HR Guidance

Settlement agreements

This business guide sets out the key issues a business should consider before entering into a settlement agreement with an employee.

Settlement agreements

Fairways HR guidance only provides an overview of the law in this area. For a complete understanding of how it may affect your particular circumstances in the workplace please contact one of our Consultants.

What is a settlement agreement?

A settlement agreement (formerly known as a compromise agreement) is a legally binding agreement between an employer and an employee under which the employee agrees to settle their potential employment claims and in return the employer will agree to pay financial compensation. Sometimes the agreement will include other things of benefit to the employee, such as an agreed reference letter.

In what circumstances will a settlement agreement be appropriate?

- An employee may have claims against an employer under both their contract of employment and under statute. These claims may arise:
  - » on recruitment;
  - » during employment; or
  - » on termination of their employment.
- In many cases, an employer may want to make a payment to an employee in return for an effective waiver of their potential claims. Employers can enter into an agreement with an employee to settle potential claims when they are still working for the business, but in most situations, their employment will have ended (or be about to end).

In what circumstances will a settlement agreement be appropriate?

To validly settle statutory employment claims, a settlement agreement must satisfy several conditions that must be met:

- The agreement must be in writing.
- The agreement must relate to a particular complaint or particular proceedings.
- The employee must have received legal advice from a relevant independent adviser (for example, a qualified lawyer or union official) on:
  - » the terms and effect of the proposed agreement; and
  - » its effect on their ability to pursue any rights before an employment tribunal.

In what circumstances will a settlement agreement be appropriate? (continued)

- The independent adviser must have a current contract of insurance (or professional indemnity insurance) covering the risk of a claim against them by the employee for the advice.

- The employee's adviser must be identified.

- The agreement must state that the conditions regulating settlement agreements have been satisfied.

Possible content of a settlement agreement

Other than the legal requirements listed above, the contents of a settlement agreement are largely at the discretion of the business and the employee involved. Examples of common clauses include:

- Compensation for loss of employment.

- Contribution to legal fees.

- Waiver of claims by the employee, including warranty that the claims listed are the only claims which the employee has against the employer.

- Re-assertion or modification of existing restrictive covenants.

- Return of the employer's property.

- Indemnity from employee in relation to tax and National Insurance Contributions.

- Undertaking from the employee not to use the employer's confidential information or make any adverse comments about the employer.

Which types of claim can be settled by a settlement agreement?

Only certain statutory claims can be settled by a settlement agreement. These include claims for:

- Unfair dismissal.

- Whistleblowing.

- Discrimination, victimisation or harassment related to age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation.

- Equal pay.

Which types of claim cannot be settled by a settlement agreement?

There are several statutory claims that cannot be settled by entering into a settlement agreement, including some types of:

- Future personal injury claims (which have not yet arisen).
- Claims for failure to inform and consult in connection with collective redundancies and on a transfer of a business.