

# Settlement Agreements

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## 1. What is a settlement agreement?

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A settlement agreement is a legally binding agreement entered into by an employer and employee setting out the agreement reached between them when a contract of employment is to be terminated or a dispute is to be resolved. In return for a payment (usually), the employee agrees to waive their statutory employment rights.

## 2. What is the effect of a settlement agreement?

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The effect of signing a settlement agreement is that, in exchange for a termination payment and any other benefits the employer agrees to provide, the individual will waive most, if not all, of their employment-related statutory and contractual rights. Once the agreement is signed, the individual will not be able to bring any claims in respect of their employment or its termination; this includes an unfair or wrongful dismissal claim, any form of discrimination claim, any breach of contract claim, a claim for unlawful deduction from wages or any claim for annual leave, expenses, bonuses or commission payments due. The effect of signing a settlement agreement is to draw a line under the employment relationship and agree that there is no going back.

## 3. Does a settlement agreement have to be in a specific form?

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For a settlement agreement to be valid the following conditions must be met:

- the agreement must be in writing;
- the agreement must relate to a particular complaint or proceedings;
- the employee must have received legal advice from a relevant independent adviser on the terms and effect of the proposed agreement and its effects on the employee's ability to pursue any rights before an employment tribunal;
- the legal adviser must have a current contract of insurance, or professional indemnity insurance, covering the risk of a claim by the employee in respect of the advice given;
- the agreement must identify the legal adviser; and
- the agreement must state that the conditions regulating the settlement agreement have been satisfied.

## 4. What else does a settlement agreement cover?

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If the employment is terminating, the agreement will usually specify a termination date, set out the arrangements which will apply up to the termination date, deal with a return of property belonging to the employer, specify any obligations after termination and it is common for an agreed reference to be provided.

## 5. How much does it cost?

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The employer usually makes a contribution towards the cost of the employee taking independent legal advice. A common contribution is £400 to £500 + vat. In addition the employer will be responsible for its own legal costs if it instructs a solicitor to act for it in the drawing up and/or negotiation of the settlement agreement.

## 6. Tax

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It is possible to treat up to £30,000 of an ex-gratia/redundancy payment made under a settlement agreement as exempt from income tax if the payment comes within section 401 Income Taxes (Earnings and Pensions) Act 2003. With effect from 6<sup>th</sup> April 2020 all termination payments above the £30,000 threshold will be subject to employer National Insurance contributions.

Acas also produce information:

<https://www.acas.org.uk/settlementagreements>

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