Negotiating a Payment Plan at Mediation

In litigation involving small and middle-market businesses, financial hardship may be an obstacle to a settlement. When the time comes to discuss settlement at mediation in these situations, the merits of the case often take a back seat to the financial realities of the parties.

Resolving a case with a party that is experiencing financial hardship requires a frank and candid communication about the financial realities, including the financially distressed party’s cash flow, assets, liabilities, access to credit and the potential impact of bankruptcy.

One of the key tools for settling a case involving a financially distressed party is a payment plan. But not all payment plans are created equal. A payment plan should be tailored to meet the particular needs of the parties. In general, the financially distressed party will want flexibility that will allow it to live up to the terms of the plan. In contrast, the opposing party will want to close the book on the case as soon as possible.

An effective mediator will be able to facilitate communication about the needs of the parties while offering creative solutions to meet those needs. Here are my thoughts about the most important considerations for negotiating a payment plan at mediation.

Length of Payment Term

The most common issue that comes up when negotiating a payment plan at mediation is the length of the payment term. Obviously, a party experiencing financial hardship usually will want a longer term for maximum financial flexibility, whereas the opposing party will want the settlement funds as soon as possible.

Reconciling these competing interests requires communication about why the financially distressed party wants the payment term it is requesting. Is it based on its projected cash flow until the settlement is paid in full? Is it based on the terms of the financing it can secure?

Where the opposing party does not want to deal with installment payments, another option is to give the finally distressed party more time to pay a lump sum. For example, whereas the typical settlement is payable within 30 days of executing the settlement agreement, the parties can agree to payment in 60, 90 or 120 days instead.

In some cases, the financing for the settlement may be contingent on an event like the sale of real property or a marital dissolution. In these situations, again, it is important for the parties to communicate about their respective interests and figure out how they can be reconciled in a way that both sides can live with in the interest of closing the deal.

No Such Thing as a Free Lunch (or Free Credit)

Another consideration for negotiating a payment plan is creating an incentive for the other side to agree to be paid over time. In the business world there is no such thing as interest-free financing. Accordingly, a party confronted with a payment plan may want to be paid a premium as part of the gross settlement amount.

A party negotiating a payment plan may even make two separate settlement demands/offers; one amount in a lump sum and a second, higher amount in installments. It could be the case that a party experiencing financial hardship is willing to pay sooner to avoid paying a premium.

Another incentive for agreeing to a payment plan is to include a significant down payment prior to the subsequent installments. A down payment may be attractive to a party that has upcoming financial obligations, such as living expenses, credit card debt and holiday shopping.

On the other hand, where a financially distressed party expects its financial condition to improve in the future, the parties can agree to a payment schedule that gradually increases over time. Along the same lines, the payment plan can include a large balloon-like payment at the end of the term.

Protection Against Defaults

While the parties negotiating a payment plan may have the best intentions in mind, defaults are a harsh reality when dealing with financial hardship. Thus, the parties must be ready to negotiate over default provisions at the mediation. In other words, what remedy will the non-defaulting party have in the event of a default?

Some parties may ask the finally distressed party to stipulate to a judgment in the amount owed in the event of a default. That judgment may or may not include the attorneys’ fees and costs required to enforce the judgment. It may require the non-defaulting party to provide the other side a reasonable opportunity to cure the default before going back to court. The parties need to think these issues through before signing off on a payment plan.

Another issue to consider is the procedure by which the non-defaulting party can obtain a judgment. Courts are strict about the conditions under which it will retain jurisdiction over a case to enforce a settlement that will be paid over an extended period of time. The alternative – initiating a new action for breach of the settlement agreement – may not be as efficient and cost-effective. Therefore, it pays to be up to speed on the most recent developments on this issue.

Ultimately, negotiating a payment plan at mediation requires compromises from both sides. With the help of a skilled, creative mediator who understands these issues, they can still reach an agreement that gives both sides closure.