



## **Employers Should Limit Risk with Severance Agreements**

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Layoffs and employee terminations are a necessary part of doing business, especially in the current economy. If you run a business and find yourself in the position of having to terminate an employee, you should seriously consider limiting your risk with a severance agreement.

A severance agreement is a contract between a departing employee and the employer. In the typical severance agreement, the employee promises not to sue the employer, waives and gives the employer a full release for any claims that may have arisen during the employment relationship. In return, the employer agrees to give some type of additional consideration (payment of money) to the employee.

California law does not require an employee to provide a severance package to a terminated employee. However, by providing a severance to the employee and obtaining a release of the employee's actual or potential claims, you can drastically reduce your exposure and the chance for a wrongful termination lawsuit.

Wrongful termination claims usually result in the employer paying monetary damages to the employee based on the terminated employee's lost income and other expenses. Some wrongful termination claims include claims for emotional distress damages, as well as "statutory penalties" which are assessed in accordance with a federal or state regulation. Wrongful termination claims can even include allegations of malicious conduct on the part of the employer which would give rise to punitive damages.

Given the amount of damages an employee might seek in a wrongful termination case, and the fact that lawsuits are costly and time consuming to defend, an employer should consider negotiating a severance agreement with a terminated employee to limit the employer's risk.

There are a number of factors to evaluate when considering use of a severance agreement:

- 1) **Be Careful with Negotiations:** You cannot force an employee to sign a release or enter into a severance agreement. Releases which are obtained through coercion or fraud are invalid. To be effective, the employee must sign the severance agreement voluntarily. To make it clear that the release was freely given, you should give the employee plenty of time to consider the release. You should also advise the employee to have his or her own attorney review the release before it is signed.
- 2) **You Must Pay Additional Consideration:** It is illegal for an employer to ask an employee to release rights in exchange for payment of money that is already owed to the employee, such as earned wages, bonuses or accrued vacation. In fact, failure to promptly pay all wages due upon

termination can result in fines called “waiting time” penalties equal to one day’s compensation for every day payment is delayed up to thirty days. Thus, you will have to give the terminated employee additional consideration above and beyond wages and benefits already owed (such as two weeks’ additional pay or continuation of health insurance benefits), to obtain a valid release.

3) **Special Rules Apply to Employees Over 40:** The Older Workers Benefit Protection Act provides special rules employers must follow in seeking a release or waiver of age discrimination claims from employees who are over 40 years of age. For example, an employee must be given 21 days to consider the waiver, and must be given 7 days to revoke the waiver after it is signed. Additionally, the waiver must also be written in understandable language and the employee must be advised to consult with an attorney before signing it.

4) **Confidentiality:** Most employers will want to keep the severance agreement confidential so other employees will not learn of it and automatically seek their own severance payment upon termination. Accordingly, the employer should put a confidentiality provision in the severance agreement. To guarantee compliance with the confidentiality provision, the employer may consider a "liquidated damages" provision that specifies an amount of money the employee will have to pay if she breaches the confidentiality agreement.

5) **Other Considerations:** The severance agreement should discuss a number of other things such as if employment references will be provided. It should also address the return of the any company or intellectual property in the employee’s possession such as computers, customer lists or trade secrets. The agreement should discuss the tax treatment of the severance payment, which is typically subject to standard federal and state withholdings.

Employers can take precautionary measures to reduce exposure to wrongful termination claims. A simple way to do this is through effective use of severance agreements. Because there are a number of factors to consider in any severance agreement, you should consult with your employment attorney regarding your particular situation.