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Don't forget critical eleventh-hour issues

By Jan Frankel Schau

It happens frequently. It is late, and the clouds seem to part in a hotly contested employment mediation. Settlement appears likely. But while the parties are elated at the prospect of settlement, they may overlook some critical issues in the rush to the finish. Here are a few common eleventh-hour issues to keep in mind.

Immigration. The parties cannot report violations of immigration status if the agreement requires confidentiality. An employer is not entitled to discovery on the issue of immigration in a Fair Employment and Housing Act case as a matter of public policy. Including such a threat in a settlement agreement likely will not be enforceable.

Noncompetes/no re-hire. Noncompete clauses are generally unenforceable as an unlawful restraint of trade. If the noncompete clause is too broad, it may defeat the entire settlement agreement as facially void. The parties also must use caution regarding "no re-hire" clauses. Most employers would not welcome back an employee who sues, but not all such provisions are enforceable.

Confidentiality. If you want to be able to enforce confidentiality provisions, usually the parties ask for a liquidated damages provision for each violation. The liquidated damages award is difficult to enforce and serves mainly as a psychological deterrent. The real risk in the event of a breach of confidentiality is the ultimate setting aside of the agreement itself. In one case, a settling party shared the news with his teenage daughter, who gloated about the 'win' on Facebook. An appellate court ruled the settlement was unenforceable because the post violated the confidentiality agreement. The lesson: be prepared to suggest specific language as to what may and may not be conveyed.

Taxes: employee. Document the allocation of the settlement in a way that is most likely to be enforceable and avoid challenge by the Internal Revenue Service. Most settlement proceeds in an employment case are taxable income to the employee. This includes back wages, front pay, emotional distress damages, interest and punitive damages. The only exceptions are payments for attorney fees and payments intended to compensate for damages "on account of personal physical injuries or physical sickness." Lawyers should expressly allocate the settlement proceeds among the various types of damages. As long as it is done at arm's length and in good faith, it is likely to be upheld.

Taxes: employer. Employers may be advised to protect themselves by demanding the inclusion of an indemnification provision in the settlement agreement, obligating the plaintiff to indemnify the employer if the IRS ever challenges the allocation. As a practical matter, individual plaintiffs rarely have the resources to defend the employer against the IRS if challenged, so this term may have little value. Unless the attorney fees are specifically allocated in a settlement agreement, the payments made in settlement of wage-based claims are generally considered wages required to be filed on a W-2. This means coming prepared to divulge just exactly what your fees will be and what costs you have in the case by the time the agreement is executed.

Enforceability of short-form agreements. Many parties are content signing the mediator's short-form agreement, hoping everyone will be bound until a longer form can be drafted. If the short form includes language to the effect that "a long form agreement will be signed hereafter," it may not be enforceable based upon the legal theory that it was merely executory. The magic words are: "This agreement is intended to be binding, enforceable, effective as of the date it is signed and final." If the short form is later superseded by a final agreement, no harm done. But if the final agreement bogs down over language or newly contemplated terms, the short-form agreement will serve to bind the parties. Even where a party claims the short form was not intended to be binding, the court may enforce it by judicial estoppel.

Enforcement: dismissed case: Be explicit about how the agreement gets enforced. It is common to include language to the effect that the settlement agreement may be enforced under CCP Section 664.6 and even to explicitly permit the confidentiality of the agreement to be waived for that purpose. But what happens after the case is dismissed — or if the settlement occurs pre-litigation and there is no pending case? You will not be able to bring a motion to enforce if there is no pending action. Section 664.6 only works if a settlement is reached while there is pending litigation. For that reason, if your payment is over an extended period of time, you will want to negotiate a stipulated judgment, or ask the court to retain jurisdiction until the final payment is made. In a pre-litigation matter, you will need to negotiate a "confession of judgment," which is a clumsy and time-intensive mechanism that is still difficult to enforce.

Enforcement: signing the settlement. A settlement generally can only be enforced if it is signed by the parties. Stipulation by counsel is unenforceable as is a signature by an agent or attorney of record. The exception is where the liability insurer is providing both defense and indemnity with no reservation of rights and adequate coverage. There, the defendant need not sign the agreement.

Enforcement: attorney fees. Enforcement provisions often include attorney fees for the prevailing party in any motion to enforce. This term, if not explicitly provided, is not automatically applied under construction of California contract law.

Arbitrator appointment. The parties may want to appoint the mediator as an arbitrator if any claim of breach of the agreement occurs. This is a term that both lawyers should consider carefully. Although a mediator may act as an arbitrator in the same matter she mediates, according to California Rules of Court, Rule 3.857, she must exercise caution in doing so and may only do so with the informed consent of the parties and in a manner consistent with all applicable laws. This means informing the parties of the consequences of revealing information during one process that might be used for decision-making in the other. It also requires a level of disclosure not required in mediation and may reveal the potential for conflict, which is not a concern in the mediation process.

Public policy. Often, a plaintiff's lawyer has already interviewed numerous employees in the same work place and has threatened to bring a class action or other representative action. As a matter of public policy, you cannot require that lawyer from refraining from doing so. Those employees have a right to be represented by whomever they choose. Be careful not to overreach by including such a term in your settlement agreement. At best, you can ask your mediator to inquire whether the plaintiff's counsel has been retained by any other employees and, if not, whether he intends to return to their workplace to pursue new claims by other employees. Usually, the lawyer will honestly reveal that either he has tried to get other employees to sign up or he has no such intention.

Malpractice. Finally, occasionally in the final moments of a settlement agreement, one of the attorneys will ask to include language that insulates the attorney from potential claims of malpractice against them. This violates the Rules of Professional Conduct, Rule 3-400, which prohibits an attorney from contracting with a client to limit the attorney's liability to the client for the attorney's professional malpractice. Don't even try.

This laundry list of eleventh-hour issues is critical because settlement agreements arising out of a mediation are difficult to set aside. All of us want to do our jobs diligently, so our clients have the advantage of having knowledgeable, experienced and reliable legal counsel as settlement documents are being drafted. Don't let yourself be caught unaware. Consider these critical terms in every employment mediation before the final handshake and both you and your clients will be well served.

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