

Settlement agreements: Employee guide

Introduction

A **settlement agreement** is an agreement between an employer and an employee, which settles employment claims. An independent legal adviser is required.

In the **settlement agreement** usually the employee waives the ability to bring employment claims on the basis that the employer pays the employee a discretionary termination payment. This could, for example, be in the form of an enhanced redundancy payment or a compensation payment for loss of office.

Independent legal advice for settlement agreements

It's a legal requirement that the employee receives independent legal advice on the terms and effect of the **settlement agreement** and its effect on the employee's ability to pursue rights before an employment tribunal. The rationale for this is that if there was no such requirement it would be much easier for employers to put pressure on an employee to waive claims. The independent legal adviser must have a policy of insurance or indemnity covering the risk of a claim by the employee.

What are the other legal requirements for settlement agreements?

- The **settlement agreement** must be in writing.
- The **settlement agreement** must relate to particular complaints.
- The **settlement agreement** must state that the conditions for regulating such agreements under the relevant statutory provisions have been satisfied.

The Advisory, Conciliation and Arbitration Service ([Acas](#)) has produced a useful [guide](#) on **settlement agreements**, which also sets out the legal requirements.

Negotiation

It is important to assess the amount of money that the employee is receiving and whether a bigger sum could be negotiated. This will involve considering any potential claims against the employer, the prospects of success and the value of such claims. A broad estimate of potential costs in pursuing any claims should also be taken into account. Usually each party must pay for their own costs in the employment tribunal. The time taken for a claim to be heard in the tribunal also needs to be taken into account. All these factors need to be weighed up against the offer to determine if the offer is a reasonable one. The independent legal adviser needs to advise on whether the deal is a good one.

In some cases it may well be possible to [negotiate](#) a higher **settlement sum**, depending on the potential claims that the employee may have and the value of any claims.

Even if the employee has no potential claims sometimes it may still be possible to negotiate a better package. An employer may be willing to increase the offer on the basis of good faith even when there is no legal reason to do so.

Tax

Generally, the first £30,000 of a [termination payment](#) is free of tax and national insurance contributions (NICs). However, there are a number of exceptions. One of the exceptions is a sum corresponding to earnings for notice is subject to tax and NIC deductions.

Legal costs for settlement agreements

Normally the employer contributes towards the employee's legal costs for obtaining legal advice on a **settlement agreement**. There is no legal requirement for the employer to contribute but it is common practice. If further legal costs are incurred usually the employee would have to cover the shortfall unless the employer agrees to increase the contribution.

References

A [reference](#) could be agreed and annexed to the **settlement agreement**. The employer would then normally be obliged to provide the agreed reference to any prospective employers. In many sectors, including the financial sector, it is standard practice only to provide a factual reference with dates of employment and job title. A factual reference could nevertheless be annexed to the settlement agreement. In some cases it may also be sensible to agree an internal announcement.

Confidentiality

Usually employees will be required to agree to confidentiality obligations. A typical clause (sometimes known as a **non-disclosure agreement** or gagging order) could prevent the employee from disclosing the terms of the **settlement agreement** and the circumstances of their departure with third parties. Often there will be a clause covering exceptions for disclosure to immediate family, professional advisers and as required by law. The employee will also often be permitted to disclose their employment history and the reason for leaving to prospective employers and recruitment consultants.

Employees cannot be precluded from whistleblowing (making a public disclosure) or reporting to the police.

Recently, the government has announced [reform](#) to tackle the misuse of **non-disclosure agreements**.

Non-derogatory statements

Often employers will require employees to agree that they will not make derogatory comments about their employer or make comments that could lower the employer's reputation.

Employers may agree to include a reciprocal clause to protect the employee. However as it is difficult for employers to police such clauses the clause may be limited to "using reasonable endeavours" to preclude employees from making derogatory comments or, alternatively, state that

the employer shall instruct certain named employees (that the particular employee is concerned about) not to make such comments.

Restrictive covenants and settlement agreements

Any restrictive covenants relating to competitive activity in the employment contract could continue to apply and could be referred to in the **settlement agreement**. An employee may be prohibited for a certain period of time from joining a competitor or setting up in competition. An employee may also be precluded for a certain period of time from soliciting clients, dealing with clients and poaching staff. The employer might agree to waive or change some of the restrictions as part of the **settlement agreement**.

Bonuses

If the employee is expecting to receive a [bonus](#) an appropriate clause ought to be included in the **settlement agreement**. Sometimes an employee may have received a previous bonus award which would vest at a later date. This could be in the form of cash, stock or options. Often when employees are made redundant they are treated as good leavers and awards continue to vest on the usual vesting dates or are accelerated. This is not always the case though.

There could be other issues to consider too, and each case will be different.

This guide is intended for guidance only and should not be relied upon for specific advice.

If you need any advice on **settlement agreements** please do not hesitate to [contact](#) me on [020 3797 1264](tel:02037971264).