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BE CAREFUL WHAT YOU INCLUDE IN A SETTLEMENT: 4TH CIRCUIT BLOCKED FUTURE LITIGATION ON A RELATED ISSUE

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Fourth Circuit decision reminds litigants that settlement agreements can have far-reaching effects on the relationship between the parties.

A **recent decision** of the U.S. Court of Appeals for the Fourth Circuit addressed a dispute concerning a ship repair contract that the U.S. Navy signed with a company called East Coast Repair. East Coast Repair claimed the Navy owed money for the repairs. But the court's decision turned not on the ship repair contract, but on a settlement agreement the parties had recently signed to resolve a separate lawsuit on a separate contract. Based on its interpretation of the settlement agreement, the court held that East Coast Repair had settled and released the later claim.

The decision reminds litigants of the importance of precision in settlement agreements. Those agreements can have a profound impact on the parties' ongoing business relationships.

Background to the 'East Coast Repair' Case

East Coast Repair signed separate contracts with the Navy for the repair of two ships: the *USS Tempest* and the *USS Hurricane*. East Coast Repair delivered the *Tempest* late and the Navy claimed it was entitled to damages as a result.

The Navy would have withheld payment, but it had already paid substantially all of the money due on the *Tempest* contract. So, the Navy decided to instead withhold payment on the other contract, for the *Hurricane*, to recoup the money. The Navy withheld over \$450,000 on the *Hurricane* contract as a "set-off" for the alleged damages on the *Tempest* contract.

East Coast Repair disputed the set-off and sued the Navy on the *Tempest* contract. The parties eventually settled their dispute. As part of the settlement, East Coast Repair released the Navy from "any and all actions, liabilities, claims ... and liabilities of any type ... arising out of or in any way relating to the *Tempest* Contract." As a result of the settlement, the lawsuit was dismissed with prejudice.

Two years later, East Coast Repair again sought to recover the \$450,000. This time, it sued the Navy under the *Hurricane* contract. East Coast Repair argued that the Navy had breached the *Hurricane* contract by deducting payment on that contract (where there was no claimed breach) to compensate for an alleged breach of the *Tempest* contract.

The Navy argued that the settlement agreement barred East Coast Repair's claim. The trial court agreed, and East Coast Repair appealed to the Fourth Circuit.

The Fourth Circuit's Decision

On appeal, the Fourth Circuit affirmed the judgment in favor of the Navy, agreeing with the trial court that the parties' settlement agreement prevented East Coast Repair from recovering the damages it sought.

The court started with the simple principle that a settlement agreement is interpreted like any other contract. So, the court determines the parties' intent by looking only at the language of the agreement. Only when the agreement is ambiguous does the court look beyond its plain language and consider evidence of the parties' intentions.

Here, the language of the agreement gave rise to a broad release of claims East Coast Repair might have against the Navy. It included "any and all claims ... in any way relating to the *Tempest* contract." The court acknowledged that East Coast Repair was technically seeking damages that were due not under the *Tempest* contract, but under the *Hurricane* contract. East Coast Repair had earned the \$450,000 it was seeking by performing work on the *Hurricane*, not on the *Tempest*. But the claim plainly related to the *Tempest* contract. Previously, in the lawsuit that was ultimately settled, East Coast Repair had claimed recovery of the same money, arguing that it was due under the *Tempest* contract because the Navy had improperly withheld the money based on a dispute about the delivery of the *Tempest*.

East Coast Repair argued that the parties had not intended to release claims so broadly. It urged the Fourth Circuit to look at subtle differences in the language between East Coast Repair's release of claims in the agreement and the Navy's release of claims. The Fourth Circuit rejected this argument, concluding that there was no justification for reading East Coast Repair's release more narrowly than it was written. The court noted that the parties could have included an exception in the agreement to allow claims related to the set-off, but they did not do so. Ultimately, regardless of what East Coast Repair claimed the parties intended, it was stuck with the plain language of the agreement it had signed.

Takeaways from the 'East Coast Repair' Decision

The *East Coast Repair* decision reminds parties to take great care in drafting their settlement agreements. When parties settle a dispute, they may not envision future disputes that could arise between them. But if they are in an ongoing relationship, their new contractual agreement (i.e., the settlement) may have just altered their relationship.

Final note: Depending on the state law governing the settlement agreement, parties may need to include special language to ensure that their release is effective. Some states, for example, require a prominent disclaimer if parties are releasing certain kinds of claims.

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