

- Governing law and jurisdiction

14. Annex sample documents

- Pre-negotiates the wording of consent orders or personal guarantees

15. Standard boiler plates

- Amendment clause, assignment clause, tax provision, severability of invalid clause, etc.

Types of settlement offers

Sanctioned Offer and Sanctioned Payment

- Order 22 of RHC or RDC
- Alternatively, make an offer outside Order 22

Calderbank offer (without prejudice save as to costs)

Open offer (not subject to without prejudice privilege)

Types of settlement offers

1. Sanctioned Offer and Sanctioned Payment

- **General rule as to costs:** the unsuccessful party pays the costs of the winning party
- Specific costs consequences
- Incentivise parties to settle the claim
- Force the party to re-assess its merits and consider accepting the offer
- Consider making a sanctioned offer if settlement negotiations are unsuccessful
- Cannot include alternative costs provision
- Example

Receiving party does not accept the offer

Offering party manages to “do better” after trial under the judgment

Offering party may obtain significantly increased costs and interest on any amount awarded

Types of settlement offers

2. *Calderbank* offer (without prejudice save as to costs)

- Cannot be disclosed to the court during substantive court proceedings
- O.62 r.5(1)(d): the court will not take *Calderbank* offer into account in exercising its discretion as to costs if a party could have made a sanctioned offer or sanctioned payment
- When to make *Calderbank* offers?
 - D does not wish to pay the amount of the offer into court and have the amount tied up
 - Party wants to make an offer that is all-inclusive as to settlement and costs
 - Drop hands offer
 - D wants to offer to make payments in instalments
 - Subject matter of the settlement includes matters other than the payment of money

Types of settlement offers

3. Open offer

- Vs “without prejudice”
 - **Genuine aim** of settling the claim
 - What matters is the substance, not the form
- Open offer
 - Full details of the offer may be referred to in court
 - Useful when one party is being particularly unreasonable in settlement negotiations



Tomlin Orders

- Consent order – parties have agreed terms of settlement and orders that all further proceedings be stayed
- *"all further proceedings in this action be stayed upon terms agreed between the parties and set forth in the Schedule hereto, except for the purpose of carrying this order and the agreed terms into effect with liberty to the parties to apply for the said purpose"*
- Effect
 - Action is stayed
 - In case of breach of terms in the Schedule, the other party can apply for an order to enforce such terms
 - Terms in the Schedule does not form part of the order, but an agreement between parties
 - The Schedule is not part of the court order and is kept confidential

Settlement Agreements in an employment context

- Normally called a “separation and release agreement”, documenting parties’ agreement for a mutual separation and mutual release and waiver
- Usually involves employer paying additional *ex gratia* payment over and above the statutory and contractual payments owed in consideration for a full waiver of all claims
- *Ex gratia* payment can be held back pending compliance with settlement terms (or any post termination restrictive covenants) and return of employer’s property
- Cannot be used to waive underpayment of statutory and contractual benefits: see section 70 of the Employment Ordinance which provides “*any term of a contract of employment which purports to extinguish or reduce any right, benefit or protection conferred upon the employee by this Ordinance shall be void*”.
- However, note that section 70 will *not* apply to a valid settlement negotiated and entered into at the end of the employment relationship: See *Kao, Lee & Yip (A Firm) v Lau Wing & Or* [2007] HKCA 275 and *Dock Brian v Pacific Gourmet Holdings Ltd* [2022] HKCFI 444.
- Recommend the employer allow the employee adequate time and opportunity to take independent legal advice, to prevent the employee from later arguing the agreement is not enforceable on the grounds of undue influence and/or coercion

Litigation after settlement

- Litigation can arise from a settlement agreement like any other contract, particularly where the agreement is poorly drafted
- Normal rules of construction of contracts apply
- Can you litigate an issue that was not dealt with in the settlement but which should have been dealt with?
 - Abuse of process?

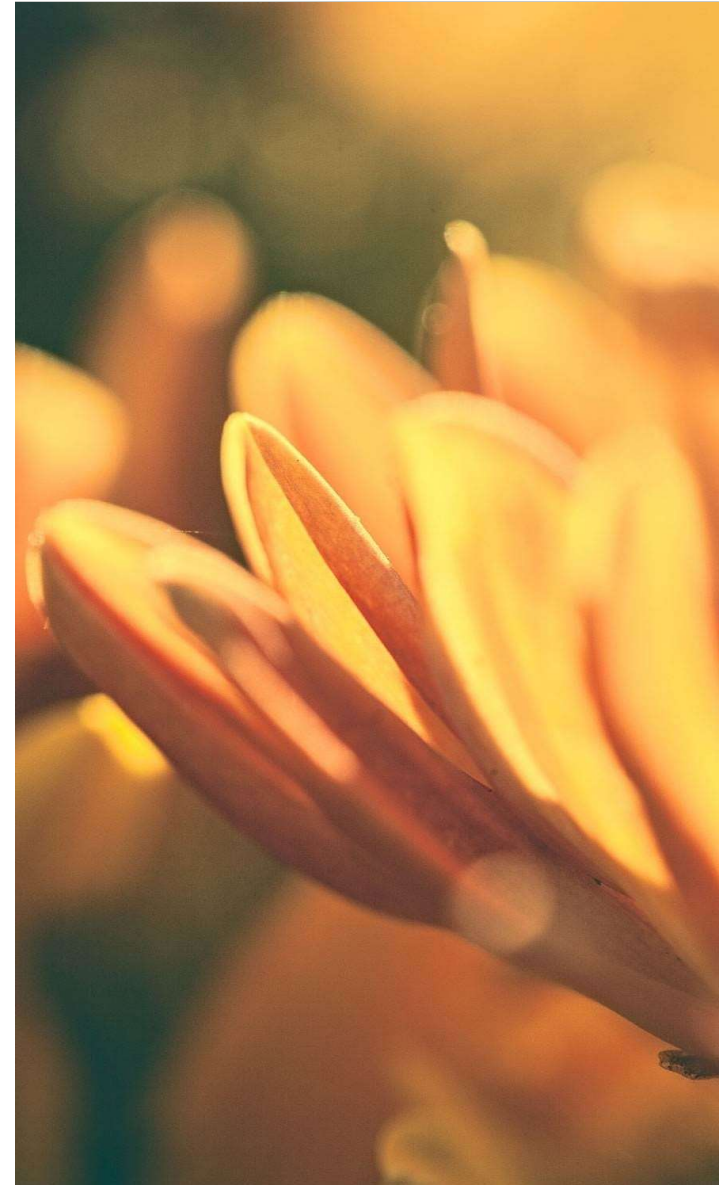
→ **Balancing exercise**



DOs and DON'Ts

DO

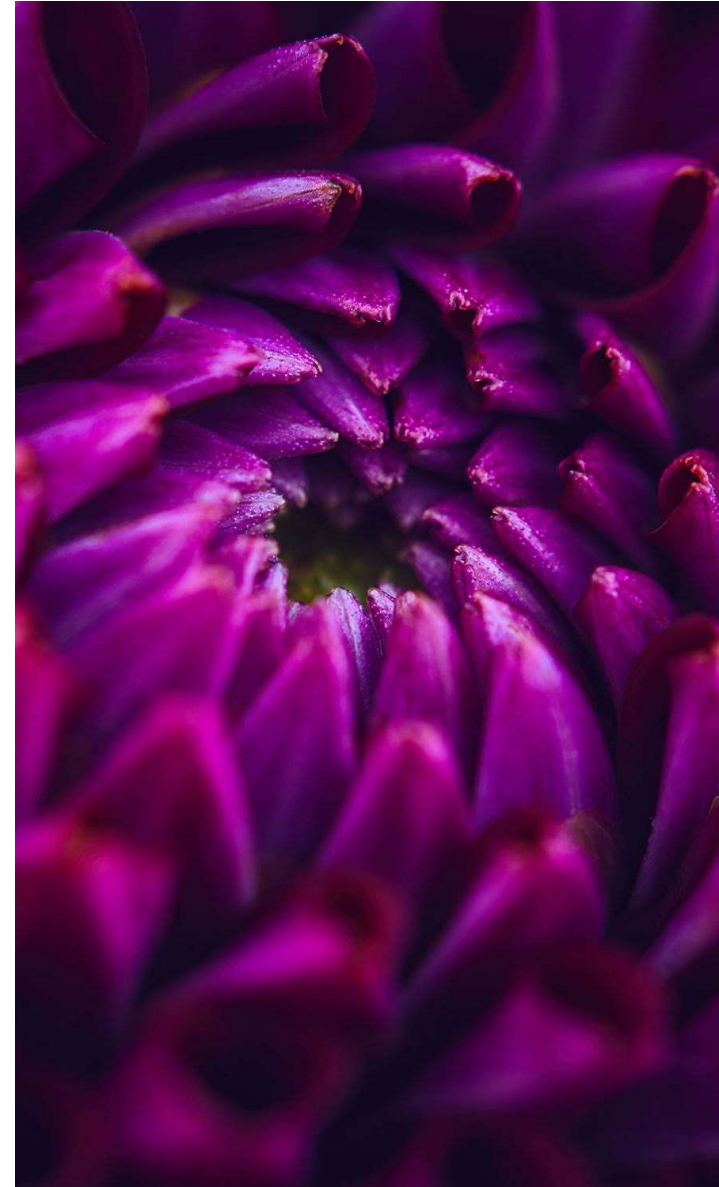
- mark correspondence “subject to contract”
- take a draft settlement agreement to a settlement meeting
- use “without prejudice” where appropriate
- agree template of any future documents in settlement agreement
- use sanctioned offers/payments and calderbank offers strategically
- use conditions/staggered payments to procure compliance with confidentiality/non-disparagement clauses



DOs and DON'Ts

DON'T

- leave terms to be agreed later
- forget to consider indemnities where there are joint tortfeasors
- assume all WP correspondence will be invisible to the court
- agree to do something if you can't do it



A microscopic image of plant cells, showing cell walls and internal structures, overlaid with a semi-transparent purple filter. The cells are arranged in a grid-like pattern, with some showing more detail than others.

Questions?

Poll Questions

Q1 What is your preferred time for webinar?

- In the morning (9am-12pm)
- During lunch (12pm-2pm)
- In the afternoon (2pm-6pm)
- After work (6pm-7pm)

Q2 What other webinar topics are you interested in?

- Privilege
- Consequential loss and liquidated damages
- Injunctions in the digital age
- Enforcement of judgments and arbitral awards
- Dawn raids and regulatory investigations

Coming up...

25 October

Topic: *Re Gatecoin* and the future of crypto currency under insolvency law

Speakers: David Kwok and Julian Ng

30 November

Topic: Handling employee termination

Speakers: Jenny Zhuang and Mandy Xu

DENTONS

Thank you!



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