

COMPROMISE AGREEMENTS - *A GUIDE FOR EMPLOYEES*

Introduction – what is a compromise agreement?

A compromise agreement is the formal name given to a termination agreement between an employer and an employee.

The effect of you signing a compromise agreement is that in exchange for a termination payment and any other benefits which your employer agrees to give you, you will be giving up most, if not all, of your employment-related legal rights.

This means that once you have signed the agreement, you will not be able to bring any claim in respect of your employment or its termination. For example, therefore, you cannot bring an unfair or wrongful dismissal claim, any form of discrimination claim, any breach of contract claim or claim for unlawful deduction from wages or any claim for annual leave or expenses or bonuses or commission payments due to you. The only claims that are normally (although not always) excluded from the scope of a compromise agreement are claims in respect of personal injury and accrued pension rights.

If, therefore, you believe you have any potential claims against your employer you need to consider carefully whether you should be signing the agreement at all and what the appropriate level of compensation is.

This guidance note sets out the types of provisions that you might typically expect to see in a compromise agreement and explains what the implications might be for you of such clauses.

1. Typical provisions in a compromise agreement

compromise agreement will typically cover such key matters as:

- the date when your employment terminated or will terminate;
- if you have any company property, where and when that must be returned;
- the range of claims the agreement is intended to compromise;
- the sum of money to be paid to you and when it must be paid;
- who will be liable for any tax due on the termination payment;
- what level of contribution to your legal fees will be met by your employer;
- what happens if you do in fact bring an employment-related claim against your employer;
- what will be told to other staff about your departure (if anything);
- whether you must observe any restrictions after the employment has terminated;
- whether certain matters must be kept confidential; and
- what reference (if any) you will get.

In addition, if you are a director on the Board of your employer (or a group company) you will typically be required to resign that directorship as part of the compromise. If you hold any shares in the company or a group company you may also be required to transfer these back to the company.

2. Tax treatment of termination payments

It is possible to treat up to £30,000 of a termination payment made under a compromise agreement as exempt from tax. The circumstances and agreement must, however, satisfy certain conditions before that relief is available.

In summary, where a termination payment is made as compensation for the loss of the right to be employed in the future, it should be capable of being paid free of tax and National Insurance to the extent that it does not exceed £30,000. Where, however, part of the termination payment is a payment in lieu of notice and / or of other benefits deriving from the employment relationship, that proportion of the payment is likely to be taxable.

A contract will often provide for the right to a payment on termination of employment. This commonly takes the form of a payment in lieu of notice (a 'PILON') clause whereby the employer may opt to make a payment in lieu of notice rather than have the employee work out their notice period.

3. Your obligations

It is important that you familiarise yourself with the provisions in the compromise agreement because if you were to breach any of them, you may find that your employer seeks to recoup the sums of money paid to you under the agreement.

You must look out in particular for clauses that:

- Require you to return any items of company property that you still hold (this can include such easily overlooked items as security passes to access the employer premises) within a set timeframe;
- Require you not to disclose to anyone the fact that you have been offered a compromise agreement and / or the sums of money on offer to you;
- Require you not to try to poach any staff away from the company after you leave, or to approach your employer's customers or suppliers (or even potential customers or suppliers); or
- Prevent you from setting up in competition with your employer.

Employers will also typically want you to agree not to make any written or verbal statements about it or any of its officers or employees. In return we would generally expect employers to agree not to make any derogatory comments about you.

If new restrictions are being imposed upon you (i.e. they are not just a reiteration of existing restrictions contained in your contract of employment) then a sum of money (even a nominal sum) by way of payment to you for entering into those restrictions should be apportioned to those restrictions. In other words the agreement might say that in consideration for you agreeing not to do certain things, a payment of (say) £100 will be made to you, less tax and National Insurance. This strategy can help protect a larger termination payment from having part of it taxed by the Inland Revenue.

4. The requirement for independent legal advice

In order for a compromise agreement to be legally binding, you must have independent advice from a lawyer or other appropriately qualified adviser on the terms of the agreement and the implications for you of signing it (you will see that the agreement requires your adviser to certify that you have received the necessary advice).

Employers will therefore typically contribute to an employee's legal costs in taking that advice. Please note that the contribution is not generally substantial (in the order of, say, £250 plus VAT) and may not cover the full cost in terms of time spent by your lawyer in advising you. Therefore part of the costs may be payable by you personally with the first £250 (for example) invoiced directly to your employer.