

SETTLEMENT AND SEPARATION AGREEMENTS

S 1

How to use a settlement agreement to resolve a workplace dispute

This chapter explains how to use settlement agreements and what provisions you should include when negotiating a settlement agreement.

| | |
|--|--------|
| Why you might consider making a settlement agreement..... | S 1/3 |
| Why might you use a separation agreement? | S 1/3 |
| What claims does a separation agreement protect against? | S 1/4 |
| Why might an employee accept a separation agreement? | S 1/4 |
| How to negotiate a separation agreement with an employee..... | S 1/5 |
| Checklist: What to include in a separation agreement..... | S 1/6 |
| Payments made under a separation agreement..... | S 1/7 |
| Should you provide references for the employee in the separation agreement? | S 1/7 |
| Recording the terms of a separation agreement | S 1/8 |
| Is the separation agreement legally binding? | S 1/8 |
| Are verbal separation agreements legally binding? | S 1/9 |
| Recording a separation agreement in a deed of release..... | S 1/10 |
| Can you enter into a separation agreement after the employee has been dismissed? | S 1/11 |
| When can a separation agreement be ruled void? | S 1/11 |
| How long should you give an employee to consider a separation agreement? | S 1/12 |
| Did the employee enter into the agreement under duress?..... | S 1/12 |
| When will a 'take it or leave' offer breach the FW Act? | S 1/13 |
| Is the meaning of the separation agreement unclear? | S 1/13 |
| Was the employee in a position to decide what was in their best interests? | S 1/14 |
| What if an employee makes an unfair dismissal claim despite the separation agreement? | S 1/15 |
| Checklist: How to determine whether a separation agreement can be legally enforced..... | S 1/15 |

TEMPLATES AND SAMPLES

| | |
|---|--------|
| Template: Informal Separation Agreement | S 1/17 |
| Template: Formal Separation Agreement..... | S 1/18 |

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INDEX

| | | | |
|------------------------|--------|---|--------|
| deed of release | | - legally binding | S 1/8 |
| - definition..... | S 1/10 | - verbal..... | S 1/9 |
| ex gratia benefit | | - ruled void | S 1/11 |
| - definition..... | S 1/4 | - unclear..... | S 1/13 |
| in-principle | | - enforceable | S 1/15 |
| - definition..... | S 1/8 | - Template: Informal Separation Agreement | S 1/17 |
| separation agreement | | - Template: Formal Separation Agreement | S 1/18 |
| - definition..... | S 1/3 | settlement agreement | |
| - protection..... | S 1/4 | - definition..... | S 1/3 |
| - negotiating | S 1/5 | - separation agreement | S 1/3 |
| - what to include..... | S 1/6 | without prejudice | |
| - payments | S 1/7 | - definition..... | S 1/5 |
| - references..... | S 1/7 | | |
| - recording..... | S 1/8 | | |

For further references to these terms, please refer to the full word index.



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WHY YOU MIGHT CONSIDER MAKING A SETTLEMENT AGREEMENT

You might consider making a settlement agreement if you think it can prevent or resolve a dispute that might lead to legal liability.

Definition: Settlement Agreement

A settlement agreement is an agreement in which all parties agree to settle all claims and matters between them. It is designed to settle a legal dispute before it goes to court.



Settlement agreements allow you to confidentially resolve disputes with your employees without admitting fault.

If an employee consents to a settlement agreement, they are giving up their rights to make any future legal claim in respect of the dispute, e.g. unfair dismissal.

Important: A common type of settlement agreement – a separation agreement – provides the agreed terms on which an employee ceases their employment.



Definition: Separation Agreement

A separation agreement is a type of settlement agreement under which the employer and the employee mutually agree to go their separate ways and to settle all matters between them.



Tip: *This chapter will mainly focus on the use of separation agreements as a means of avoiding disputes.*



WHY MIGHT YOU USE A SEPARATION AGREEMENT?

Dismissing an employee can lead to legal claims, such as unfair dismissal or adverse action claims. These claims can also arise if an employee feels they have no choice but to resign due to an employment dispute, i.e. constructive dismissal. Employing separation agreements can mitigate the risk of these legal claims arising.

You can avoid a legal claim if you offer the employee a separation agreement, provided:

- any investigation being undertaken into the employee's conduct or performance is fair;
- you give the employee reasonable time to consider the offer and take advice about it (see page S 1/12); and
- the employee accepts the offer and voluntarily resigns.



Caution: Some separation agreements also include a clause that releases the employee from any future liability or claims by the employer. Be cautious about including such a provision. Make sure the separation agreement is confined to matters you know about.

WHAT CLAIMS DOES A SEPARATION AGREEMENT PROTECT AGAINST?

A separation agreement will typically cover all types of claims that can be made relating to the employee's employment, e.g. unfair dismissal or breach of contract.

However, an employee could still make a complaint to an independent regulator, i.e. Fair Work Ombudsman (FWO), that may make a claim on its own behalf.



Important: Employees are protected under statute from giving up their legal right to pursue superannuation and workers' compensation claims.

WHY MIGHT AN EMPLOYEE ACCEPT A SEPARATION AGREEMENT?

An employee might accept a separation agreement due to the ex gratia benefit attached to it.



Definition: Ex Gratia Benefit

In the context of settlement agreements, an ex gratia benefit is a benefit that the employer does not have to give to the employee, but has chosen to give on the condition that the employee enters into the settlement agreement.

Caution: Generally, you cannot ask an employee to give up their legal rights in exchange for something to which they are already entitled, i.e. their employment entitlements. A separation agreement will only be valid if it offers an ex gratia benefit, monetary or otherwise, on top of the employee's lawful entitlements.



An employee may also accept a separation agreement if you give them the option to resign as an alternative to having their employment terminated. This is beneficial to the employee as it allows them to tell potential employers that they left their position with you voluntarily, which improves their chances of future employment.

Resigning rather than being fired can also be more favourable when applying for some financial services, e.g. loans.

Tip: *The purpose of a separation agreement is to try to avoid legal proceedings. For this reason, you may want to consider including a more generous offer in the separation agreement than you would be likely to make if legal proceedings were commenced against you.*



Important: If you do not give the employee significant ex gratia benefits as part of the separation agreement, it is unlikely that you will be able to enforce any post-employment restraint clauses included in the agreement.



Please refer to restraint clause in the word index for more information.

HOW TO NEGOTIATE A SEPARATION AGREEMENT WITH AN EMPLOYEE

When you begin negotiating a separation agreement with an employee, make it clear that any settlement you propose is being made 'without prejudice'.

Definition: Without Prejudice

Without prejudice is a legal term that means the details of the discussion between two parties cannot be mentioned in court if the negotiations break down and the dispute results in litigation.



The aim of ‘without prejudice’ discussions is to encourage parties to make genuine attempts to settle disputes without fear of their discussions being disclosed in court. While this will not always stop the dispute going to court or tribunal, it will:

- support your intention that the discussions between you and your employee are confidential; and
- indicate that you do not necessarily wish to be bound by the terms of the separation agreement.



Important: You can only claim that communication you had with an employee is without prejudice if you keep the communication confidential.



Caution: It is best to assume that anything you say while negotiating a separation agreement with an employee could end up before a court or tribunal.



CHECKLIST: WHAT TO INCLUDE IN A SEPARATION AGREEMENT

A typical separation agreement includes:

- ☐ The date when the employee’s employment will end.
- ☐ A sum to be paid to the employee that includes:
 - an amount in lieu of notice;
 - an ex gratia benefit; and
 - a redundancy payment, if relevant.
- ☐ Any unpaid wages or accrued leave entitlements to be paid to the employee.
- ☐ A clause stating that the employee agrees not to make any future legal claims against you.
- ☐ A clause stating that neither you nor the employee will criticise one another.
- ☐ A clause stating that the employee will not disclose the terms of the agreement to anyone except for specific purposes, e.g. for legal or accounting reasons.

A typical separation agreement includes these things

Tip: *In some cases, it may also be appropriate for the separation agreement to make arrangements for the administrative aspects of the employee's departure, e.g. the manner and content of the departure announcement.*



See pages S 1/17 and S 1/18 for separation agreement templates.

PAYMENTS MADE UNDER A SEPARATION AGREEMENT

Redundancy payments and resignation payouts are taxed differently, so the total amount an employee receives under a separation agreement may vary depending on how the agreement is drafted.

If you and the employee agree to treat the termination of employment as a redundancy, the separation agreement should not refer to the employee resigning or to any arrangement by which the employee provides services to you after the termination date, e.g. if you and the employee have plans for the employee to provide services under a consultancy arrangement in the future.

Take tax into consideration when drafting an agreement

Please refer to redundancy and resignation in the word index for more information.

SHOULD YOU PROVIDE REFERENCES FOR THE EMPLOYEE IN THE SEPARATION AGREEMENT?

Think carefully before you agree to provide the employee a reference within a separation agreement.

Important: If you do include a reference as part of the separation agreement, make sure it is not made on behalf of your company as a whole.

A reference should be made on a personal basis by an individual manager who has dealt closely with the employee in the past and consents to being a referee.

The separation agreement should also stipulate which member of your company will deal with external queries about the ex-employee.



RECORDING THE TERMS OF A SEPARATION AGREEMENT

Once you have determined the terms of the separation agreement, it needs to be recorded.

The terms of a separation agreement can be recorded:

- informally; or
- in a formal document.



Tip: *A formal document might be appropriate if you think you might be facing significant legal exposure.*

Alternatively, you may decide to introduce the proposed terms of the separation agreement to an employee on an in-principle basis in an informal document, and then record the terms in the more formal document once an in-principle agreement is reached.



Definition: In-Principle

In-principle means the parties have reached an agreement about the important terms of the agreement with an intention to replace it with a more comprehensive document later.

IS THE SEPARATION AGREEMENT LEGALLY BINDING?

Whether a separation agreement is legally binding depends on what a reasonable person would conclude was your and the employee's intention.



Example

Mary starts an unfair dismissal claim against her former employer, Sharon. Sharon and Mary attend an FWC conciliation meeting and agree to settle the claim. Sharon's lawyer puts together a deed of release recording the terms they agreed on. However, when Sharon emails it to Mary, Mary refuses to sign.

The FWC will look at what was said at the conference to rule one of three ways:

1. *The agreement between Mary and Sharon is already binding because they made a formal separation agreement at conciliation, even though Mary had not signed the deed of release.*
2. *Mary and Sharon made a binding separation agreement, and both Mary and Sharon must sign the deed. However, Mary can refuse to sign the deed if it does not accurately record what they agreed on at the conference.*
3. *Mary and Sharon reached a mutual understanding about the terms of a deed of release, but there is no binding agreement unless the deed is signed, and neither party is legally required to sign it.*

Example:
Is a verbal agreement legally binding?

ARE VERBAL SEPARATION AGREEMENTS LEGALLY BINDING?

Important: Separation agreements do not have to be in writing to be legally binding.

Whether a verbal separation agreement is legally binding depends on the circumstances surrounding the making of the agreement. The key issue are whether you and the employee intended to be legally bound by the terms. Both parties need to understand and be aware that there is intention to create an agreement.

Example

Reaching a verbal agreement during an FWC conciliation conference has been held to be binding on the basis that the words and conduct of the parties reasonably inferred an intention to be bound.

Case Law

In Csontos v QT Hotels & Resorts Pty Ltd (2016), the applicant refused to sign a settlement agreement or discontinue his unfair dismissal application, even though the matter had been resolved at conciliation and the employer had paid the settlement amount to him.



The applicant sought an additional payment or he would continue with the unfair dismissal application. He did not think he was bound by the terms of the agreement, as it was never in writing.

The FWC said the evidence showed that the applicant understood he had made a verbal agreement during the conciliation conference. Although the applicant subsequently wished to renege on the agreement and have his claim determined, the FWC held that the legal effect of that verbal agreement was that the parties had settled the matter.



Caution: Where a conference is conducted by the FWC in an application for unfair dismissal, unrepresented employees are subject to a 3-day cooling off period. This means that even if a verbal agreement was validly entered into, it can be withdrawn by the applicant at any time within the 3-day period.

RECORDING A SEPARATION AGREEMENT IN A DEED OF RELEASE

Sometimes a separation agreement is recorded in a deed of release.



Definition: Deed of Release

A deed of release is a formal document in which the employee agrees to give up their rights to sue their employer for anything relating to their employment (except rights under workers' compensation legislation or compulsory superannuation contributions, which cannot be given up).

In most cases, it is not necessary for a separation agreement to be recorded in a deed. However, if it is recorded as a deed, it will need to be executed in accordance with the employer's internal rules and constitution (if the employer is a company), or the rules of association (if the employer is an incorporated association).



Important: The deed of release must be signed according to strict procedures.

The rules for making a deed vary according to:

- the State or Territory where the deed is prepared; and
- whether it is prepared by a company or individual.

Tip: *Should you wish to use a deed of release, seek legal advice about the rules that will apply to your business in your jurisdiction.*



CAN YOU ENTER INTO A SEPARATION AGREEMENT AFTER THE EMPLOYEE HAS BEEN DISMISSED?

You can make a separation agreement with the employee after you have dismissed them, provided they agree.

Example

Jack dismisses Sam, who then makes an unfair dismissal claim. At the conciliation conference, Jack and Sam sign a separation agreement that includes the following provisions:



- *Jack makes an ex gratia payment to Sam;*
- *Jack revokes Sam's dismissal;*
- *Sam resigns with effect on the date of dismissal; and*
- *Sam releases Jack from all claims and liability relating to the employment and his dismissal.*

WHEN CAN A SEPARATION AGREEMENT BE RULED VOID?

A court or tribunal may rule that a separation agreement is void if:

- you did not allow the employee enough time to consider the proposal (see page S 1/12)
- it is found not to be legally binding (see page S 1/8);
- the employee entered into it under duress (see page S 1/12);
- the meaning of an essential term in the separation agreement is unclear (see page S 1/13); or
- the employee signed the separation agreement in circumstances that affected their ability to decide in their best interests (see page S 1/14).

A separation agreement may be ruled void in these circumstances

HOW LONG SHOULD YOU GIVE AN EMPLOYEE TO CONSIDER A SEPARATION AGREEMENT?



Caution: A separation agreement may be rejected by a court or tribunal if it finds you did not allow the employee enough time to consider the proposal.

Generally, an employee should not be expected to state their position to the proposed terms of the separation agreement on the same day they are offered.

You should give the employee the opportunity to do the following before responding:

- ‘sleep on it’; and
- seek advice.



Tip: If you require a response on the same day, allow the employee time away from their ordinary duties to enable them to consider the terms of the separation agreement.



Caution: Never ask an employee to sign any proposed separation agreement on the spot. This could be interpreted as placing unfair pressure (or duress) on the employee.

DID THE EMPLOYEE ENTER INTO THE AGREEMENT UNDER DURESS?

Forcing an employee to sign a separation agreement would occur if you tell them that you plan to dismiss them and offer a separation agreement on a ‘take it or leave’ basis, i.e. to sign the agreement or be dismissed. This will be viewed by a court as if you had dismissed the employee outright.



Caution: This can also be a breach of the general protections provisions of the *Fair Work Act 2009* (Cth) (FW Act).



Tip: If you do not intend the proposed terms of a separation agreement to be considered on a ‘take it or leave’ basis, you should include a clear statement to that effect in your written separation offer.

The document must communicate to the employee that:

- you are issuing proposed terms only; and
- no decision has been made to terminate their employment.

WHEN WILL A 'TAKE IT OR LEAVE' OFFER BREACH THE FW ACT?

Under the FW Act, employees are protected from adverse action for exercising their workplace rights. Do not make a 'take it or leave' separation offer to an employee who has exercised a workplace right by making a complaint or claim, such as:

- lodging a workers' compensation claim;
- making a sexual harassment complaint; or
- making a complaint to the FWO.

Please refer to general protections in the word index for more information.

Important: State and Territory workers' compensation legislation also protects employees from victimisation for making a compensation claim.

Please refer to workers' compensation and victimisation in the word index for more information.



IS THE MEANING OF THE SEPARATION AGREEMENT UNCLEAR?

A court or tribunal may rule a separation agreement is void if the meaning of the agreement is unclear. The meaning of a separation agreement will be unclear if an essential term or provision:

- is missing; or
- can have more than one meaning.

Important: In most cases, a separation agreement will still protect you from legal liability even if the employee signed it under some mistaken impression about how a provision worked. However, this will not be the case if you knew the employee signed on the basis of a mistaken view and you did not correct them in order to take advantage of that mistake.





Case Law

In Potter v Darwin City Council (2010), solicitors for the employer and for the claimant proposed terms to settle an unfair dismissal claim. In a telephone conversation, the solicitors agreed certain terms on behalf of their clients, including payment by the employer of a settlement sum of \$17,500. It was agreed that the settlement terms would be included in a deed of release. When the proposed deed was delivered by the employer's solicitor, it showed that the settlement sum of \$17,500 would have tax deducted. The employee then claimed there was no deal.

**Case Law:
Employee's
mistaken
belief does
not render
separation
agreement
void**

The Tribunal noted that the fact that the settlement agreement did not say whether the \$17,500 was net or gross did not make this term of the settlement uncertain. That is because the usual rule is that unless parties deliberately stipulate that a settlement sum is to be a net sum, the agreed sum is before tax.

The Tribunal also stated that, while the employee mistakenly believed the amount would be net and told his solicitor to accept the offer on that basis, neither the employer nor its solicitor did anything to cause this mistaken view.

Therefore, the Tribunal ruled that there was a binding agreement to settle the unfair dismissal application made between the parties and that this agreement was reflected in the deed.

WAS THE EMPLOYEE IN A POSITION TO DECIDE WHAT WAS IN THEIR BEST INTERESTS?

A court or tribunal may set aside a separation agreement if it finds the agreement was signed in circumstances that seriously affected the employee's ability to decide what was in their best interests.

This often occurs if the employee:

- does not understand English well; or
- was not provided sufficient opportunity to have the terms of the proposed separation agreement explained to them.

Tip: *A separation agreement cannot be ruled void simply because the employer has more bargaining power than the employee, or it is difficult for the employee to find new employment.*



**CHECKLIST: HOW TO DETERMINE WHETHER
A SEPARATION AGREEMENT CAN BE LEGALLY
ENFORCED**



Use the following questions to help determine whether your separation agreement with an employee can be legally enforced:

- ☐ Are the terms recorded in a document signed by both you and the employee?
- ☐ Are any of the terms of the formal document uncertain or unclear?
- ☐ Did the employee choose to sign, without being under any duress or being given a 'take it or leave' ultimatum?
- ☐ Has the employee been given enough time and opportunity to consider the proposal, and to obtain independent advice before they signed the agreement?
- ☐ Have you complied with your obligations with the separation agreement, or at least demonstrated an intention to do so, e.g. paid the employee a settlement amount?
- ☐ Was the employee in a position to be able to effectively determine whether the agreement was in their best interests?

**WHAT IF AN EMPLOYEE MAKES AN UNFAIR DISMISSAL
CLAIM DESPITE THE SEPARATION AGREEMENT?**

Remember: If an employee enters into a separation agreement with you, it means the employee has given up their right to make an unfair dismissal claim against you in return for an ex gratia benefit.



If the employee takes your payment but refuses to discontinue an unfair dismissal claim, you can apply to the FWC for the unfair dismissal application to be dismissed because it is:

- frivolous;
- vexatious; or
- has no reasonable prospects of success.



Case Law

In Stanuovo v Plastic Systems (2011), an employer raised performance and misconduct concerns with an employee, and told the employee that the company intended to terminate his employment for misconduct.

The employer indicated that before taking that step, the employee would have an opportunity to resign. A proposal was made for terms of separation that involved the parties signing a deed of release. The employee signed the deed of release and resigned.

Case Law: Unfair dismissal claim dismissed

The Tribunal ruled that the employee had been taken by surprise and that his resignation was forced. However, over the next week the employee negotiated various changes to his separation arrangement contemplated by the deed. While he did not sign an amended deed, neither did he challenge the deed or argue that it was not enforceable.

When the employee later filed an unfair dismissal claim, the employer applied to the FWC to have the claim dismissed on grounds that it was frivolous, vexatious, or had no reasonable prospects of success, because of the signed deed of release. The FWC agreed and dismissed the claim.



Important: An employee who seeks to continue an application, notwithstanding there is an agreement to settle the matter in place, may also be exposed to costs. The FWC or court can impose a costs order against an employee due to their unreasonable act or omission in connection with the conduct or continuation of the matter, which caused the employer to incur costs.



TEMPLATE: INFORMAL SEPARATION AGREEMENT

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INFORMAL SEPARATION AGREEMENT

[insert date]

[insert employee's name & address]

Dear

Separation

I confirm that [insert full name of employer] (the Employer) offers you the following terms for separation:

- 1 Your employment with the Employer will end on [insert termination date] by reason of [redundancy/ your resignation/mutual separation].
- 2 The Employer will pay you \$(insert gross total), less applicable tax deductions, which sum includes an amount in lieu of notice, [redundancy pay] and an ex gratia payment.
- 3 The Employer will pay you \$(insert gross total), less applicable tax deductions, in satisfaction of your unpaid employment entitlements accruing to your termination date, being the sum of unpaid salary and [insert number of hours] hours of unused annual leave.
- 4 The Employer will provide you with a statement of service and will agree to take best endeavours to ensure that none of its employees, officers or agents disparage you to any employee of the Employer or any third party (it is not the Employer's policy to provide references, although you are free to approach individual employees for personal references).
- 5 You agree:
 - (a) to hereby release and forever discharge the Employer, or any officer, employee or agent of the Employer, or any controlled entity or related body corporate of the Employer, in respect of any and all present and future claims, actions or liability (including any claim for costs) arising out of or in relation to your employment with the Employer, except for claims, actions or liabilities arising under workers' compensation legislation statutory superannuation or to enforce this agreement;
 - (b) not to disparage the Employer, or any officer, employee or agent of the Employer, or any controlled entity or related body corporate of the Employer to any person;
 - (c) as a fundamental term of this agreement, not to disclose the terms of this letter, or the circumstances relating to its production, to any person except for the purposes of obtaining confidential legal, tax or accounting advice or except where required by law or to enforce this agreement.
- 6 You will return to me prior to the termination date all property and other things in your possession that belong to the Employer or any of its clients, including any document containing or recording information confidential to the Employer and/or its clients.
- 7 You acknowledge that you understand the terms of this letter and have had the opportunity to seek appropriate independent advice prior to agreeing to those terms.
- 8 You acknowledge that none of the Employer, its officers, employees or agents has made any representation, promise or inducement or has been party to any conduct material to you entering into this agreement other than those matters set out in this letter.

This letter does not constitute notice of termination of employment. Rather, it is only an offer made on behalf of the Employer to make an agreement with you on the terms contained in this letter.

This document is a starting point to help you develop a document appropriate to your individual situation. It will need to be tailored to your specific circumstances in light of any applicable laws that apply in your jurisdiction. You should seek your own advice about the necessary amendments. © Portner Press, 2017



TEMPLATE: FORMAL SEPARATION AGREEMENT

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FORMAL SEPARATION AGREEMENT

THIS SETTLEMENT AGREEMENT is dated

PARTIES:

[insert full name, ACN and business address of employer] (Employer)

[insert full name and address of employee] (Employee)

INTRODUCTION:

- A The Employer has employed the Employee since [insert commencement date] (Employment).
- B The Employment will end on [insert termination date] as a consequence of [redundancy/ resignation/mutual separation] (Termination).
- C The Employer and the Employee agree on the terms of this agreement:
 - (a) to resolve all matters, rights and entitlements relating to and/or arising out of the Employment and/or the Termination now or in the future (Employment Matters); and
 - (b) for the Employer and the Employee to provide mutual releases in relation to Employment Matters.

IT IS AGREED:

1 OBLIGATIONS OF THE EMPLOYER

1.1 Consideration

In consideration for this agreement the Employer will:

- (a) in the manner prescribed in clause 1.2, make a payment to the Employee in the gross sum of \$[insert gross sum], which sum includes an amount in lieu of notice, payment for other employment entitlements and an ex gratia payment;
- (b) [transfer ownership in the computer and printer located at the Employee's residence to the Employee for nil consideration;]
- (c) [subject to clause 1.3, reimburse the Employee for any legal costs the Employee has incurred in relation to this agreement up to a maximum of \$[insert figure] inclusive of GST.]

1.2 Termination payments

On the next pay day after the Termination the Employer will deposit into the Employee's nominated bank account the following lump sum amounts:

- (a) an employment termination payment in the gross sum of \$[insert gross figure], less \$[insert figure] for taxation;
- (b) a payment for unused annual leave (including leave loading) and unused long service leave in the gross sum of \$[insert gross figure], less \$[insert figure] for taxation; and
- (c) \$[insert figure] being the tax-free part of the genuine redundancy payment.

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