

Term sheets and mediator proposals: not always enforceable, but valuable

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After a long, challenging day of mediation, the parties frequently reach agreement on the essential terms of a settlement. Eager to memorialize the deal, counsel draw up a term sheet, presuming it will be enforceable. That writing may indeed be enforceable if certain conditions are met, but enforceability is not guaranteed. It is important for parties to understand the potential limitations of a term sheet, which likely does not include all the provisions typically found in a long-form, comprehensive settlement agreement.

Sometimes, it may not be possible to finalize a term sheet at mediation because the parties have reached an impasse on critical terms. The parties may then ask the mediator for a proposal to resolve their differences. In either circumstance, whether agreeing to a term sheet or responding to a mediator proposal, parties need to understand exactly what their acceptance actually means.

This article addresses the California statutory rules and contract principles governing enforceability of agreements reached at mediation. We also discuss federal cases on this topic. Ultimately, we explain how a term sheet or mediator proposal can be a valuable tool in moving the parties to agreement, even if its ultimate enforceability is uncertain.

“Words to That Effect”

A term sheet prepared at mediation is not admissible or subject to disclosure unless parties have complied with California Evidence Code Section 1123, which is an exception to the general rule that bars disclosure of communications made during a mediation. Under sections 1123(a) and (b), a binding, enforceable, and admissible agreement is created when the settling parties have signed the agreement, and the agreement states that it is “admissible” or “subject to disclosure,” or “*words to that effect*,” or alternatively, the agreement provides that it is enforceable or binding, or “*words to that effect*.” While section 1123 allows parties to draft enforceable agreements with some flexibility, the California Supreme Court ruled in *Fair v. Bakhtiari* that including an arbitration clause among a list of settlement terms was not sufficient to manifest the parties’ intent to be bound. (*Fair v. Bakhtiari*, 40 Cal.4th 189, 197 (2006).)

“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.” *Id.* Without taking that extra step, a term sheet may not be enforceable in court, even if the parties subjectively believed otherwise at the time of contract formation.

Whether a settlement agreement satisfies the section 1123 requirements is a fact specific inquiry. In *Estate of Thottam v. Peter Thottam*, 165 Cal.App.4th 1331 (2008), the

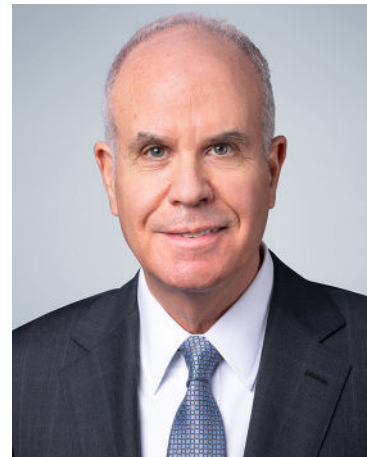
court evaluated whether a chart prepared during a mediation depicting how the decedent’s assets were to be divided among her three children could be admitted under section 1123 in a subsequent settlement enforcement action. The court of appeal found that the parties’ premediation confidentiality agreement, consenting to disclosure “as may be necessary to enforce any agreements resulting from the [mediation]...” made the agreement disclosable for enforcement purposes. The court then found that the chart, which listed various assets to be distributed, and which was signed and dated by each party, constituted a “written settlement agreement” capable of enforcement under 1123. In *In Re Marriage of Daly & Oyster*, 228 Cal. App. 4th 505 (2014), the parties characterized a stipulated judg-

ment as their “marital settlement agreement” and further agreed that the court would “reserve jurisdiction to supervise [enforcement] of the Stipulated Judgment.” *Id.* at 511. The court found that this language demonstrated the parties’ intent for the document to be disclosable and enforceable under section 1123. As noted above, enforceability is strongly dependent on the particular facts of the settlement.

Material Terms

In addition to including language that the agreement is binding and enforceable, a settlement arrived at through a mediator proposal, term sheet or memorandum of understanding must also set forth all material terms of the parties’ agreement. Rarely, however, do short-form settlement documents

Judge **Suzanne H. Segal** (Ret.) is a neutral and **Mark Loeterman** is a mediator at Signature Resolution.



succeed in doing this. Most mediator proposals, term sheets and MOUs are placeholders, intended to document key terms pending negotiation of a more comprehensive final agreement. In complex disputes, it is not uncommon for parties to reach agreement on a range of issues during the mediation, but defer additional issues for further negotiation: What releases will be included? What consideration will be paid? Will there be a future relationship between the parties? What about liquidated damages? Confidentiality? Under certain circumstances, a formal agreement must be fully drafted before an enforceable agreement is in place. In California, the 1998 *Weddington* decision best illustrates these issues. There, a state appellate court ruled that to be enforceable, a settlement agreement “must not only contain all the material terms but also express each in a reasonably definite manner.” The law of contracts, the court said, “precludes specific enforcement of a contract when it cannot be determined exactly what terms the parties agreed upon.” (*Weddington Productions, Inc. v. Flick*, 60 Cal. App.4th 793 (1998).)

Justice Joyce Kennard’s concurring and dissenting opinion in *Fair*, discussing the *Weddington* decision, is instructive. While agreeing with the majority that the settlement memorandum at issue was inadmissible under section 1119(b) and not within the settlement agreement exception of section 1123, she concluded that the ambiguity of a key term showed that no contract had been formed. Justice Kennard rejected the majority’s holding that “[an] arbitration clause was not, and could never be, such a provision [under Section 1123(b)].” For Justice Kennard, “[O]nce a court has determined that a document prepared and signed by the party during mediation is actually a ‘written settlement agreement’ – that it embodies a meeting of the minds on all material terms needed for settlement – the inclusion in that settlement agreement of a provision for arbitration ... may be viewed as an acknowledgement by the parties that their settlement agreement is binding and enforceable.”

Federal cases have taken a dif-

ferent approach. In *Facebook, Inc. v. Pac. Nw. Software, Inc.*, 640 F.3d 1034 (9th Cir. 2011), the Ninth Circuit relied on the express language of a settlement agreement reached at a private mediation to rule that the transfer to Facebook of the Winklevoss twins’ shares in ConnectU was appropriate, even though additional documents were contemplated to fully effectuate the transfer. The agreement stated that “they may execute more formal documents, but these terms are binding, and this document may be submitted into evidence to enforce this agreement.” According to the court, this left no doubt that the parties meant to bind themselves, even if other important terms of the deal – deemed important but not “necessary” terms – would be determined later. Unlike *Weddington*, the Ninth Circuit appeared to be comfortable enforcing the agreement even with some uncertainty in the terms.

In *Sony Elecs., Inc. v. HannStar Display Corp.*, the district court found that a mediator proposal failed to bind the parties. The mediator had emailed his proposal to both Sony and HannStar under a “double-blind” procedure through which the parties would separately indicate their acceptance or rejection. After they had both accepted the proposal, the mediator emailed that “This case is now settled subject to agreement on terms and conditions in a written settlement document.” (*In re TFT-LCD (Flat Panel) Antitrust Litig.*, (*Sony Elecs, Inc. v. HannStar Display Corp*) 835 F.3d 1155, 1157 (9th Cir. 2016).)

When HannStar refused to pay the agreed amount, Sony alleged breach of contract for HannStar reneging on the settlement. The district court denied the motion, stating that the email exchange with the mediator was inadmissible under California law and not intended to be enforceable or binding. Instead, the district court found that the mediator proposal was “subject to the execution of an appropriate Settlement Agreement, MOU, or Agreement in Principle.” The Ninth Circuit disagreed, finding that federal privilege law controlled and that the mediator proposal was admissible in federal court for enforcement purposes.

Clarity of Terms

Other jurisdictions may have less stringent standards for enforceability of settlement documents. The Seventh Circuit has held that a two-sentence handwritten agreement between an employee and the company she sued for employment discrimination and retaliation was enforceable, even though a more comprehensive typewritten document was never executed by the parties. (*Beverly v. Abbott Laboratories*, 817 F.3d 328, 334 (7th Cir. 2016).) Applying an objective test under Illinois law, that court held that even though it omitted material terms, the handwritten document sufficiently defined the parties’ intentions and obligations.

A New York court ruled in 2017 that even when no formal agreement was signed between the parties to a business transaction, their term sheet was a binding and enforceable agreement because it reflected “all essential terms” of a contract – “an offer, acceptance of the offer, consideration, mutual assent, and an intent to be bound” sufficient to find a meeting of the minds. More importantly, the subsequent actions of the parties signaled that there was a deal upon which both sides relied. (*Mcgowan v. Clarion Partners, LLC*, 2017 N.Y. Slip Op. 30019(U).)

Keeping these other decisions in mind, practitioners should confirm that any informal settlement agreements reached during a mediation make it perfectly clear that the parties will contemplate the future execution of a more detailed agreement.

Procedural Status Determines Enforcement Mechanism

Assuming the substantive requirements for enforcement have been satisfied, the procedural posture of a case will affect how an aggrieved party seeks relief for a breach. If litigation is pending, a settlement may be enforceable under California Code of Civil Procedure Section 664.6, which empowers the court to enter judgment on the motion of either party when the agreement specifically requests that the court retain jurisdiction for enforcement purposes. While the statute previously referred only to a “writing signed by the parties,” as a result

of an amendment enacted during the Covid-19 pandemic in 2020, this definition was expanded to include signature by an attorney representing a party, provided that the client has expressly authorized such execution. The amendment similarly covers signature by an agent acting on behalf of an insurer.

By contrast, if the matter is pre-litigation, then a separate action for breach of contract or suit in equity must be filed.

Why Use Mediator Proposals, Term Sheets, MOUs?

Even when term sheets or mediator’s proposals are not enforceable, they can still be valuable in confirming agreement on specific points, and in achieving an ultimate resolution of the entire dispute. With the assistance of a mediator, parties can use term sheets, MOUs and proposals to work through their most difficult issues. Term sheets and mediator’s proposals memorialize the agreements reached and allow parties to begin the process of preparing an enforceable settlement agreement.

Once the most contentious issues are put to rest, the tone of the negotiation changes. The parties often become more open and amenable to resolving other issues. Mediator’s proposals and term sheets can serve as valuable tools to move parties toward agreement at a critical juncture in the negotiations, when they are engaged, focused, committed and present.

Conclusion

When parties reach agreement at a mediation, it is natural to assume that their dispute is over. This assumption may be erroneous, however, unless the parties have addressed the material terms of their agreement and carefully documented their intentions and expectations – through words like “binding” and “enforceable.” Nevertheless, even when mediator proposals, term sheets and MOUs are not independently binding and enforceable, they are still useful tools in resolving legal disputes. If parties understand the limits of these agreements, term sheets and mediator’s proposals are highly effective methods of moving parties closer to a final resolution.