NEGOTIATING AND DRAFTING SETTLEMENT AGREEMENTS*

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Negotiating and Drafting Settlement Agreements

A. Overview

1. The Context of the Settlement

   This section addresses the negotiation and drafting of settlement agreements for employment disputes. Settlements may come from direct negotiations between the parties (or their respective counsel), from mediation, or from negotiations before or during arbitration proceedings. These contexts share many of the same substantive issues, and thus many negotiation and drafting issues are similar. When the context presents special issues, they will be specifically addressed.

2. Severance Agreements

   On termination of an executive’s employment, most employers provide severance benefits, typically in exchange for a release of claims against the employer. Moreover, many employment disputes arise because the employer terminates or threatens to terminate the employment relationship. Some employment disputes—involving current employees—result in a negotiated termination or resignation of employment.

   All of these situations raise severance issues, so they usually result in an agreement containing provisions typically found in severance agreements. Accordingly, this section, in addition to addressing general aspects of settlement agreements, highlights negotiating and drafting issues common in severance agreements.1

3. The First Draft of the Agreement

   It is customary for the employer's counsel to prepare the initial draft of a settlement agreement involving an employment dispute.2 Thus, the executive's counsel is usually in the position of reviewing and responding to a document prepared by the other side. Typically, that initial draft will be one-sided—maybe even outrageously so. Moreover, the executive's counsel has little direct control over the timing of that draft.

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1For further discussion, see Executive Compensation Issues for Emerging Companies.

2Almost invariably, a severance agreement will be drafted by the employer's counsel and presented to the executive (or the executive's counsel).
One way to avoid this situation is for the executive's counsel to take the initiative and prepare the draft agreement. Of course, this results in more work for the counsel, at least initially. Some executive's counsel are more than willing to cede the drafting to the other side, particularly when the counsel is working on a contingency basis. However, ceding control over the first draft allows the employer's counsel to determine when the document is ready, what terms are covered, and what language to use to express the terms.

Preparing the first draft can be a tactical benefit, especially in negotiating terms that were not clearly and completely addressed in the pre-drafting negotiations. Thus, taking the initiative helps ensure a balanced and fair first draft, as well as improving both the substance and the timing of the final agreement.

Typically, once the broad terms of a settlement have been agreed on, the executive is eager to get the paperwork done and receive the settlement proceeds. The employer, on the other hand, has little incentive to expedite the process, unless some external deadline (e.g., a trial date) is imminent. Indeed, employers sometimes prefer to move slowly if for no other reason than to delay writing the settlement check. Thus, in the final pre-drafting stage of negotiations, an executive's counsel should try to get a firm commitment from the other side on the timing of the process, including the date for payment of the settlement proceeds.

To induce the employer to expedite the process, the executive's counsel should try to build financial incentives into the settlement. The most obvious way to do that is to provide for interest on the settlement proceeds at a high rate beginning on a specified date, such as 10 days after the broad terms of agreement are in place. Another approach is to require the employer to deposit the settlement proceeds into an interest-bearing escrow account, held by the executive's or the employer's counsel pending the consummation of the deal, with the interest going to the executive. This approach removes the incentive for the employer to move slowly in writing the settlement check.

4. Reciprocity and Mutuality

After agreement is reached regarding the key financial and nonfinancial terms of a settlement, the executive's counsel should focus on other terms that are sometimes overlooked altogether or overlooked until the executive's tactical leverage is reduced. These terms include a release in favor of the executive, a favorable oral or written reference, a non-disparagement clause in favor of the

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3Employer's counsel will invariably insist on having the employer review and approve the draft before sending it to executive's counsel. Thus, even when the employer's counsel is reasonably prompt in preparing a draft, which is often not the case, the employer's review frequently delays the process longer than the executive and the executive's counsel would like.
executive, and effective enforcement mechanisms for the employer's obligations under the agreement.

A useful tactic for the executive's counsel during negotiations on nonfinancial issues is to insist on reciprocity and mutuality—"what's good for the goose is good for the gander." Once that principle is established, the employer's counsel will be less likely to insist on extreme provisions in the agreement (e.g., an onerous liquidated damages clause), and a balanced settlement agreement is more likely. These issues are addressed in detail later in this section.

B. Severance Agreements—Special Issues

1. In General

As discussed earlier, a severance agreement is a type of settlement agreement. Typically, severance agreements are prepared unilaterally by the employer's counsel and presented to the executive to sign; negotiations over the terms may then ensue. These negotiations may raise some special issues. For example, should the executive negotiate for a better package or agreement? In this case, the answer is generally "yes" (that is, generally it does not hurt to ask).

2. Whether to Negotiate

The answer to the question of whether one should negotiate is "it depends." Frequently, the executive should try to negotiate an enhanced package, with counsel in the background. This approach is less expensive for the executive and is also less confrontational. In addition, it is often far more effective, particularly when the executive's negotiating leverage is based more on personal and political factors than on legal ones. In these situations, direct intervention by the executive's counsel can be counterproductive because it appreciably changes the dynamics of the negotiations, usually precipitating direct involvement by the employer's counsel, who is likely to focus on the legal merits of the executive's position rather than those personal and political factors that better serve the executive's interests.

If the executive is unable or unwilling to negotiate directly or if that approach appears unpromising or has been tried but failed to achieve an acceptable result, then the executive's counsel can step forward to deal directly with the employer or the employer's counsel. Generally, little is lost by trying this incremental approach. Even when it does not work, the executive and the executive's counsel may learn about the strengths and weaknesses of their bargaining position in the process.

3. With Whom to Negotiate

When the executive decides to negotiate directly with the employer,
choosing the person with whom to negotiate is an important tactical decision. Sometimes, the proposed severance agreement or a cover letter specifies who will handle any questions about the agreement. The executive should not feel constrained by that designation since the designated person often is not the best person with whom to negotiate. The executive or the executive's counsel should try to identify someone in the company who has both the power and the inclination to help the executive. Often, the executive is better off negotiating with people in his or her management chain, that is, someone the executive has worked with rather than people in the human resources or counsel's offices. Moreover, the executive generally is better off negotiating with a human resources representative rather than a company attorney.

4. How to Negotiate

A key to any severance negotiation is determining what negotiating leverage the executive has and can use. The amount of leverage depends on the situation. If the executive has a strong (or at least colorable) legal claim, that is critical leverage, although occasionally it pays to hold it in reserve. Absent a legal claim—or before asserting one—the executive can try to “push the buttons” of the employer through people in the company who know and like the executive. The “buttons” include fairness, guilt (a great motivator), fear (of bad publicity, the government, or higher management), and friendship.

An especially powerful button is the desire of many company officials to be perceived as fair and reasonable in the eyes of others, such as other executives, senior executives, directors or shareholders of the company, customers or clients of the company, or people in their industry. With some companies and some employees, these nonlegal factors work, especially for executives. This is especially true when proposed changes will cost the employer little or no money but will help the executive.

5. Standard Severance Policies

Typically, it is harder to negotiate potential changes in the context of a reduction in force. Employers often say they cannot or will not make changes that could undermine the standard package or create a bad precedent. Even in the face of such a mindset, changes can be obtained—even substantial ones—through the creative approaches discussed below.

6. Withdrawal of Offer

Can the employer rescind or withdraw a proffered severance package during any consideration period if the executive asks for more? The answer is generally “yes,” but this rarely happens. An executive's attorney is safe in assuming that the standard package provided under a company policy or an ongoing exit or reduction program will not be withdrawn. Under the OWBPA,
moreover, the employer arguably cannot withdraw the offer during the 21/45 day consideration period.\(^4\) In any event, the consideration period is routinely extended; however, the executive's attorney should be alert to the risk that the employer might not extend it and should get written confirmation of any extension to the extent practicable.

7. **COBRA**

A discharged executive has the right under COBRA\(^5\) to continue group health insurance or medical coverage, at the existing benefit level and rates for up to 18 months after the off-payroll date (up to 29 months if the executive is disabled under Social Security standards). The employer can require the employee to pay up to 102 percent of the cost of continuing this benefit coverage. Nonetheless, employers sometimes will agree to pay all or part of the COBRA premiums for some period of time.\(^6\)

C. **Severance Agreements—Economic Terms**

1. **In General**

Negotiating a severance agreement offers many opportunities to structure the economic terms beyond the mere payment of a lump-sum settlement amount. Some of these approaches can be adapted for use in structuring the economic terms of a settlement agreement in a non-severance situation. Accordingly, those approaches are set forth here.

2. **Severance Pay and Other Cash Compensation**

   a. **Severance Pay Options**

   The basic options are lump sum and salary continuation. Typically, benefits end when a lump sum is paid, and some benefits continue during a continuation period, although exceptions occur both ways. Employers will

\(^4\)But see Ellison v. Premier Salons Int'l Inc., 981 F. Supp. 1219, 1 EXC 397 (D. Minn. 1997) (holding that the 21 day review period is relevant only to the issue of whether an employee's waiver of his or her rights under the ADEA was knowing and voluntary and that OWBPA does not provide for an irrevocable power of acceptance).

\(^5\)29 U.S.C. § 1161 et seq.

\(^6\)Executives should review severance arrangements with their employers under the new health care reform law to ensure that any healthcare coverage provision complies with the new laws. The health care reform law no longer includes an exception to the nondiscrimination requirements of Health Section 125 of the Internal Revenue Code for fully insured group health care policies purchased only for key executives and “preferential” insured health care benefits for former employees after their COBRA continuation period expires. Now, the nondiscrimination requirement, which prohibits discrimination in favor of high-paid employees and those with better health benefits, will apply to both self-insured and fully insured group health plans, and any violations under the latter come with harsh penalties and could lead to civil action against employers. The reform law's nondiscrimination requirement applies only to non-grandfathered fully insured plans and will go into effect Jan. 1, 2012.
sometimes negotiate a switch from one to the other at the executive’s request.

b. Effect of Options

During a salary continuation period, employers often will continue to pay for health/medical benefits on the same terms as during active employment, although the employer can require the employee to pay up to 102 percent of the cost. Employers sometimes will continue other benefits, such as life insurance coverage, pension or 401(k) contributions and accruals, and vesting under stock plans, and so on. Employers generally do not continue disability benefits or vacation and sick day accruals during a salary continuation period, although sometimes vacation accruals can be negotiated.

c. Termination of Severance Pay

An important negotiating point is whether continuation pay will end when the executive gets a new job. Some severance arrangements provide this; such a provision may or may not impose a duty to mitigate on the executive. Other arrangements provide that the executive may choose to cease continuation pay and obtain a lump-sum payment for the balance on starting a new job or merely on request. Of course, if the proposed agreement contains a defeasance or mitigation provision or lacks an option to choose a lump-sum payment, the executive should try to negotiate for a change.

An executive who is concerned about the prospect of running out of severance pay before finding a new job may try to negotiate a trade-off—exchanging a fixed duration of severance pay for a potentially longer variable duration, depending on when the executive gets a job. For example, in lieu of 26 weeks of fixed severance pay, an executive may prefer to receive severance until (and only until) reemployment, which could happen after only 10 weeks or after 40 weeks. In such a situation, the employer will always insist on a time limit and may insist on a duty to mitigate. Sometimes a combination of fixed and variable pay is negotiated, providing a floor and a ceiling.

A modified arrangement sometimes is negotiated to meet the executive’s security objectives (i.e., limiting the risk of missing paydays), while meeting the employer’s concern that the executive will not make appropriate efforts to find a job. For example, under a variable payment arrangement with an outside date, the executive may receive pay until reemployment and then split (e.g., 50/50) with the employer the amount of severance covered by the remainder of the severance period. This shares risks and benefits.

d. Incentive Compensation

Severance pay is typically based on base salary and does not include bonuses, incentive pay, commissions, and so on. Nonetheless, executives
should be alert to opportunities to lay claim to such compensation. Employers will often argue that incentive compensation is discretionary or is not payable to executives who depart before the payment date for such compensation. Sometimes, however, the executive may have been given an oral or written assurance of a minimum or guaranteed bonus (such as in an offer letter). Even without that, an executive may be able to make a strong equitable claim for at least a pro rata bonus. Such a claim can have special merit toward the end of the business year when the compensation would normally be paid, especially if the executive has met most or all of the applicable standards for the extra compensation. Those claims can be quite substantial.

e. Leave Pay

It is always important to ascertain the executive's entitlement, or potential claim, to accrued but unused vacation or other leave pay. Sometimes, the whole year's allotment can be obtained; other times, only the pro rata portion is allowed. The employer's manuals and policies should be consulted and what other executives have received previously should be considered. Increasing the amount of vacation pay is a way to enhance the package without “breaking the mold” of the standard package.

f. Creative Approaches

When an employer refuses to alter a standard severance pay amount or period, executive's counsel should look for creative ways to improve the package “around the edges” while leaving the core intact. Examples of such improvements include the following:

• Defer the effective date of the termination. This could be in the form of a “notice period” or simply continued employment. If the off-payroll date is postponed, the executive gets paid longer before getting the standard package. It may be understood (or better, stated) that the executive will not be expected to perform any or much service during all or part of the extended period, presumably while looking for a new job.

• Add a consulting agreement (discussed later).

• Convert some benefit to cash. For example, if the executive does not need proffered outplacement services, occasionally an employer will allow the cost of that service to be “traded in” for cash; this can be as much as 15 percent of the executive’s salary. Similarly, if the executive does not need medical coverage (e.g., when covered under a spouse’s plan), the cost of such coverage might be traded in.

• Get more money allocated to incentive compensation or to leave pay (see above).
• Agree to a restrictive covenant, such as a covenant not to compete or to solicit customers or employees, which has value to the employer (see below).

• Consider tax issues (see below).

g. Offsets and Clawbacks

In most states, employers are not allowed to offset unilaterally against “wages” any amount that the employer contends the employee owes the employer (e.g., cash advances, loans, alleged thefts). Nonetheless, employers can require an employee under some circumstances to allow an offset as a condition for receiving certain consideration, such as a loan or advance.

In this regard, the executive's counsel should be aware of and investigate whether the executive's compensation and the specific settlement amount could be subject to the employer's clawback policy, if one exists. With recent developments in the regulation of financial institutions and executive compensation, employers are frequently inserting clawback provisions into executive agreements and other executive compensation plans. Clawbacks are contractual provisions that may require an executive to repay compensation following a specific event or trigger and are usually triggered upon an executive's termination of employment, an executive’s misconduct, or an executive's departure and subsequent work for a competitor. In addition to contractually-based clawbacks, certain federal regulations allow clawbacks of executive compensation. Executive's counsel should be aware of these regulations and how they may affect the client's compensation after the separation of employment occurs.

3. Benefits

As discussed earlier, COBRA provides a right to continued medical coverage, and some benefits are commonly extended during a salary continuation period. In any event, as to all benefits, executives should gather all pertinent information as soon as possible, including benefit and account statements, plan documents, summary plan descriptions, and so forth. This is

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7See, e.g., N.Y. Labor Law § 193. [Note, sec. 193 has been amended recently to allow some offsets.]

especially applicable to any severance plan documents. With these documents, the executive and counsel can assess the effects of the severance on those benefits—what is being preserved and what may be lost (e.g., due to inadequate accrual or vesting). This process can identify problems, clarify ambiguities, and locate improvements that can benefit the executive, often without substantial cost to the employer.

Executive's counsel should be alert to the possibility that the employer might be terminating the executive for the purpose of preventing the executive from obtaining a benefit (e.g., vesting in a pension). Although this is obviously hard to prove, such a purpose could violate § 510 of ERISA.9

When the executive is close to, but short of, a date for accruing or vesting some benefit, ways to bridge to that date should be negotiated. This is especially applicable to pensions, 401(k) matching contributions, deferred compensation plans, and stock plans. Ways to do this include getting a longer severance period, spreading the same severance pay over a longer period, getting an authorized leave of absence (i.e., continuing employment status without pay), or getting credit for some prior service with the employer or a predecessor-in-interest.

With respect to nonqualified plans (e.g., some deferred compensation and stock option plans), it may be possible to obtain accelerated or continued accrual or vesting, particularly when the executive was terminated without cause. Sometimes an employer can be persuaded to provide some cash in lieu of a forfeited benefit.

4. Consulting

Sometimes it is advantageous for both the employer and the executive to enter into a consulting agreement after the end of employment. The employer may have continued use for the executive's expertise, contacts, or institutional memory, and the executive can obtain additional income that may not interfere with other employment.

Sometimes, a consulting agreement is a way for the employer to ensure the executive's good will, avoid trade disparagement, or prevent the executive from competing or soliciting clients or employees. A consulting agreement is a way for the executive to obtain more money in exchange for something of real value to the employer, which makes it easier to negotiate.

Sometimes, a "no show" consultancy can be arranged. For example, the

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9Similarly, if an employer terminates an executive for the purpose of preventing the executive from obtaining compensation (e.g., a large commission or bonus), there may be a breach of the implied covenant of good faith and fair dealing. See Wakefield v. Northern Telecom, Inc., 769 F.2d 109, 1 EXC 214 (2d Cir. 1985), subsequent proceeding, 813 F.2d 535 (2d Cir. 1987).
executive may be paid to “be available” or to be “on call.” Obviously, executive’s counsel should be careful to ensure that the agreement is not drafted in a way that imposes real, significant obligations as a condition for payment, if that is not the intent. Otherwise, the employer could stop payments for alleged nonperformance. Consulting agreements are especially useful when the employer does not want to alter a standard package but is otherwise willing to improve the deal.10

5. Attorneys’ Fees

The executive’s counsel should try to get the employer to pay the executive's attorneys' fees for reviewing and negotiating the agreement. Payment of attorneys' fees may be traded off against other amounts that would be subject to employment taxes, thereby saving both parties some taxes. With the passage of the Civil Rights Tax Reform Act in 2004, attorneys' fees associated with a claim for discrimination may be deducted from adjusted gross income (above the line), thus essentially making them fully tax-deductible.11 The definition of “discrimination” for purposes of deductible attorneys’ fees includes most statutory employment rights as well as those under any statute or common law “regulating any aspect of the employment relationship.”12 It is helpful to have the employer write a separate check for the amount of the attorneys’ fees. The employer should issue a Form 1099 to both the executive and the attorney for the amount of the fees; the executive then deducts the full amount from adjusted gross income.

6. Outplacement Services

Some employers offer professional outplacement services. For some executives, particularly those who have not been in the job market for a long time, these services can be very helpful. If this option is not offered and the executive could benefit from it, the executive should ask for it. If the executive does not need or want such outplacement services, the employer may be willing to trade the cost for cash. Some employers refuse to do so, however, taking the position that the outplacement service is offered to help the executive find a new job/career and the executive can take it or leave it.

In the absence of professional outplacement assistance, the executive may ask for and obtain help from the employer in looking for a job. The ability to use a company office, secretarial and reception services, a telephone, voice mail, e-mail, and photocopying and other services can be a substantial benefit,
especially when it helps preserve the appearance that the executive is “looking for a job from a job.” The executive should be aware, however, that sometimes the outplacement provider will monitor communications on its equipment and report to the former employer anything that may violate the separation agreement.

7. **Property and Perquisites**

The executive's counsel should be alert to issues involving personal property, such as the executive's Rolodex (or electronic equivalent), personal papers and files, copies of some “business” documents, and office furnishings. As to documents, ascertain whether a confidentiality agreement is already in place. If so, it may govern the executive's rights to keep, obtain, or use certain documents. Employers sometimes allow executives to keep (or purchase at a reduced price) such company property as the executive's personal office computer, laptop, personal digital assistant, home fax machine, cellular telephone, or even company car.

8. **Unemployment Insurance**

The executive's counsel should always remind the terminated executive of the right to collect unemployment insurance (UI) benefits. Those benefits are not payable until the executive applies. UI benefits are not payable to employees who quit without sufficient reason or are fired for misconduct. The executive and/or his or her counsel should ascertain what the employer will tell the state Department of Labor regarding the termination and have this acknowledged in the agreement. Generally, UI benefits are payable regardless of whether lump-sum or fixed-period severance payments are made but are not payable while the executive is on the active payroll (e.g., during a "notice period").\(^{13}\) It appears that these distinctions are not uniformly applied. If an executive is denied UI benefits improperly, an appeal can be filed. Initial determinations are often reversed on appeal.

9. **Tax Considerations in Settlements**

a. **Background**

Before Aug. 20, 1996, it was sometimes possible to structure and allocate settlements so that some, or all, of the proceeds would not be subject to income taxes, specifically amounts received as compensation for emotional

\(^{13}\) In some states the executive will not be eligible for benefits if he or she continues to receive the full salary and exactly the same benefits that the employer paid while the executive was working if the severance agreement or arrangement between the employer and the executive provides that the salary and benefits will stop when the executive finds work elsewhere. See, e.g., New York State Department of Labor, “Before You Apply For Unemployment: Frequently Asked Questions,” available at http://www.labor.state.ny.us/ui/claimantinfo/beforeyouapplyfaq.shtm#18 (last visited May 9, 2011).
distress under tort or statutory claims.\textsuperscript{14} At that time, I.R.C. § 104(a)(2) was amended to permit exclusion from income only for damages received “on account of personal physical injuries or physical illnesses” (emphasis added). For these purposes, “emotional distress shall not be treated as a physical injury or physical illness,” except to the extent of damages paid for medical care.

Under § 104(a)(2) as amended, the opportunities for tax-free settlement amounts are all but eliminated. The remaining possibilities for tax-free or tax-deferred amounts include:

- damages received on account of physical injuries or illnesses (tax-free);
- damages paid for the costs of medical care (tax-free);
- amounts paid into tax-deferred accounts (e.g., 401(k)s and pension plans) (tax-deferred);
- employer contributions to a “rabbi trust” for the executive’s benefit (tax-deferred);
- structured settlements, with payments made in later taxable years\textsuperscript{15} (tax-deferred); and
- attorneys’ fees paid in connection with “discrimination” claims\textsuperscript{16} (tax-deductible).

\textbf{b. Payroll Taxes}

Amounts received as compensation for interest, emotional distress, or punitive damages, although subject to income taxes, are not wages for purposes of FICA and other payroll taxes and contributions.\textsuperscript{17} Similarly, an amount paid as consideration for cancellation of a fixed-term employment


\textsuperscript{15}Special care must be taken so that settlements are compliant with I.R.C. § 409A. Section 409A provides that parties may elect the amount and timing of a separation payment resulting from an arms-length negotiated settlement in connection with an involuntary termination at any point before the employee obtains a legally binding right to the payment. Treas. Regs. § 1.409A-2(a)(11). Such payments, cannot be used, however, to change the timing or payment form of other deferred compensation payments to which the employee was already entitled.

\textsuperscript{16}The position of the IRS is that the amount of attorneys’ fees paid to the attorney by the employer is taxable income to the employee. \textit{Commissioner v. Banks}, 543 U.S. 426 (2004). With the passage of the Civil Rights Tax Reform Act, however, attorneys’ fees in connection with a discrimination action (broadly defined), paid either directly by the employer or by the employee, are completely excludable from gross income (i.e., an above-the-line deduction) and therefore are no longer taxed. 26 U.S.C. § 62(a)(20).

\textsuperscript{17}Note that a Form W-2 tax report is issued for wages, a Form 1099 tax report is issued for nonwage income, and no tax report is issued for nontaxable payments.
agreement is not considered wages. Thus, for amounts allocated to such nonwage categories, the employer and executive can each save 7.65 percent on income up to $106,800 for 2011 (subject, of course, to the effect of other wages during the year), plus 1.45 percent beyond that amount.

D. Other Severance and Settlement Issues

1. Releases and Waivers

   In the settlement of an employment dispute or when an enhanced severance package has been negotiated, the employer invariably insists on a release of any and all claims and rights by the executive against the employer (and its agents, representatives, successors, assigns, and so forth). Likewise, many employers require such a release as a condition of providing basic and/or enhanced severance benefits. For adequate consideration, such releases are fair and appropriate.

   A waiver that does not conform to the requirements of the OWBPA is ineffective as to ADEA rights. It would still be effective as to all other rights and claims, assuming it is otherwise knowing and voluntary and is not barred by some other statutory provision, such as those relating to minimum wage and overtime pay claims under the Fair Labor Standards Act and workers’ compensation claims.

   Releases included in separation agreements and settlement agreements prepared by employer’s counsel are often unduly broad, perhaps unknowingly. For example, read literally, such releases often would encompass an executive's rights under benefit or compensation plans, vested or otherwise. Such a release would undoubtedly be unenforceable as to vested rights, but the release language should be clarified anyway. Similarly, the release language should exclude the executive’s proprietary interests that may be associated with the employer, such as the executive's interest in investment funds, partnerships, or ventures and any securities or bank accounts the executive maintains with the employer. In any event, the executive's counsel should be sure to exclude specifically from the scope of the release all benefits and rights that should be excluded.

   In appropriate circumstances, the executive’s counsel should try to

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19 In 2011, the FICA tax rate for employees was lowered to 4.20%, while the employer tax rate remained unchanged at 6.2%. The Medicare contribution rate remained at 1.45% for each side.

20 29 U.S.C. § 626(f). As noted above, the OWBPA requires that, for a waiver of ADEA rights to be enforceable, the waiver must meet certain minimum standards, including at least 21 days to consider the agreement (45 days in connection with an exit incentive or employment termination program offered to a group or class of executives); at least 7 days to revoke the agreement after signing; advice in writing to consult with an attorney before signing; and specific mention of waiver of ADEA rights.
exclude from the release whatever existing rights the client has under any company liability insurance policy (e.g., director's and officer's liability) or under company defense and indemnification policies or practices (which often are set forth in corporate by-laws or board resolutions). In the release, the executive’s counsel should be careful not to forfeit reimbursement for business expenses; the executive should submit the expenses and get reimbursed before signing the agreement or at least reserve the ability to submit the expenses for reimbursement.

If the executive expects to preserve any rights under any other agreements or plans, the executive’s counsel should ensure that they are incorporated into or mentioned in the settlement or severance agreement. Otherwise, they could be deemed released, particularly when the agreement has an integration clause.

A release by the employer of any rights and claims against the executive may be desirable or even essential. Employers often resist such releases, especially in a typical severance situation; mutual releases are more common in negotiated settlements of asserted claims. When a release by the employer is agreed to, employers sometimes want an exception for after-discovered claims, such as any claim for defalcation or theft, particularly when the executive's departure was fairly recent. Such exceptions must be narrowly tailored, and the executive's counsel should obtain a representation from the employer that it is aware of no basis for any such claims against the executive.

2. Confidentiality

Employers generally want the terms of a severance package to be kept confidential when an executive gets a nonstandard package. Generally, executives have no real problem with this, as long as they accept the financial terms. Such confidentiality provisions obviously make it harder for other executives (and their attorneys) to learn about enhanced severance terms—which is the whole point, from the employer’s perspective.

The typical confidentiality clause contains some exceptions, but they are usually incomplete. The executive should ask for the following exceptions: (1) the executive's professional advisors (attorney, accountant, financial planner, and so forth); (2) the executive's immediate family (and perhaps other specified family, friends, and so forth); (3) tax and regulatory authorities; (4) any proceeding arising under or pertaining to the severance agreement; and (5) any subpoena or other compulsory legal process (although employers sometimes insist that the executive give prompt notice of any such process received, so the employer can move to quash).

The executive's counsel should be careful about retroactive application of a confidentiality clause, i.e., purporting to proscribe disclosures that the client
may have made before the deal was made. (It is generally a good idea to advise executives to be discreet about settlement talks even before formal agreement is reached.) Also, it is good practice to be careful with any provision that makes confidential the “existence” or “fact of” the severance agreement; generally, try to limit scope to the terms of the agreement, unless a good reason exists for a broader scope. Particularly when the confidentiality clause is very broad, it can be useful to have a “safe harbor” clause, specifying what your client can say safely, if asked what happened (e.g., “we entered into an amicable resolution”). A review of case law reveals that confidentiality clauses are seldom the subject of litigation.

3. References and Non-disparagement

A good job reference can be very valuable to an executive. Forestalling a bad job reference can be even more valuable. An agreed-on reference letter is a good idea. It is often useful for the executive to draft a reasonable proposed letter that the employer should accept and then negotiate from that draft. The agreed-on letter can be annexed as an exhibit to the severance agreement. The letter can have two forms: a “To Whom It May Concern” letter that the executive can use any time and a standard letter to be sent out by the employer in response to any requests.

The content of the letter can also be the script for any oral references given. It is advisable to name specific individuals who are deemed acceptable to respond to any call for a reference and to obtain assurances that no one else will handle such a call. Failing that, it is advisable to reach an agreement in which, in response to any reference request, the employer will state that pursuant to standard company policy it can only confirm limited employment information (such as the last position held and the dates of employment).

Employers often seek non-disparagement clauses in favor of the company (including its officers, agents, products, and services). Executives often accept such clauses, although some limitations may be negotiated (e.g., statements pursuant to subpoena or court order or a “safe harbor” for statements made during job interviews or during legitimate competitive activities). Executives also may seek non-disparagement clauses in their favor. These are broader than provisions limited to job references. Employers sometimes object that a broad non-disparagement clause is impractical and unenforceable as applied to all of the company’s employees. This objection can be countered by having the non-disparagement clause apply to certain categories of executives (e.g., all officers over a certain rank or in a certain division) or to certain named persons.

4. Restrictive Covenants

In some contexts, employers try to include in severance agreements restrictive covenants, such as a covenant not to solicit customers or employees
(non-solicitation), a covenant not to compete for a period of time within certain geographic and/or business parameters (noncompetition), or a covenant not to disclose confidential or proprietary information (nondisclosure). Sometimes, an executive may already be subject to such restrictions contained in prior agreements (such as employment agreements, compensation agreements, and stock or stock option grant agreements), and the employer may ask to confirm their continued validity or to extend their scope. Alternatively, the executive may seek to narrow or eliminate them.

These covenants present obvious limitations on the ability of many executives to earn a living after leaving the employer. A logical argument can be made that such restrictions should not extend beyond the end of the severance pay period in such circumstances. Put another way, severance pay should be paid for the entire duration of any such restrictions.

In most states, noncompetition and non-solicitation covenants are enforceable to the extent that they protect an employer's legitimate protectable interests in trade secrets or confidential or proprietary information and are reasonable in time, place, and scope. Such covenants are treated differently in other states. Some states consider such covenants as promoting public policy and encourage them by statute or common law; other states (like California) consider such covenants to be against public policy and therefore totally or largely unenforceable. In most states, unreasonable provisions can be “blue-penciled” to make them reasonable. Some states declare any unreasonable provision to be unenforceable, without “blue penciling” to preserve reasonable aspects.

One way of handling an employer's legitimate noncompetition or non-solicitation concerns is to be very specific about what is prohibited. For example, the executive may covenant not to solicit named customers or employees for a period of time or not to compete as to named clients or products. A list can be attached as an exhibit to the agreement.

It is important to keep in mind the difference between non-solicitation and non-hire. A clause that prohibits an executive from soliciting co-workers to leave the employer would not prohibit the executive from actually hiring a co-worker who approaches the executive. The same thing applies to customers and clients.21

5. Cooperation

Employers sometimes want to ensure that former executives will cooperate in the future if necessary for a lawsuit, claim, or regulatory matter as to

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which the executive has knowledge. For example, the employer's counsel may want to interview the executive or to have the executive available for an affidavit, deposition, or trial. While the executive is receiving severance benefits, the employer might have some self-help remedies when a former executive fails to cooperate. In any event, an employer may seek a written assurance of cooperation.

If the executive is willing to provide future cooperation, which is typically the case, some ground rules are appropriate. For example, it may be agreed that any cooperation must not interfere unreasonably with the executive's business or personal pursuits or that the executive will be available only outside business hours or up to a certain amount of time; at a minimum, the executive should be required to cooperate only to a “reasonable” extent. Moreover, it is often advisable to negotiate a per diem or per hour compensation arrangement for such services, sometimes with a small amount of time (say, one day) provided free, plus assurance of pay (or reimbursement) for all expenses. In addition, sometimes it is appropriate to seek a commitment that the employer will pay reasonable legal fees incurred by the executive in connection with such cooperation.

6. “Gag” Clauses

Employers sometimes seek to prohibit former executives from providing information to, or cooperating with, regulatory agencies or other persons who might have claims against the employer. For example, a clause might provide that the former executive may not file a charge with the EEOC, may not voluntarily assist the EEOC or any other administrative agency, may not voluntarily appear as a witness or party in any judicial or administrative proceeding in which the employer is a party except at the employer's request, and must notify the employer of any subpoena and cooperate with any efforts by the employer to resist that subpoena.

These clauses present a tension between public policy considerations (i.e., encouraging and facilitating disclosure and investigation of potentially unlawful conduct by employers) and private considerations of the parties (i.e., the desire by an employer to try to ensure complete peace, which an executive may be willing to provide in exchange for appropriate consideration). Because of the public policy considerations, such gag clauses may not be enforceable.22

22 See, e.g., EEOC v. Waffle House, Inc., 534 U.S. 279 (2002) (although an employee signed a predispute arbitration agreement, the EEOC was not precluded from pursuing relief on employee’s behalf because it was doing so to vindicate public interest); Connecticut Light & Power Co. v. Secretary of Labor, 85 F.3d 89, 1 EXC 194 (2d Cir. 1996) (employer's proposed settlement provision, which would have prohibited employee's voluntary appearance as a witness or party against the employer, found to violate the Energy Reorganization Act's antidiscrimination provision); EEOC v. Astra, U.S.A. Inc., 94 F.3d 738, 1 EXC 184 (1st Cir. 1996) (settlement agreement clause that prohibited former employees from assisting the EEOC held to violate public policy); E.E.O.C. v. Morgan Stanley & Co., Inc., 2002 WL 31108179 (S.D.N.Y. Sept. 20, 2002) (releases signed by
7. Applications for Future Employment

Employers sometimes seek to preclude a former executive from ever seeking reemployment with the employer, particularly when the executive has asserted claims against the employer. Some executives object to such a provision, considering it unfair and punitive. The usual rationale for such a provision is that it protects the employer from a discrimination or retaliation claim if it denies the former executive's subsequent application for a job. Typically, executives accept such a provision, although certain exceptions should be considered. For example, it is reasonable to exclude circumstances in which a future employer of the executive is acquired by or merged with the former employer, the executive applies for employment without realizing that the prospective employer is part of the former employer, or the parties knowingly agree to the new employment.

8. Liquidated Damages

Employers sometimes include a provision that the executive will forfeit or disgorge all or part of the severance package (or a certain sum of money) if the executive does certain things (e.g., sues on a released claim or violates a restrictive covenant or confidentiality clause). Obviously, such a provision should be opposed whenever possible and narrowed to the extent possible. In the latter event, it can be argued that a lower amount is sufficient to provide the desired incentive for the executive to comply.

Generally, the executive's risk of forfeiture or disgorgement is not a problem when the triggering event is something well within the executive's control, such as suing on a released claim. A real risk may exist, however, when the triggering event is less readily controllable or identifiable, such as an alleged breach of confidentiality or of a restrictive covenant. One way to limit the risk is to insist that the employer provide advance written notice of any alleged breach and a reasonable opportunity to cure, when it is possible to do so. In addition, making such provisions reciprocal can provide protection for the executive and can result in more moderate terms.

9. Dispute Resolution and Attorneys' Fees

Employers sometimes include a provision that any dispute under a settlement or severance agreement will be resolved through arbitration. Even so, such employers may provide that they reserve the right to go to court to seek injunctive relief for violation of the executive's commitments, such as restrictive

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employees in settlement of gender bias claims and the employer's code of conduct violated public policy because the documents prevent employees from cooperating and communicating with the EEOC).
covenants. Even when the employer does not include an arbitration clause, executive's counsel should consider suggesting one. Arbitration can be an effective, inexpensive, and speedy way of enforcing or defending rights and obligations under a settlement agreement. A provision stating that, before commencing any arbitration or litigation, the parties will enter into direct, good faith negotiations and will try mediation is also advisable.

If the settlement is the result of a mediation process, the settlement agreement should include a provision that, if any disagreement arises regarding the interpretation or implementation of the agreement, the parties and their counsel will discuss the disagreement with the mediator before any legal proceedings are commenced. It is generally in the executive's interest to include a provision that, in the event of a dispute, the arbitrator or court will have the authority to award reasonable attorneys' fees, costs, and expenses to the party that substantially prevails.

10. Conclusion

With careful attention to all aspects of negotiating and drafting the settlement agreement, the executive's attorney can materially advance the client's economic, practical, and legal interests under the final agreement signed by the parties.