

# A GUIDE ON REDUNDANCY AND SETTLEMENT AGREEMENTS

Employment Law



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## A guide on redundancy and settlement agreements

### WHAT IS A REDUNDANCY?

#### Redundancy



It is a type of dismissal, and the statutory definition encompasses three types of situations: business closure, workplace closure, and reduction of work of a particular kind. Redundancy is a potentially fair reason for dismissal and therefore may give an employer a defence to an unfair dismissal claim.

A redundancy dismissal is likely to be fair if:

1. The employer identifies an appropriate pool for selection
2. The individuals in the pool are consulted with
3. An objective selection criterion is applied to those in the pool
4. The employer considers suitable alternative employment where appropriate

A redundancy must be genuine. Employees selected for redundancy due to any of the protected characteristics in the Equality Act 2010, or on grounds of fixed-term or part-time status, have the right to bring a claim for discrimination or for less favourable treatment due to their fixed-term or part-time status.

### WHAT RIGHTS DOES AN EMPLOYEE HAVE IF THEY ARE MADE REDUNDANT?

Employees in a redundancy have the following rights:

- A right to individual consultation
- In a collective redundancy, all affected

employees have the right to be informed and consulted in accordance with section 188 of the Trade Union and Labour Relations (Consolidation) Act 1992

- The option to move into a different position within the company if applicable
- Employees with two years' qualifying service have the right to time off to look for work or arrange training
- The right to contractual notice, subject to statutory minimum notice
- Employees with two years' qualifying service have the right to receive a statutory redundancy payment. An employee may also be entitled to a contractual redundancy payment, if there is an express or implied right to one.

### WHAT IS A SETTLEMENT AGREEMENT?

#### Settlement Agreement



This is an agreement between an employer and employee that sets out the terms of the employee's termination of employment. It usually includes a waiver of the employee's statutory and contractual claims on termination in return for some sort of (usually) monetary incentive. The agreement is legally binding and if a party is in breach, the persecuted party is free to bring a claim.

If an employee has a claim against their employer which could be brought in an employment tribunal, a settlement agreement may be used to stop the employee from making the claim or taking it any further.

### WHAT IS A PROTECTED CONVERSATION?

A protected conversation – sometimes referred to as pre-termination negotiation – is a conversation to discuss termination of employment and set out proposed terms of a settlement agreement.

### WHAT DOES WITHOUT PREJUDICE MEAN?

‘Without prejudice’ can be used as a heading or label or within the body of any letter, email or other document which forms part of an exchange of correspondence. It will prevent statements made in a genuine attempt to settle an existing or potential dispute from being used as evidence or admissions in court or tribunal proceedings against the party who made them. Parties are more likely to enter into settlement discussions if they can speak openly and without restriction.

It is common to see the words ‘without prejudice’ being used with the phrase ‘subject to contract’, which also confirms that nothing said during the negotiation process will give rise to a legally binding contract. All the terms must be agreed and signed by both parties first.

### WHAT ARE THE DIFFERENCES BETWEEN REDUNDANCY AND SETTLEMENT AGREEMENTS?

Settlement agreements are sometimes offered in the context of a redundancy.

However, settlement agreements are voluntary. The employee does not have to sign the agreement and has room for negotiating the terms. Settlement agreements can also include larger sums of money than what the employee is entitled to in terms of a statutory redundancy payment, which make them more attractive to employees.

Settlement agreements may also be offered in circumstances other than redundancy, such as when an employer wants to dismiss the employee due to gross misconduct but does not want to deal with a potential claim for unfair dismissal.

An employer may offer a settlement agreement package that is more attractive to an employee than the redundancy package they are entitled to. If this is agreed, the employer can avoid the lengthy process of consultation, avoid future claims brought against them by the employee, and the terms are kept confidential from other employees.

If an employee rejects the settlement offer, the employer may still go through the redundancy procedure and the employee may take advice on whether it has been done fairly or whether they have any claims against the employer for unfair dismissal. This is why an employee will consider whether the amount being offered in the settlement agreement is adequate, because if they have any potential claims, they may be able to receive an amount of compensation greater than the settlement sums being offered.



## HOW IS A SETTLEMENT AGREEMENT NEGOTIATED?

If an employee suspects that this is not a genuine redundancy, they could let the employer know that they will be claiming unfair dismissal if the settlement payment is not increased. If the redundancy is genuine, however, the employee could simply ask the employer to be more generous.

Some employees prefer to negotiate themselves, by trying to convince the employer to budge on certain aspects of the agreement, for example, increasing an ex-gratia payment.

The employee can alternatively negotiate through their solicitor, particularly where there are complex legal arguments to put forward. Obtaining independent legal advice is a requirement of a settlement agreement because the employee will be waiving their rights to bring or continue any claims against their employer. A solicitor would be advising the employee on the strengths of a potential case they may bring and explain on that basis which terms in the agreement are more easily negotiable. The solicitor would also advise on which terms are standard and may be difficult to convince the employer to change.

## WHAT MUST AN EMPLOYER INCLUDE IN A SETTLEMENT AGREEMENT?

The statutory requirements for a valid settlement agreement are in section 203(3) of the Employment Rights Act 1996. A settlement agreement must be in writing but there is no particular requirement for it to be in the employee's first language. There may however be factors for the employer to consider if the agreement is not in the employee's first language. The employee may argue that this amounts to race discrimination or may later seek to challenge the validity of the settlement agreement and argue that they were under

duress (unlawfully coerced). Additionally, the employee may have more questions, or challenge the agreement more if they do not understand it, which could lead to greater costs for the employer.

As stated above, obtaining legal advice is a requirement, so it is common for an employer to offer an amount towards the legal fees, and this amount will usually be detailed in the agreement.

## ARE PAYMENTS IN SETTLEMENT AGREEMENTS TAXABLE?



Payment entitlements under the employment contract, such as salary, holiday pay, bonuses, and payment in lieu of notice are taxable.

The termination payment is not taxable up to £30,000. Any termination sums over and above £30,000 will be taxed and subjected to national insurance contributions (NICs). HMRC can recover unpaid tax and NICs, penalties and interest from the employer under the Income Tax (Pay as You Earn) Regulations 2003. The employer has the primary liability for this. If tax and NICs have not been properly accounted for, penalties for late payment and inaccurate returns could arise.

## CONFIDENTIALITY CLAUSES IN A SETTLEMENT AGREEMENT INCLUDE?

A confidentiality requirement is very common in settlement agreements. It is a benefit for both the employer and employee.

The clause will likely restrict the employee informing others about the offer or any of its terms. There are standard exceptions that are usually included, allowing the employee to tell their spouse or partner, provided they keep the information confidential.

The agreement should make it clear that the employee can still speak to the police or a regulator about a criminal issue or misconduct. The employee can also make a protected disclosure, commonly known as whistleblowing, under section 43A of the Employment Rights Act 1996.

In terms of informing a recruiter or prospective employer, the agreement usually allows this for the sake of confirming employment history. The terms of the agreement cannot be mentioned usually, however, the employee will likely be allowed to state that the reason their employment terminated was redundancy. An employee will also be allowed to speak to an insurer about income protection claims.

#### WHAT ARE OTHER STANDARD TERMS FOUND IN SETTLEMENT AGREEMENT?

Examples of standard terms:

- ✓ The employer will pay the employee the outstanding balance for salary, bonuses, commission, and accumulated holiday (as well as additional termination payment)
- ✓ A date on which the employment will end, and whether the employee will work during their notice period and do a handover
- ✓ An explanation on what happens to current benefits, such as share schemes or health schemes, or the company car
- ✓ An explanation on which payments have tax deductions and who bears the liability for further tax
- ✓ The employer will likely fund the legal costs incurred by the employee in obtaining independent legal advice on the agreement (usually subject to a limit).
- ✓ The employee will not make derogatory comments about their employer, whether that be in person or on social media

#### TIME AN EMPLOYEE SHOULD BE GIVEN TO CONSIDER A SETTLEMENT AGREEMENT



Acas has guidance on settlement agreements. It states that as a rule, a minimum of **10 calendar days** should be allowed for an employee to consider the proposed formal written terms of a settlement agreement and to receive independent advice, unless the parties agree otherwise.

#### LEGAL SUPPORT

If you need advice about drafting or considering a settlement agreement, please contact our employment team.





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