# It's Not Boilerplate: Essential (and Nonessential) Terms in Settlement Agreements

**Presenter:**
**GILBERT L. SANCHEZ**
Kemp Smith LLP
221 North Kansas, Suite 1700
El Paso, Texas 79901
gilbert.sanchez@kempsmith.com

**Authors:**
**CLARA B. ("C.B.") BURNS**
**SCOTT W. KENDALL**
Kemp Smith LLP
221 North Kansas, Suite 1700
El Paso, Texas 79901
clara.burns@kempsmith.com
scott.kendall@kempsmith.com

State Bar of Texas
**Labor and Employment Law Institute**
August 23-24, 2019
San Antonio, Texas

# TABLE OF CONTENTS

## I. INTRODUCTION

Once a dispute between an employer and employee has settled, it may be tempting for attorneys to let down their guard when it comes time to draft the settlement agreement. Any attorney who has seen one of their own settlement agreements come back around in subsequent litigation knows that drafting a settlement agreement is not the time to simply go through the motions. Numerous pitfalls await attorneys who do not pay careful attention to each and every paragraph of the settlement agreement. The purpose of this article is to highlight the essential (and nonessential) terms in settlement agreements that every attorney should consider when drafting their own agreement.

## II. OPENING CLAUSES/RECITALS

The opening paragraph and recitals to a settlement agreement are important for purposes of defining the parties and putting the settlement agreement into context.

The opening paragraph should state that the employee and employer have fully and finally agreed to settle all issues, claims, and disputes between them as set forth in the agreement. It should also provide structure for the agreement by creating defined terms to be used throughout (*e.g.*, the "AGREEMENT"; the "COMPANY" or "EMPLOYER"; "SMITH" or "EMPLOYEE"). If multiple related entities have been sued, then those entities should be included as released parties in the settlement agreement. Even if related parties are not specifically sued, generally, "employer" should include parent companies, subsidiaries, and any other related entities to ensure that there is no dispute that those related parties are included in the settlement.

Immediately following the opening paragraph are the recitals, which provide context for the settlement agreement. The first recital should include a description of the lawsuit, charge of discrimination, or other pending claim or issue between the parties that the settlement agreement is intended to resolve.

Another common recital is a denial of liability. When the only claims at issue are against the employer, the recital provides that the employer denies all claims and allegations brought against it in the underlying lawsuit, charge of discrimination, or other pending claim. If there are counterclaims or other allegations against the employee, the recital would also include the employee's denial of liability. Following this recital, the agreement should state that in order to avoid additional time and cost of litigation, the parties have chosen to resolve the underlying lawsuit, charge, or other pending issue by entering into the settlement agreement. Depending on the circumstances, the parties may choose to include additional language that the employer knows of no claim it may have against the employee, and that it has no present intention to file a claim against the employee.

The final paragraph should state that in exchange for the consideration, promises and covenants within the agreement, the parties agree to everything that follows in the agreement.

## III. CONSIDERATION

### A. GENERALLY

A settlement agreement is a contract and as such, must be supported by adequate consideration. Accordingly, the agreement should clearly describe the consideration. As that is usually payment of money, the amount, method, and timing of any payments made to the employee and the employee's attorney (if applicable) should be described. If the consideration is something else, such as a mutual release or an agreement to provide some type of nonmonetary relief, the agreement should describe that. When describing the amounts to be paid, be sure to include the form of payment and whether the payment will be reflected as a 1099 payment, or whether it is subject to withholding and reflected through a W-2. If the settlement agreement provides for attorneys' fees, it is generally more practical, for taxation and record-keeping purposes, that these fees be paid separately to the attorney and not be included as one lump sum paid to the employee. Taxation issues are discussed in further detail, below.

This section also should include a statement that but for the settlement agreement, the employee and his or her attorney are not otherwise entitled to receive the payment described as part of the agreement. This ensures that the

parties understand that the consideration given for the settlement agreement is not something that is otherwise owed to a party. Similarly, the parties should include clarifying language that the consideration does not represent compensation or wages otherwise owed to the employee, and that the employee represents and agrees that he/she has already been paid all compensation or wages owed to him/her.

Finally, the section regarding consideration should address when payment is to be made and delivered to the employee. Certainly, the parties should discuss timing expectations in their settlement negotiations and allow for a reasonable amount of time upon full execution of the agreement to fund the settlement. For settlements that include releases of claims under the Age Discrimination in Employment Act, the timing of the funding of the settlement should take into account the 7-day revocation period (discussed below).

## B. TAXATION

Disputes over taxation issues on settlement payments to be made in employment cases can sometimes hijack the settlement process, so it important that the parties understand this area of the law, and account for it in their settlement agreement.

The Internal Revenue Service ("IRS") has set forth a four-step process for properly determining the income and employment tax consequences, and appropriate reporting of employment-related judgments or settlement payments:

1. Determine the character of the payment and the nature that gave rise to the payment;

2. Determine whether the payment constitutes an item of gross income;

3. Determine whether the payment is wages for employment tax purposes (Federal Insurance Contributions Act ("FICA"), and income tax withholding); and

4. Determine the appropriate reporting for the payment and any attorneys' fees (Forms 1099 or Form W-2).[1]

Generally, most payments made as part of an employment-related settlement will constitute an item of gross income—back pay, front pay, compensatory damages, consequential damages, etc.—paid in settlement for a claim made under an employment-related statute (*i.e.,* Title VII, FLSA, ADEA, etc.).[2] Additionally, an award of attorneys' fees is includible in a plaintiff's gross income. *See Commissioner v. Banks*, 543 U.S. 426 (2005).[3] The types of payments that may normally be excluded from gross income are those received because of personal physical injuries or physical sickness from a tort or tort-like injury. *See* 26 U.S.C. § 104(a)(2).[4] However, damages recovered from an employment-related dispute generally are not recoveries for a personal physical injury.

In addition to determining whether the settlement payment constitutes an item of gross income, the parties must also determine what portion, if any, of the settlement payment constitutes wages for employment tax purposes. In this regard, the parties are responsible for accurately allocating the settlement payment among wages, non-wages, and attorneys' fees. When considering whether to accept an allocation of damages in a settlement agreement, the IRS generally considers: (1) whether there was a bona fide adversarial settlement as to the allocation of payment between types of recoveries; and (2) whether the terms are consistent with the true substance of the underlying claims.[5]

Sometimes, parties seek to have the entire settlement payment be paid as non-wages on a Form 1099 and not subject to withholdings, as that is the simplest way to fund settlement and, at least temporarily, results in a larger settlement check to the employee. However, it subjects both the employer and the employee to substantial potential tax

---

1 *See* Income and Employment Tax Consequences and Proper Reporting of Employment-Related Judgments and Settlements, Office of Chief Counsel Internal Service memorandum, October 22, 2008 ("IRS Settlement Payment Memorandum"), at 2. A copy of this memorandum is attached to this article as Appendix A.

2 *Id.* at 2-3.

3 *Id.* at 6.

4 *Id.* at 4-5.

5 *Id.* at 10-11.

liability. If portions of the settlement proceeds are misclassified as non-wages, the employee will be responsible for all taxes, including the employer's portion. If the employee is unable to satisfy the tax burden of settlement proceeds, the IRS will likely turn to the employer for payment. In addition, if an employer fails to deduct and withhold income tax amounts by treating the employee or former employee as a nonemployee, the employer may be subject to additional liability, penalties, and interest.[6] Thus, it is in all parties' best interest to agree to a settlement allocation that accurately reflects the circumstances and substance of the employment claims settled, and not agree to designate the entire settlement payment as non-wages.

Under the Federal Insurance Contributions Act ("FICA"), social security and medicare taxes are owed on all remuneration paid by an employer to its employees.[7] In addition, employers are required to withhold income tax on remuneration for employment paid to its employees (*i.e.*, wages), and the employer is required to withhold from the employee's pay the employee's half of FICA taxes.[8] The IRS and the courts agree that back pay is wages for FICA and income tax withholding purposes (except where received on account of a personal injury or physical sickness).[9] The IRS and many courts agree that front pay also constitutes wages for FICA purposes, but the Fifth Circuit has ruled otherwise, finding that only the back pay portion of a settlement is considered wages for FICA purposes. *See Dotson v. United States*, 87 F.3d 682, 689 (5th Cir. 1996).[10]

An award of attorneys' fees in a settlement agreement that is identified separately from the back pay and other payments made directly to the employee is generally excludable from wages.[11] However, attorneys' fees are generally considered taxable income to the employee.[12]

Payment for non-economic damages such as emotional distress and mental anguish are not considered personal physical injuries or physical sickness, and are therefore considered taxable income to the employee.[13] However, such damages are not considered wages, and therefore, payment for non-economic damages is not subject to withholdings.[14]

Once the parties determine the character of the payment and the nature that gave rise to the payment, whether the payment constitutes an item of gross income, and whether the payment is wages for employment tax purposes, all that is left is determining the appropriate reporting for the payment and any attorneys' fees. An employer is required to furnish information returns (Form W-2, Wage and Tax Statement) to employees, as well as to the Social Security Administration ("SSA"), that report the amount of wages, withholding and other information. Therefore, an amount paid as back wages to an employee is generally reported by the employer to the employee and to the SSA on a Form W-2. If a portion of a settlement payment is income, but does not constitute wages (e.g., payment for mental anguish), the payment should be reported on a Form 1099. In addition, the employer will need to issue a Form 1099 to both the employee and his or her attorney for the attorneys' fees amount where a separate check is issued to the attorney.[15]

## C. CONSIDERATION OTHER THAN SETTLEMENT PAYMENT AND ATTORNEYS' FEES

Any additional forms of consideration (such as a continuation of benefits or to pay an employee's benefits premiums for a certain amount of time) should be adequately described in the settlement agreement as well.

---

6 *See* I.R.C. § 3509.
7 *Id.* at 8.
8 *Id.*
9 *Id.* at 11.
10 *Id.* at 9.
11 *Id.* at 11-12.
12 *Id.* at 17-18.
13 *Id.* at 4-5.
14 *Id.* at 10.
15 *Id.* at 15-20.

## IV. RELEASE OF CLAIMS / COVENANT NOT TO SUE

### A. IN GENERAL

To ensure that the release is clearly defined and covers all potential claims between the parties, it must be carefully tailored to include the specific claim or claims at issue in the underlying dispute, and broad enough to encompass any other claims that could arise from the dispute giving rise to the settlement agreement.

"In order to effectively release a claim in Texas, the releasing instrument must 'mention' the claim to be released." *Kerlin v. Sauceda*, 263 S.W.3d 920, 931 (Tex. 2008) (quoting *Victoria Bank & Trust Co. v. Brady,* 811 S.W.2d 931, 938 (Tex. 1991)). However, the parties do not need to identify each potential cause of action relating to the underlying subject matter giving rise to the settlement agreement. *Keck, Mahin & Cate v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 20 S.W.3d 692, 698 (Tex. 2000). "Although releases often consider claims existing at the time of execution, a valid release may encompass unknown claims and damages that develop in the future." *Id.*

Therefore, in addition to specifically mentioning the known claim(s) at issue, the release should include all causes of action that the employee (or employer) now has or may have in the future, whether known or unknown, relating in any way to any act or omission of any kind occurring on or before the settlement agreement's date of execution. The release should include general claims arising under contract, tort or common law, and specific claims under all relevant, state and federal employment-related statutes. This includes, but is not limited to: Title VII of the Civil Rights Act of 1964, Section 1981 of the Civil Rights Act of 1866, the Older Workers Benefit Protection Act, Age Discrimination in Employment Act, Chapter 21 of the Texas Labor Code (the Texas Commission on Human Rights Act), Chapter 451 of the Texas Labor Code, the Texas Payday Law, the Equal Pay Act, the Fair Labor Standards Act, the Employee Retirement Income Security Act of 1974, the Civil Rights Act of 1991, the Family and Medical Leave Act of 1993, and the Americans with Disabilities Act of 1990.

It also is helpful to include language to the effect that the employee warrants that he or she does not have pending any other employment-related charges, claims or lawsuits against the employer with any government agency, court or other adjudicatory body, to ensure that the parties have fully disclosed and are fully aware of all claims and have included those claims in the settlement and release. If there are other pending administrative claims, for example, that the parties intend for the settlement to cover, the parties need to address how those pending administrative claims will be dismissed (e.g., the employee will withdraw any open charge of discrimination or request a dismissal, and will agree not to see monetary relief on any such claim).

### B. OLDER WORKERS BENEFIT PROTECTION ACT

If the employee signing the agreement is forty (40) years of age or older and the agreement is intended to settle age discrimination claims, the agreement must include a separate section regarding the Older Workers Benefit Protection Act ("OWBPA") in order to effectively release age discrimination claims under the Age Discrimination in Employment Act ("ADEA").

Pursuant to the OWBPA, an individual may not waive or release any right or claim of age discrimination unless the waiver is knowing and voluntary. A release is not considered knowing and voluntary unless the following are met:

1. The release must be written in a manner calculated to be understood by the employee signing the release, or by the average individual eligible to participate;

2. The release must specifically refer to claims arising under the ADEA;

3. The release must not purport to encompass claims that may arise after the date of signing;

4. The employer must provide consideration in addition to anything of value to which the employee already is entitled;

5. The employee must be advised in writing to consult with an attorney prior to executing the agreement;

6. The employee must be given at least 21 days within which to consider the agreement; and

7. The employee must be allowed 7 days after signing to revoke the agreement;

*See* 29 U.S.C. § 626(f)(1). A release in settlement of a charge filed with the Equal Employment Opportunity Commission ("EEOC"), or an action filed in court, alleging age discrimination under the ADEA is not required to provide for the 21-day consideration period or the 7-day revocation period. *Id.* at § 626(f)(2).

Careful attention should be paid to the language advising the employee to consult with an attorney prior to executing the agreement. Some courts have held that language merely stating that an employee "understands that he should consult with an attorney prior to signing this agreement" is not sufficient to meet the OWBPA's requirements and effectively release all age discrimination claims. *See, e.g.*, g *Williams v. Disco Hi-Tec Am., Inc.*, 2005 WL 2259853, at *4 (N.D. Tex. Sept. 15, 2005) ("The language in the Agreement is passive and does not "advise" Williams to do anything. The language does not "give advice to," "caution," "warn," "recommend," or "inform" Williams to consult with an attorney; it only makes Williams aware of a right that he has, but does not "advise," him to take advantage of, act on, or take any action regarding that right."). Therefore, to satisfy the OWBPA's requirements, the agreement should provide: "[Employee] acknowledges that he/she is hereby advised in writing to consult with an attorney and has been given a fair opportunity to consult with an attorney, prior to the execution of this Agreement."

It should also be noted that although the agreement must expressly state that the employee has 21 days to consider the agreement, the employee may sign the agreement at any time, and does not need to wait the entire 21 days.

## V. DISMISSAL OF LAWSUIT WITH PREJUDICE

To the extent there is a pending lawsuit or charge underlying the settlement agreement, a section should be included obligating the employee to execute and file appropriate settlement documents with the court or applicable government agency dismissing the lawsuit or charge with prejudice. Typically, the parties will include language that this obligation becomes due within a certain number of days after the agreement is executed and/or the employee receives the agreed upon consideration for the agreement.

## VI. NO INTERFERENCE OF RIGHTS

As stated earlier, the agreement should provide that the employee (or employer, if applicable) represents that he or she has not filed or initiated any other lawsuits, claims, charges, complaints, etc. against the employer or with any agency based upon any acts or omissions occurring before the effective date of the agreement.

With respect to lawsuits, claims, charges, complaints, etc. the employee may file after the agreement has been signed, specific language must be included to avoid violations of public policy or any anti-retaliation provisions of federal statutes. The EEOC has consistently taken the position that conditioning settlement on the employee's promise not to file an EEOC charge is unlawful retaliation, in violation of federal employee-rights statutes.[16] It has also said that provisions that limit an employee's right "to testify, assist, or participate in an EEOC investigation are invalid and unenforceable."[17] Continuing with this trend in combatting overly broad releases, in 2013, the EEOC announced new enforcement priorities, vowing to "target policies and practices that discourage or prohibit individuals from exercising their rights under employment discrimination statutes, or that impede the EEOC's investigative or

[16] EEOC, Notice No. 915.002, Enforcement Guidance on Non-Waivable Employee Rights (Apr. 10, 1997), http://www.eeoc.gov/policy/docs/waiver.html ("Agreements that attempt to bar individuals from filing a charge or assisting in a Commission investigation run afoul of the anti-retaliation provisions because they impose a penalty upon those who are entitled to engage in protected activity under one or more of the statutes enforced by the Commission.").

[17] EEOC, Understanding Waivers of Discrimination Claims in Employee Agreements, http://www.eeoc.gov/policy/docs/qanda_severance-agreements.html.

enforcement efforts" such as overly broad waivers and settlement provisions that employees might construe as prohibiting them from filing charges or assisting in agency investigations.[18] Likewise, the Department of Justice, National Labor Relations Board, Occupational Safety and Health Administration, Securities and Exchange Commission, and other state and federal agencies have taken similar positions regarding employees' rights to engage in protected activity through filing charges or complaints, or from participating in investigations and proceedings.

Therefore, although the employee is promising to release all claims against the employer, the agreement must include language that nothing within the agreement affects the employee's right to file charges or complaints with any state or federal administrative agency, or from participating in or cooperating with any state or federal proceeding. This section should also inform the employee that notwithstanding the foregoing, the employee agrees to waive his or her right to recover monetary damages in any charge, complaint, or lawsuit filed by the employee or by anyone else on the employee's behalf, except for payments received from a government agency for information provided to the government agency.

## VII. MEDICARE

As of July 1, 2009, the Medicare, Medicaid, and SCHIP Extension Act of 2007 ("MMSEA") requires liability insurers, including self-insurers, no-fault insurers and workers' compensation insurers to:

- Determine Medicare/Medicaid Status for all claimants; and

- Report to the Centers for Medicare and Medicaid Services ("CMS"), the federal administrative agency responsible for administering Medicare and Medicaid when those claims are resolved.

This mandatory reporting reinforces efforts to ensure Medicare is a secondary payer when other applicable Plans or funds are available.

Whether MMSEA is important to a settlement agreement depends upon whether the alleged claims involve workers' compensation or other physical injury, and/or if the settlement payments are intended to compensate the plaintiff for past or future medical costs. If the settlement is unrelated to workers' compensation or physical injuries, the agreement must only:

- Clarify that there are no outstanding Medicare or Medicaid claims related to the facts or allegations forming the basis of the employee's claims against the employer, and

- State that if Medicare ever were to seek payments from employee, the employee would be required to satisfy those payments from the consideration already provided in the agreement and would indemnify and hold harmless the employer from any additional recovery.

However, if workers' compensation, physical injury, or payments for medical costs are involved, the employer (or the employer's insurance carrier) will need to go through the analysis above and prepare alternative language for the settlement agreement. First, the employer must determine if the plaintiff is a Medicare Eligible Claimant.[19] If so, the employer or other liability insurer (including self-insurers, no-fault insurers and workers' compensation insurers), known as a Responsible Reporting Entity (RRE), is required to report to CMS on every case where payment under a settlement, award, judgment or other payments is made that involves a Medicare beneficiary. If this is the case, language such as the following should be considered for the Agreement:

---

[18] EEOC, Strategic Enforcement Plan FY 2013–2016, http://www.eeoc.gov/eeoc/plan/sep.cfm.

[19] Generally, a Medicare Eligible Claimant is one who: (1) Is receiving retirement benefits from Social Security or the Railroad Retirement Board; (2) Any US citizen claimant 65 years or age or older; (3) A disabled person entitled to SSDI (such as disabled war veterans); (4) Claimant with end-stage renal disease; (5) Anyone who has been assigned a Medicare Health Insurance Claim Number (HICN); or (6) A beneficiaries survivor's claim (wrongful death action).

EMPLOYEE is a Medicare beneficiary. Accordingly, the details of this Agreement, including the identities of EMPLOYEE, his/her attorney, certain personal information about EMPLOYEE, the amount of the consideration herein, the date of the Agreement, and the injuries alleged — may be reported to the Centers for Medicare & Medicaid Services (CMS), as well as certain agent(s) necessary to facilitate reporting to CMS, pursuant to the responsible reporting entity's duty to comply with Section 111 of the Medicare, Medicaid & SCHIP Extension Act of 2007 (MMSEA). EMPLOYEE acknowledges his/her duty to cooperate with EMPLOYER in order to allow the Responsible Reporting Entity to fulfill the obligation to comply with MMSEA. EMPLOYEE agrees to provide EMPLOYER with any and all information necessary for EMPLOYER to comply with MMSEA.

EMPLOYEE agrees to timely [may consider a specific timeframe] provide EMPLOYER with a copy of all letters or other written correspondence from EMPLOYEE or EMPLOYEE's counsel notifying CMS or any other governmental entity that EMPLOYEE's claims or lawsuit have settled. EMPLOYEE and EMPLOYEE's counsel further agree to provide EMPLOYER with all copies of correspondence from and to CMS of the Medicare Secondary Payer Recovery Contractor (MSPRC) relating to conditional payments made by Medicare associate with EMPLOYEE's injuries and/or treatment. Once this Agreement is finalized and signed by EMPLOYEE, EMPLOYEE or EMPLOYEE's counsel will deliver to EMPLOYER a Final Determination letter (FD) issued by CMS/MSPRC regarding satisfaction of all conditional payments within five (5) days of the FD being received by EMPLOYEE or EMPLOYEE's counsel. As to future medical payments, EMPLOYEE and EMPLOYEE's counsel agree that it is EMPLOYEE's sole and continuing responsibility to maintain an accounting of all medical expenses relating to this claim or lawsuit, and sufficiently set aside and administer such funds for future medical expenses to protect Medicare's interests against future payments for medical expenses relating to this claim or lawsuit.

EMPLOYEE further represents and warrants that all bills, costs, or liens resulting from or arising out of EMPLOYEE's alleged injuries, claims or lawsuit are EMPLOYEE's responsibility to pay. EMPLOYEE agrees to assume responsibility for satisfaction of any and all rights to payment, claims or liens of any kind, that arise from or are related to payments made or services provided to EMPLOYEE or on EMPLOYEE's behalf EMPLOYEE agrees to assume responsibility for all expenses, costs or fees incurred by EMPLOYEE related to EMPLOYEE's alleged injuries, claims or lawsuit, including, without limitation, all Medicare conditional payments, subrogation claims, liens or other rights to payment, relating to medical treatment or lost wages that have been or may be asserted by any health care provider, insurer, governmental entity, employer or other person or entity. Further, EMPLOYEE and EMPLOYEE's attorney will indemnify, defend and hold harmless from any and all damages, claims and rights to payment, including any attorneys' fees, brought by an person, entity or governmental agency to recover any of these amounts.

## VIII. WAIVER OF REINSTATEMENT AND FUTURE EMPLOYMENT

Because of the strained relationship between the parties and to avoid the potential of any future claims, employers (in particular) often want to include a provision in the settlement agreement wherein the employee waives any right to reinstatement or future employment with the employer, and agrees to not seek re-employment with the employer.

There have been instances in which the legal validity of such language has been challenged as retaliatory, but most courts have found that an employer may use a waiver of reemployment or reinstatement as a basis for a non-discriminatory or non-retaliatory reason not to rehire an employee who previously raised claims against the employer. For instance, the Tenth Circuit has found that "[i]f the [employer] refused to consider plaintiff for future employment because she brought a Title VII claim that the agency had to settle, the agency would be in violation of Title VII. If, however, the agency relied not on the fact that it settled plaintiff's Title VII claim, but on the terms pursuant to which the claim was settled, it did not necessarily violate Title VII." *See Jencks v. Modern Woodmen of*

*America*, 479 F.3d 1261, 1266–67 (10th Cir. 2007); *Kendall v. Watkins*, 998 F.2d 848, 851 (10th Cir. 1993). *See also Franklin v. Burlington N. & Santa Fe Ry. Co.*, 2005 WL 517913, at *4 (N.D. Tex. Mar. 3, 2005) ("An employer's adverse employment action that relies only on the fact that a claim was settled may violate Title VII, but an employer's reliance on the terms on which the claim was settled does not necessarily violate Title VII.").

To further bolster the legitimate, non-discriminatory or non-retaliatory reason for not re-hiring the employee in the future, the parties may want to consider adding additional language, such as an acknowledgement that the clause is being included "because of the strained relationship of the parties" and that the settlement agreement constitutes a legitimate, non-discriminatory, and non-retaliatory reason for not re-hiring the employee.

## IX. CONFIDENTIALITY

Confidentiality is generally a crucial term of a settlement agreement. A confidentiality clause is necessary to ensure that the employee and employer, as applicable, agree not to disclose, directly or indirectly, the terms and conditions of the settlement agreement and potentially spur up additional claims. This paragraph should include language that the parties agree that the settlement negotiations and the terms of the settlement agreement are confidential and will not be disclosed or discussed by the party with any person, entity, or organization other than specifically identified individuals, which can be the employee's spouse the parties' attorneys, accountants, tax preparers. The agreement should, however, clarify that if a party is required by law or court order, to disclose any of the terms, the party is not in breach by following the law or court order. With respect to those individuals who can be informed of the settlement terms, the agreement should provide that the parties are responsible for informing them of the confidential nature of the settlement terms.

In light of the recent #MeToo movement, non-disclosure/confidentiality provisions contained in settlement agreements relating to claims of sexual harassment have new implications. Section 13307 of the Tax Cuts and Jobs Act signed by President Trump on December 20, 2017 states that no tax deduction is allowed for any settlement or payment related to sexual harassment or sexual abuse if the settlement or payment is subject to a nondisclosure agreement. *See* 26 U.S.C.A. § 162(q). Moreover, numerous states have introduced legislation seeking to prohibit non-disclosure/confidentiality provisions altogether when used in the context of settling claims for sexual harassment or sexual abuse. Although no such legislation has been introduced or passed yet in Texas, this is one area of the law that is rapidly changing and worth keeping an eye on.

Finally, because damages are often difficult to prove in the event the confidentiality provision is breached, parties may elect to include a specific amount of liquidated damages to be paid in the event of a breach. Parties who wish to include a liquidated damages provision must be careful to not make this amount too high so as to render the provision unenforceable. *See Valence Operating Co. v. Dorsett*, 164 S.W.3d 656, 664 (Tex. 2005) ("Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss." (quoting Restatement (Second) of Contracts § 356 (1981)); *Phillips v. Phillips*, 820 S.W.2d 785, 788 (Tex. 1991) ("In order to enforce a liquidated damage clause, the court must find: (1) that the harm caused by the breach is incapable or difficult of estimation, and (2) that the amount of liquidated damages called for is a reasonable forecast of just compensation.").

Alternatively, parties may consider providing separate consideration for the promise to keep the terms of the settlement agreement confidential.

## X. NON-DISPARAGEMENT / NEUTRAL REFERENCE

Parties often seek to include nondisparagement language that precludes parties from making publicly disparaging comments about the other that would harm their reputations. With respect to the employee, this is not a difficult burden, as the individual employee simply agrees not to make disparaging comments about the employer. However, when the employer agrees to nondisparagement, it can be more complicated because the employer could breach this provision if its employees were making disparaging comments about the plaintiff-employee. Accordingly, consideration needs to be given to how to reasonably limit the employer's obligations. For example, the parties can agree that specific management employees, such as the employee's supervisors/managers and/or human resources

personnel, are prohibited from making disparaging comments. Or, the language of the agreement can require the employer to "instruct" certain employees of the nondisparagement obligations.

This agreement also should address any negotiated obligation regarding references. Generally, the best and most acceptable stance for both sides is to identify in the agreement a specific source to be contacted regarding employee references (*e.g.*, the human resources department). The parties should also determine what type of information can be provided in response to a reference request. Pursuant to Texas Labor Code §§ 103.001 – 103.005, an employer who discloses information about a current or former employee is immune from civil liability for that disclosure or any damages proximately caused by that disclosure unless it is proven by clear and convincing evidence that the information disclosed was known by that employer to be false at the time the disclosure was made or that the disclosure was made with malice or in reckless disregard for the truth or falsity of the information disclosed.

Regardless of the protections provided by this statute, employers are generally reluctant to disclose too much regarding a former employee's employment for fear of defamation or other claims if negative information is revealed. Accordingly, and commonly, the parties agree that the employer will provide only a neutral employment reference that includes objective, verifiable information such as the employee's dates of employment, the last position held, and the final rate of rate.

## XI. NON-ADMISSION

It is important for the agreement to include language stating that the employee acknowledges that the employer has not admitted to have acted wrongfully with respect to the employee (and vice versa, if applicable), and that the employer specifically disclaims any liability to or wrongful acts against the employee. In the event the settlement agreement is ever permitted by a court to be considered as evidence, this clause will refute any inference that the employer, by settling with the employee, admitted to any wrongful conduct.

## XII. PERSONS BOUND BY RELEASE/NON-ASSIGNMENT AND INDEMNIFICATION

To ensure that the claims covered by the settlement agreement have not been assigned to any other party, the employee and employer, if applicable, should acknowledge that they have not assigned or given any such claim to any person or entity. Further protection should include an indemnification provision, so that if someone does pursue a released claim on, for example, the employee's behalf, the employee in that case will indemnify and hold harmless the employer from any such claims.

## XIII. SEPARABILITY AND GOVERNING LAW

The agreement should state that if any section or clause of the agreement is found unenforceable, then it should be severed and the remainder of the agreement should be enforced, with the exception that if the section containing the release is found unenforceable, then the agreement becomes void and any party that received consideration must immediately return all such consideration provided. Finally, this paragraph should identify what state's law applies (*e.g.*, Texas) to the agreement. The parties may also want to include a venue provision.

## XIV. TAX CONSEQUENCES

The parties need to address any tax consequences in the agreement. Typically, the employer should not be making tax representations to the employee (or vice versa) and the agreement should acknowledge that no such advice or representations are being made, and also should include language regarding any indemnification obligations regarding a party's failure to properly comply with relevant tax laws.

## XV. ENTIRE AGREEMENT

As with any other contract, the settlement agreement should contain what is often referred to as a "merger clause" or "integration clause"—a statement that the parties agree that the settlement agreement contains the entire understanding between the parties, that it supersedes all prior agreements relating to the subject matter of the

settlement agreement, and that the parties acknowledge that they have not relied upon any other written or oral statements or agreements made outside of the agreement. This paragraph should also include a statement that the settlement agreement cannot be modified unless agree to in writing by both parties.

## XVI. CONSTRUCTION

As a canon of construction, courts will often construe ambiguous provisions against the drafter of the agreement, particularly when the drafter has greater bargaining power. To protect against this from affecting either party, the settlement agreement can include language stating that the agreement should be construed as a whole, that the agreement was not drafted by a single party, and that it should not be strictly construed for or against either party.

## XVII. OTHER ACKNOWLEDGEMENTS

The agreement also can include other helpful acknowledgments:

- The parties have carefully read the entirety of the agreement;
- The parties (and particularly the employee) have been given a fair opportunity to discuss and negotiate the terms of the agreement with the assistance of legal counsel
- The parties (and again particularly the employee) have been given a fair and reasonable time within which to consider the agreement before signing;
- The parties understand the provisions of the agreement; and
- The parties (particularly, the employee) are entering into the agreement voluntarily and knowingly.

## XVIII. EFFECTIVE DATE

In most cases, the agreement should become effective when it has been fully executed by both parties. However, if the agreement includes a release of ADEA claims under the OWBPA, then it will not become effective until the seven-day revocation period has passed.

## XIX. EACH PARTY TO BEAR THE PARTY'S OWN ATTORNEYS' FEES AND COSTS

Generally, the parties are going to negotiate a settlement amount that includes attorneys' fees. To ensure that this is the intent, the agreement should contain an express statement that each party to the agreement shall bear that party's own costs and attorneys' fees in connection with the underlying dispute and the preparation of the settlement agreement.

## XX. SIGNATURE PAGES

Certainly, the settlement agreement should be signed by each party. The parties may also want to require notarization of the signatures to avoid claims that any signature is forged or is otherwise invalid.

## XXI. CONCLUSION

This article is not meant to be an exhaustive treatment of every paragraph that should be included in every employment-related settlement agreement. Although there are certain provisions that should always be included, there is no such thing as a "one-size-fits-all" settlement agreement. Therefore, this article should be used as a guideline for attorneys who draft employment-related settlement agreements and want to make sure they have considered including the essential (and nonessential) terms that are often included.