LEWIS SILKIN

Ius Laboris UK Global HR Lawyers
LEWIS SILKIN

Settlement agreements



Inside

What is a settlement agreement?
Requirements for a valid agreement
Claims that may or may not be waived
Content of the agreement
Without prejudice and subject to contract
Pre-termination settlement discussions
COT3 agreements

Introduction

First introduced by statute in 1993, settlement agreements (previously known as compromise agreements) have become increasingly common as a means for an employer and employee to settle claims and/or effect a clean break from the employment relationship.

Given the legal implications of signing a settlement agreement, it is important that both parties understand the full effect of such agreements.

For a summary of the legal issues and claims that can arise when an employment contract comes to an end, see our Inbrief *Termination of employment*.

What is a settlement agreement?

A settlement agreement is a legally binding agreement, regulated by statute, between an employee and employer. Under the agreement, the employee will usually receive a payment, or other advantage, in return for agreeing not to commence (or to stop pursuing) employment-related claims against the employer.

Other than by involving the Advisory, Conciliation and Arbitration Service (ACAS), a settlement agreement is the only way in which an employee can effectively waive statutory claims such as unfair dismissal or relating to redundancy or discrimination.

Effectively, it draws a line under the employment relationship and should provide comfort to the employer that, save in certain circumstances, it will face no further liabilities in relation to the employee concerned.

In practice, a settlement agreement will also deal with all other claims which an employee may have such as those relating to breach of the employment contract. Although it is not legally necessary to follow the settlement agreement route to waive pure contractual claims, it makes sense to include everything in one document.

When might a settlement agreement be used?

Settlement agreements are typically entered into where employment has terminated or is about to be terminated. An agreement to settle claims, however, can also be entered into where employment is continuing, for example in relation to claims for discrimination or unlawful deductions from wages.

A settlement agreement will often be offered to an employee who is being made redundant in exchange for an enhanced payment over and above the minimum statutory and contractual requirements.

It may also be used to settle actual or potential employment-related claims before they reach a public hearing in an employment tribunal or court, and in this way may help to spare the employer potentially embarrassing publicity.

Why should an employee sign one?

An employee cannot be forced to sign a settlement agreement. An employer will usually offer some form of incentive for them to do so. As mentioned above, most commonly, and assuming the agreement is being entered into on termination of employment, this will be by way of an enhanced termination payment or other such benefit. Other incentives might include an agreed form of reference or a continuation of employee benefits for a period post-termination.

Requirements for a valid settlement agreement

For a settlement agreement to be valid, there are certain conditions which must be met:

- The agreement must be in writing
- The agreement must relate to a 'particular complaint' or 'particular proceedings' (in other words, thought must be given, and be documented as having been given, to the possible claims that the employee will waive by signing the agreement)
- The employee must have received legal advice from an independent adviser (most commonly, this will be a solicitor) on the terms and effect of the proposed agreement and its effect on the employee's ability to pursue any rights before an employment tribunal. Note that this does not require the independent adviser to take a view on whether the deal offered is a good one or whether they think the employee should accept it
- The independent adviser must be identified in the agreement and have a current contract of insurance, or professional indemnity insurance, covering the risk of a claim against them by the employee in respect of their advice
- The agreement must state that the conditions regulating settlement agreements have been satisfied

Claims that may be waived

By signing a settlement agreement the employee waives his or her legal rights to bring claims that they may have against their employer. This will usually include claims arising under the contract of employment (although as mentioned above, a waiver of contractual claims does not need to be through a settlement

agreement) and certain statutory employment rights. Contractual claims might include breach of contract, notice, contractual holiday pay and other payments or benefits under the employment contract. The main statutory claims that can be given up under a settlement agreement are those for:

- redundancy pay
- unfair dismissal
- unlawful deductions from wages
- all claims relating to discrimination, equal pay and family leave rights. These include claims for discrimination based on sex, colour, race, nationality or ethnic or national origins, disability, marital or transgender status, sexual orientation, religion or belief, age, maternity, paternity and pregnancy (although not claims relating to pay - see below), and less favourable treatment for part-time and fixed-term employees
- any rights under collective consultation laws and TUPE Regulations that can lawfully be waived (see below for the exceptions to this)
- claims relating to working time, rest breaks or leave, or statutory holiday pay

Claims that cannot be waived

Not all claims can be settled by means of a settlement agreement. Claims in respect of accrued pension rights and personal injury claims that have not yet arisen cannot be settled. Nor can claims in respect of certain statutory rights. Most significantly, this includes claims for the failure of the employer to inform and consult with appropriate representatives on collective redundancies or on the transfer of an undertaking under TUPE 2006, and claims for the right to statutory maternity, paternity, adoption or shared parental pay.

There continues to be much debate as to the extent to which future claims (other than those in respect of personal injury - see above) can be settled under a settlement agreement. Case law has made clear however, that if it is possible to settle claims that have not yet arisen and about which the parties to the agreement do not yet have any knowledge, then the language used must make it sufficiently certain that this is the intention of the parties.

Content of a settlement agreement

The contents of a settlement agreement are largely at the discretion of the parties and should be negotiated and agreed on an individual basis. As a minimum, the agreement should deal with all the obligations and entitlements of employer and employee in relation to the settlement of claims and/or termination of employment.

Non-statutory guidance produced by ACAS on settlement agreements includes a basic model form of settlement agreement. Using this model agreement is optional. If an employer chooses to use it, changes should be made to fit the circumstances of each case and, in many situations, it will be advisable to enter into a more comprehensive form of settlement agreement.

Typically, it will contain provisions relating to the following:

- Arrangements for the continuation of contractual payments and entitlements up to (and sometimes beyond) the termination date and payment of any sums due on termination (e.g. accrued holiday, pay in lieu of notice)
- Arrangements for the payment of an ex-gratia amount as compensation for loss of employment and/or in consideration for the waiver or withdrawal of claims
- The actual waiver or withdrawal of claims, typically together with a warranty that there are no other claims of which the employee is aware that they have against the employer
- A restatement (and sometimes modification) of the employee's ongoing duty of confidentiality and any restrictive covenants to which they are subject. Both employer and employee may also want some comfort that neither will disclose the existence or terms of the agreement or the circumstances leading to it being negotiated. A "no-derogatory comments" clause is also often included for the benefit of one or both parties. In light of recent scrutiny of the use of some non-disclosure agreements or terms in settlement agreements to prevent allegations of misconduct being reported to appropriate authorities, careful consideration should be given to the scope of any such clause
- Practical arrangements, such as payments into the employee's pension scheme, purchase of company property (for example a car or mobile phone), and the return by the employee of company property
- Contribution to the employee's legal fees. Given the importance of ensuring that a settlement agreement is legally valid, it is likely that the employer will agree to pay a certain amount towards the fees of a lawyer/independent adviser for the employee (although this is not legally required). This would be documented in the agreement, along with the requisite confirmation that the conditions regulating settlement agreements have been satisfied
- Indemnities which may be provided from employee to employer, for example in relation to the tax treatment of any sums payable under the agreement (see below)

Tax

It is usual for the agreement to include a tax indemnity from the employee to the employer. This means that if tax over and above that which has been deducted is payable, it will be the responsibility of the employee (who may need to declare any such payments in his/her tax return) and not the employer.

"Without prejudice and subject to contract"

A settlement agreement will often be marked as being "without prejudice and subject to contract".

"Without prejudice" means that statements made in the course of negotiations cannot be used in evidence against the party that made them (for example as an admission of guilt)

in any court or tribunal proceedings. It is important to note that the "without prejudice" rule will only apply where discussions are a genuine attempt to resolve an existing dispute between the parties.

"Subject to contract" means that the agreement cannot be relied upon by either employer or employee until it has been properly signed. This is less important in relation to those statutory claims which require the settlement

agreement to be signed before they can be waived. It is, however, more relevant in relation to claims that do not need the formality of a settlement agreement. The use of "subject to contract" will usually be enough to avoid any argument that agreement has been reached orally before the settlement agreement has been signed.

Pre-termination settlement discussions

Since July 2015, employers (and employees) are able to embark on discussions with a view to terminating the employment relationship on agreed terms without those discussions being admissible in most subsequent unfair dismissal proceedings (unless there has been "improper behaviour").

This rule operates alongside the existing rule on "without prejudice" discussions and, in effect, extends the "without prejudice" rule to situations where there is no "existing dispute" (see above). Significantly, however, the content of these settlement discussions is only inadmissible in so far as it relates to ordinary unfair dismissal claims. The regime does not prevent discussions relating to other claims such as automatically unfair dismissal, discrimination and breach of contract from being referred to in the tribunal (unless they are covered by the "without prejudice" rule).

ACAS has published a statutory Code of Practice on settlement agreements which a tribunal can take into account in the context of any subsequent proceedings.

COT3 agreements

A COT3 is the form used to record the terms of an agreement to settle an employment tribunal claim (or potential claim) that has been negotiated with the assistance of an ACAS conciliation officer.

Unlike a settlement agreement, there are no formalities that must be observed in drawing up a COT3 agreement. It will be binding provided that it meets the minimum requirements for any legally binding contract and an ACAS officer has been involved to conciliate the settlement.

In particular, there is no requirement for the employee to have received advice on the terms and effect of the agreement from an independent adviser. The ACAS officer will be aiming to reach a general settlement of the issues involved, however, rather than representing the specific interests of either party. Those who require advice on their own behalf may wish to consult an employment law specialist as well as ACAS.

For further information on this subject please contact:

Richard Moore
Partner
+44 (0) 20 7074 8387
richard.moore@lewissilkin.com

This publication provides general guidance only: expert advice should be sought in relation to particular circumstances. Please let us know by email (info@lewissilkin.com) if you would prefer not to receive this type of information or wish to alter the contact details we hold for you.

© 2018 Lewis Silkin LLP