

## Technical factsheet

### Settlement offers

This factsheet is part of a suite of employment factsheets and a pro forma contract and statement of terms and conditions that are updated regularly. These are:

The contract of employment  
The standard statement of terms and conditions  
Working time  
Age discrimination  
Dealing with sickness  
Managing performance  
Disciplinary, dismissal and grievance procedures  
Unlawful discrimination  
Redundancy  
Settlement offers  
Family-friendly rights  
Employment status: workers

The settlement offer was introduced by s111A of the [Employment Rights Act 1996](#) to provide a tool to assist employers to resolve issues at work. The offer and the subsequent discussions between the employer and the employee can result in them concluding a settlement agreement by which the employment is terminated in a mutually acceptable way.

It has always been open to employers and employees to agree to end the employment and settle potential claims by means of a payment to the employee, and previously this resulted in a contract known as a compromise agreement. However, both starting and conducting such negotiations was risky for the employer unless there was already a dispute between the parties, which was usually when the employee had already been dismissed or had resigned. The reason is that the 'without prejudice' rule, which protects the conversation and keeps it confidential between the parties, only applies where there is an existing dispute at the time the offer is made, and the side making the offer is genuinely trying to settle it. So, 'without prejudice' only works where the employer is either contemplating or might reasonably be contemplating litigation arising from their concerns.

Any discussions prior to this, in which the employer might be suggesting terminating the employment, is not protected by 'without prejudice' and could therefore amount to a dismissal. Evidence of the conversation could be raised in court as evidence of a desire to dismiss and it would be almost impossible for the employer to argue that the dismissal was fair. They would not have carried out any proper procedure, and evidence of what was said could be raised later by the employee in tribunal as evidence of the employer's motives or intention to end the relationship.

It is still possible to conduct 'without prejudice' discussions and negotiations where a lawyer or and Acas are involved, but there has now been a change in the law, making such situations more straightforward. The introduction of 'settlement agreements' enables much earlier discussion about ending the employment without risk to the employer. Acas has a [code of practice](#) and [guidance](#) on settlement agreements; these are referred to in this factsheet as 'the code' and 'the guidance'.

### **Who can make a settlement offer?**

It can be made by either the employer or the employee, although in practice it is most likely to be the employer.

### **When will the employer make a settlement offer?**

These offers are being used widely, but most commonly an offer to settle is made by the

employer where there are concerns about the employee's conduct or performance, or where a redundancy process is pending, and they wish to bring about the end of the employment as quickly and smoothly as possible. Although these are the most common scenarios, an offer can be used to try to bring about a termination of employment in any situation and for any reason (subject to the comments about discrimination later).

The change in the law means that the employer may be able to make an offer before any formal process, such as performance management or disciplinary procedure, has been started, or prior to initiating a redundancy process. It may also be done in response to a grievance. Proposing a settlement agreement may well speed things up and avoid the bad feeling that often results from elongated formal procedures around dismissal or redundancy. It may also be possible for the employer to initiate an Acas early conciliation process to settle the dispute with their assistance. If agreement can be reached, Acas will issue a COT3, which is an agreed settlement protected in the same way as any other settlement agreement. However, the employee is not required to obtain independent legal advice prior to agreeing a COT3 since it has been done under the supervision of an Acas officer, which saves time and expense.

It is worth mentioning that there are several matters that the settlement agreement cannot cover; information and consultation obligations on a TUPE transfer or on a collective redundancy must be compromised by Acas under a COT3, and there was some doubt about whether a COT3 is needed to settle future claims of which an employee is not currently aware and which have not yet arisen. However, in the court of session in [Bathgate v Technip UK Ltd](#), it was decided that if the parties make it clear, all future claims may be excluded as part of a settlement agreement.

However, there is some unhappiness about this decision and, to be on the safe side, legal advisers may well suggest that a COT3 would be the best route for settling any future claims the employee may have against the employer.

### **The form of the offer**

There are no hard-and-fast rules about this, and an offer may be made orally or in writing. Employers are strongly advised to ensure that the offer is made in writing, even if the issue is first raised orally in a meeting with the employee. The guidance suggests that it should be made clear to the employee why the offer is being made, although this is not required by the statute.

The guide provides two template letters that may be used by the employer for this purpose. The first is designed to be used where no formal process has been started; the second is where the employee is already the subject of formal proceedings, such as a disciplinary or performance management process. The letter will need to be modified to indicate whether it is setting out the offer for the first time, or whether it is confirming an offer that has already been made at a meeting between the employer and the employee.

### **The contents of the offer**

Normally, the offer will be of a financial settlement, and most employers also offer an agreed reference. It is important to remember that the reference should be truthful and not misleading. In fact, the offer may contain anything of value to the employee – for example, the writing off of a debt to the employer or the transfer of ownership of a car, phone or a laptop, or a combination of any of those. It is also normal practice for the employer to include payment of the employee's reasonable legal costs in relation to the agreement, although this is not covered by the legislation and is a matter for agreement between the parties.

Confidentiality can also be a consideration in relation to settlement agreements. Employers normally want to ensure that departing employees do not reveal business information to competitors. Likewise, if a payment is made as part of a settlement agreement, employers would not want the terms of that agreement publicised.

## **Considering the offer**

The employee needs to be given sufficient time to consider the offer and to seek legal advice, and the code suggests that this should be at least 10 days. It seems likely that most employers will stick with this time frame unless there are particular reasons for extending it. The period can be shortened by mutual agreement, but this is likely to be only in exceptional circumstances where it is to the advantage of both parties.

The employer needs to ensure that there is provision for at least one meeting at which the offer can be discussed properly, and also potential subsequent meetings if the employee wants more detail or wishes to make a counter offer.

## **The offer as evidence in a tribunal**

The introduction of settlement offers is a great improvement for employers as it means that, where a settlement offer is made and unsuccessful discussions ensue, the employee cannot use the conversation or offer as evidence in subsequent unfair dismissal proceedings. This is subject to the rule about unlawful discrimination explained below. The key point is that it is not necessary for there to be any existing dispute between the parties, and an employer is free to start a discussion at any time.

The law relating to ‘without prejudice’ conversations remains as it was before the new law was introduced. Therefore where, for example, the employee has resigned or has already been dismissed, and solicitors or advisers are involved, the whole process can then be conducted ‘without prejudice’. There is more detail about the without prejudice principle in the guidance, but the rest of this factsheet is confined to settlement offer discussions.

## **The content of the meeting**

The employer should lay out the full offer to the employee, telling the employee precisely what is proposed, and why. They should also make it clear to them that:

- The conversation will not be admissible in any unfair dismissal proceedings.
- The process is voluntary and the employee does not have to take any part in the discussions if they do not wish to, and can withdraw from the process at any time.

- They are to be given a reasonable amount of time to consider the offer, and be told how long the employer is proposing to allow them.
- They are free to turn down the settlement offer.
- They may wish to be accompanied at meetings relating to the offer by a work colleague or trade union official (although this is not a legal requirement).

The guidance recommends that the discussions are conducted by the employer in a sensitive manner, ensuring that the employee is able to air concerns and raise issues, and is given full and informative answers to any questions.

### **Refusal of the offer**

If the employee does not wish to engage in the discussions, or refuses the offer made and no settlement can be negotiated, then they will continue to work as normal. If the employer later chooses to begin a formal procedure such as a redundancy process or a disciplinary or performance management process, which ultimately results in the dismissal of the employee, the settlement offer cannot be produced as evidence in court to support unfair dismissal proceedings.

The employer may wish to bear in mind the impact of unsuccessful negotiations and most employers would want to be reasonably satisfied that the employee is likely to wish to settle. Failed negotiations are likely to sour the relationship and cause friction between employer and employee.

### **Unlawful discrimination**

The protection extends only to claims for unfair dismissal. If the employee believes that the termination of their employment is being sought because of a protected characteristic, ie because of their sex, race, colour, age etc, then the discussion can be brought into evidence in an unlawful discrimination claim. It is very risky to seek a settlement agreement where there is any possibility of such a claim, since if no settlement is reached, the employee will be able to use the conversation as evidence of unfavourable treatment. Unlawful discrimination and the protected characteristics are explained in

### **Other situations in which the protection does not apply**

The employee will still be able to use the settlement offer as evidence in proceedings for unfair dismissal where they allege that the real reason that the settlement is being sought is one that would make the dismissal automatically unfair. These reasons include, for example, that the employee was seeking to join a trade union or was a whistleblower, or was being dismissed for their political opinions. The full list of these particular reasons is laid out in ss98A-101A Employment Rights Act 1996 and on page 23 of the [Acas guidance](#).

The employer also loses the benefit of this protection where there is evidence that there has been some kind of 'improper behaviour' in the way in which the settlement negotiations have been conducted. What constitutes improper is a matter for the employment tribunal in the facts and circumstances of each case. If the employer was guilty of bullying the employee and attempting to intimidate them into signing the agreement, not giving enough time for the employee to consider the offer, or if there was any evidence of physical assault or victimisation, or threats of dismissal if the employee did not sign, there would be improper behaviour. These matters are all discussed in detail in the guidance. It has also been recently established in case law that a settlement agreement may be invalidated if it is induced by a misrepresentation (a false statement of fact) by either party.

### **The settlement agreement**

The settlement agreement itself is a legally binding document by which the employee waives their rights to take any claim against the employer in relation to their employment. This includes unfair dismissal but will ultimately also cover all other types of claims including discrimination, matters relating to wages, redundancy and notice.

In order for the settlement agreement to be valid:

- The agreement must be in writing.
- The agreement must state what claims are being settled, not just that it is in full and final settlement of all claims.
- The employee must have received advice from a relevant independent adviser on the terms and effect of the proposed agreement and its effect on the employee's ability to pursue that complaint or proceedings before a tribunal or court.
- The independent adviser must have a current contract of insurance or professional indemnity insurance covering the risk of a claim by an employee in respect of loss arising from that advice.
- The agreement must identify the legal adviser.
- The agreement must state that the statutory provisions that set out the above conditions regulating the validity of the settlement are complied with.
- Recent case law has established that a valid settlement agreement cannot be made by someone who lacks the mental capacity to enter into it.

The agreement will contain a number of clauses:

- setting out the date of termination of the employment
- setting out the payment, along with the time when payment will be made
- the tax position on those payments (see below)
- any other agreed actions, such as agreement of a reference and transfer of items to the employee
- a list of the actions that are being settled, eg unfair dismissal, redundancy etc
- a declaration for the independent adviser to sign.

It is also likely to contain:

- a confidentiality clause stating that neither party will discuss the agreement with anyone else (see the discussion on reform in this area at the end of this factsheet)
- a clause that states that neither party will make any derogatory statements to third parties about the other.



A model agreement is provided at the back of the guidance, with notes appended to guide employers. As a general rule, it is advisable for employers to seek legal advice when dealing with such matters, to ensure that all the requirements are fulfilled and that the business is properly protected from claims. The model agreements are available in the guidance.

The tax position regarding payments made in relation to these agreements is complicated and depends on the basis for the payment. Broadly, any ex gratia or non-contractual payment in respect of compensation for loss of the position, including a redundancy payment, is tax free up to £30,000. Payments made in lieu of holiday or notice are taxable, as are any payments made in exchange for agreeing to a restrictive covenant. Although detailed tax law is outside the scope of this factsheet, employers settling multi-faceted claims, particularly those with an element of discrimination, may refer to the case of [L v HMRC 2024](#).

All payments in lieu of notice (pilons) are fully taxable regardless of whether there is a pylon provision in the employment contract or not.

In certain circumstances, payment for injury to feelings, which is not related to the termination of employment, can be made tax free, whereas any payment for injury to feelings, which is related to the termination, is taxable in the usual way, subject to the £30,000 tax free allowance. For an example of this, see the case of [Mathur v HMRC](#).

Employer national insurance contributions (NICs) are now payable on the balance of any termination payment above £30,000. Termination payments will remain free of employee NICs.

### **Confidentiality clauses and settlement agreements**

There has recently been considerable concern about the use of confidentiality clauses or non-disclosure agreements (NDAs) – often called ‘gagging’ clauses – in settlement agreements. They seek to prevent the employee revealing any details of the content of the settlement or the reason for it. This has led to a number of victims of serious

harassment feeling unable to disclose anything about what has happened to them, which has resulted in the perpetrator going unpunished. The Equalities and Human Rights Commission (EHRC) published guidance in November 2019, which is not legally binding but which can be used to provide evidence of good or bad practice in the courts and tribunals, so employers and legal advisers will be drafting settlements with the principles in mind. The main points in the guidance include that:

- the employer should make it absolutely clear what is confidential and what is not, rather than using a general catch-all clause.
- The employer must not put the employee under any duress to enter into the confidentiality clause.
- The employer should show that it has continued to deal formally with the allegations being made, and not use the settlement as an opportunity to brush the issue under the carpet.
- The employer should ensure that the employee gets independent legal advice on the clause and should cover the cost of that advice.
- The clause should never be used in a way that is unlawful, eg to silence a whistleblower, or prevent the reporting of a crime or a submission to a regulator.

## **Reform**

The previous government had committed to reform of confidentiality clauses but had only planned to introduce limited reforms prior to losing power in July 2024. Changes to the law that were announced on 28 March 2024, but which were not implemented prior to the change of government, were intended to ensure that victims would no longer be prevented from accessing vital support or legal advice under NDAs or so-called 'gagging orders'.

The government stated that confidentiality clauses, or NDAs, can protect sensitive employment information, yet too often they are misused to silence victims – denying them access to justice or support services to rebuild their lives.

The change to the law was intended to clarify that NDAs cannot be legally enforced if they prevent victims from reporting a crime and would ensure information related to criminal conduct can be discussed with police or legal advisers without fear of legal action. In

February 2025 the government announced that it was considering an amendment to the Employment Rights Bill banning the use of NDAs by employers to ensure they are not used to hush-up cases of sexual harassment or discrimination. It remains to be seen what approach will be taken, and when we have clarity on this the factsheet will be updated.

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