

# Palmerslaw

## Guide to settlement agreements

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There may be occasions during an employment relationship when everything does not go according to plan and, in some instances, it may be necessary to terminate the working relationship between an employer and an employee. In such circumstances, a settlement agreement can help ensure the parting of the ways is on the best terms possible, avoiding costly and time-consuming employment disputes in the process.

## What is a settlement agreement?

A settlement agreement is a legally binding arrangement between an employer and an employee, which sets out the financial and other terms on which they will go their separate ways.

In essence, such agreements include a severance payment made by the employer in return for the employee agreeing not to bring certain legal claims against the employer.

There are various circumstances in which a settlement agreement may be proposed, including:

- Redundancy
- Mutual agreement
- Dismissal
- To settle an employment tribunal claim

# What is included in a settlement agreement?

The contents of each settlement agreement will vary depending on the particular circumstances of that case. However, there are some elements which will be common to most agreements, which include:

- The amount of compensation to be paid (such as payments for redundancy, unpaid wages, bonuses, pay in lieu of notice and any holiday pay entitlement)
- Any restrictions on future employment
- Confidentiality requirements, which may permit the employee to tell people they have entered a settlement agreement, but not to discuss its contents, or may prohibit the employee from even mentioning that a settlement agreement has been put in place
- Any assurances given by the employer
- The reference that will be provided by the employer upon request
- Whether an announcement will be made to colleagues and clients
- A mutual agreement that the parties will not make derogatory comments about each other

Settlement agreements cannot be used to exclude liability for personal injury claims, but a carefully worded warranty can provide some protection. Despite having waived 'all' claims, an employee who signs the agreement will also be able to bring claims if the employer breaches the contract, as well as in respect of any accrued pension rights.

# The legality of settlement agreements

To be legally valid, the settlement agreement must comply with a number of conditions, including:

- It must be in writing
- It must relate to a particular complaint
- The employee must have received legal advice from a relevant independent adviser, such as a solicitor, on the terms and effect of the proposed agreement and its effect on their ability to take a claim to an employment tribunal
- The adviser must have professional indemnity insurance to cover the risk of a claim by the employee in relation to the advice provided
- The agreement must state that the conditions regulating settlement agreements have been satisfied



# What are the financial implications of a settlement agreement?

While it is a legal requirement that employees see a lawyer under s.203 Employment Rights Act 2006, as they are compromising a number of their rights by signing the agreement, the employer is not actually under any obligation to contribute to the employee's legal fees. However, as it is in the employer's interest that the employee signs, a contribution will usually be made to cover the costs of advice in relation to the terms of the agreement and the signing.

In general terms, the payments made to the employee in respect of salary and holiday pay will be subject to the normal deductions for tax and national insurance contributions.

Employees may be entitled to receive any compensation for their loss of employment tax-free up to £30,000. Anything over £30,000 will be taxed accordingly. If the employee receives a tax-free compensation payment, then the employer should ask for indemnity against the risk that HM Revenue & Customs will decide the payment does not truly represent compensation and needs to be taxed.

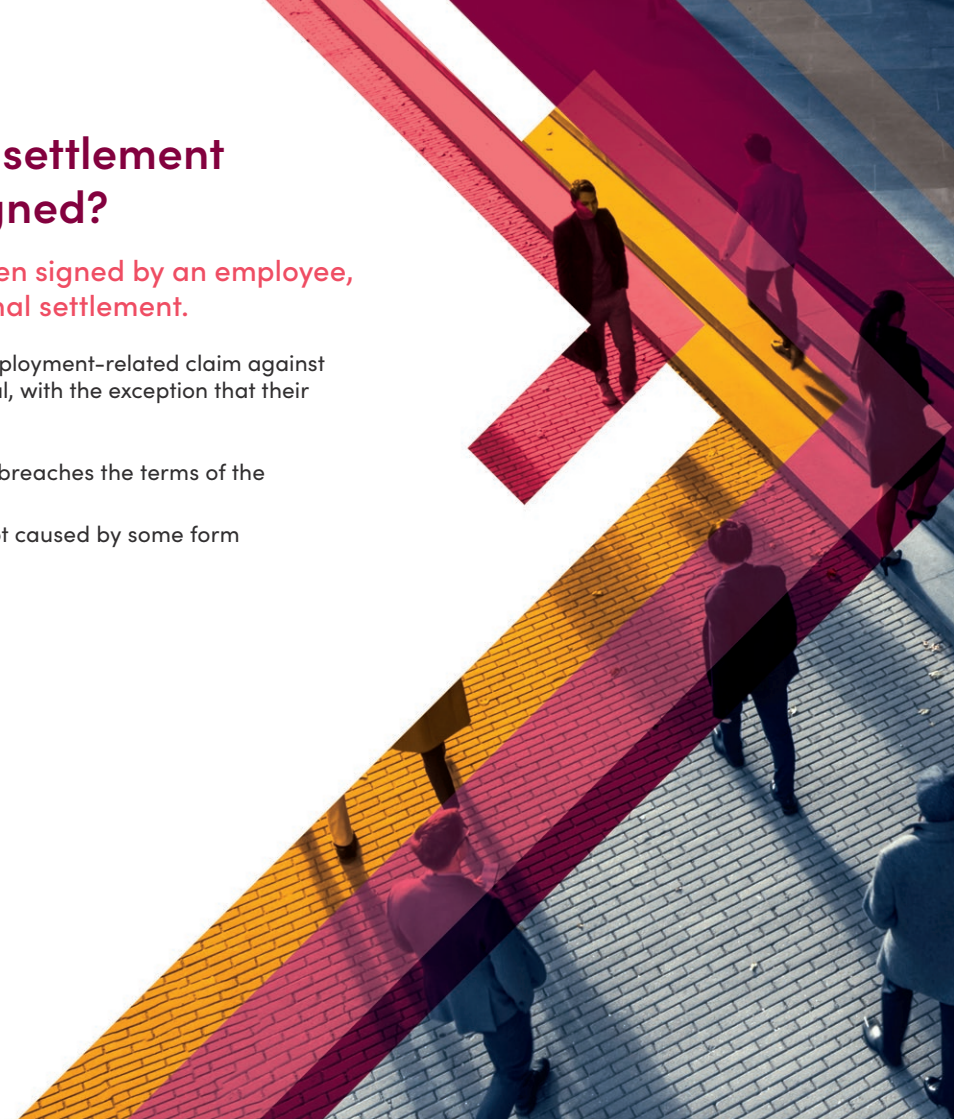


# What happens once the settlement agreement has been signed?

Once a settlement agreement has been signed by an employee, they accept the terms as a full and final settlement.

As a result, they waive their rights to bring an employment-related claim against the (former) employer in the employment tribunal, with the exception that their right to bring the following claims is preserved:

- A claim for breach of contract if the employer breaches the terms of the agreement
- Personal injury claims where the injury was not caused by some form of discrimination
- Claims in respect of accrued pension rights



# What happens if the employee refuses to sign the agreement?

While there is no obligation, legal or otherwise, on the employee to sign the settlement agreement, there may be financial implications of not doing so.

Where the employee does not sign a settlement agreement, their employment will be terminated with them receiving only what they are contractually or statutorily entitled to, rather than the full package on offer.

If the employee decides not to sign and to instead pursue a claim against the employer at the employment tribunal, they will usually have three months, minus one day, from the date of termination to lodge their claim. However, if the employee decides not to sign the settlement agreement, they will not receive a contribution towards the related legal fees from the employer, and so will be liable for these.

## How can Palmers Solicitors help?

At Palmers Solicitors, we have the expertise required to prepare and advise on settlement agreements, including negotiating the final terms. Our responsive and proactive approach results in quick turnaround times, ensuring the working relationship is ended as swiftly and efficiently as possible.

For tailored advice on the law surrounding settlement agreements, or any other employment law matter, please contact us.



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