



Insight

Commercial Dispute Resolution

May 2010

Recent amendments to the Corporations Act: Shaking up the Golden Handshake

Amid the global financial crisis in 2009, the Federal Government announced reforms to Part 2D.2 of the *Corporations Act 2001* (Cth) (**Corporations Act**) to address public disapproval for what was characterised as rewarding company executives for poor performance in the form of a “golden handshake”. On 24 June 2009, it introduced into Parliament the *Corporations Amendment (Improving Accountability of Termination Payments) Bill 2009 (Bill)*, which, after amendment, came into operation on 24 November 2009. The amendments to the Act have significantly expanded the circumstances in which shareholder approval must be obtained before termination benefits can be provided to executives and company officers on retirement from office or a position of employment. A breach of these new provisions in the Act could lead to a potential prosecution of companies.

Summary of the Changes

The effect of the new legislation is reflected in the table below.

Issue	Previous Position	New Position
When must shareholder approval be obtained to pay a termination benefit?	When the payment exceeds seven times the recipient's annual remuneration.	When the total value of the benefits exceed one year's base salary, i.e. the average base salary over the previous 3 years ¹ .
Does shareholder approval have to be obtained for directors only?	Directors only.	Not only directors, but for any person who holds a “ <i>managerial or executive office</i> ”. i.e. a person who has been a director at any time over the previous 3 years and, in the case of a listed company, key members of management and (if different) the 5 highest remunerated executives over the last year.
What is a “termination benefit”?	Some ambiguity existed in respect of what constituted a termination benefit.	The definition of termination benefit has been expanded and clarified. Examples of termination benefits include a payment in lieu of notice, a payment for a post-employment restraint and payments made as a result of the automatic or accelerated vesting of share based payments.
Who can participate in the shareholder vote?	A director could participate in the vote to approve their own termination benefit.	Directors and executives who hold shares in the company cannot participate in the vote to approve their own termination benefit.
What if the payment is made without shareholder authorisation?	No express requirement for immediate repayment.	The individual must pay back unauthorised termination benefits immediately.
What are the sanctions for making a payment without shareholder approval?	Civil penalties of \$2,750 for individuals and \$16,500 for corporations, with a risk of 6 months' imprisonment.	Civil penalties have been increased to \$19,800 for individuals and \$99,000 for corporations, with a risk of 6 months' imprisonment.

1. Specific rules apply in the case of an executive who has held office for less than 3 years.



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Case Law - Dome Resources NL v Silver²

To date there have not been any cases decided under the new amendments with the result that there is little judicial guidance on the ambit and future operation of the revised Part 2D.2 of the Corporations Act. However, the New South Wales Court of Appeal examined the application of these provisions as they existed in 2000 in the case of *Dome Resources NL v Silver*³.

In this case Mr Silver provided his services as director to Dome through interposed companies. Mr Silver retired as a director of Dome and claimed payment for a retirement benefit in the amount of approximately \$474,000 pursuant to a retirement deed. Dome claimed it was not liable to pay him the retirement benefit because, in doing so, it would contravene section 200B of the Corporations Act. This was on the basis that the payment would exceed the financial cap then in place under section 200G, when determined with reference to the annual sums paid to Mr Silver's interposed companies, as opposed to only the annual remuneration paid to Mr Silver himself.

The Court of Appeal concluded that the payments to the interposed companies could be considered "remuneration" for the purposes of determining the financial cap under section 200G of the Corporations Act. However, even taking this additional amount into account, the Court of Appeal still held that the termination benefit owed to Mr Silver under the deed did not exceed the financial cap by reason of taking into account the period of Mr Silver's employment and member approval was therefore not required. As a result, Dome was ordered to pay Mr Silver the termination payment under the retirement deed.

The Dome decision is an example of how some claims by former executives will now proceed by reason of the reduced "cap" and the prohibition on companies now paying prescribed termination benefits. It should be remembered that the "cap" applies to the "estimated annual base salary" as opposed to the former test of "total remuneration". This new test is much narrower.

2. [2008] NSWCA 322.

3. [2008] NSWCA 322.

Conclusion

The amendments are expected to impact on companies, particularly those considering a restructure of their senior management team. It may well result in litigation where companies now refuse to seek member approval, or indeed are unable to obtain member approval. Further, senior executives may now negotiate more rigorously on remuneration rates, performance-based bonuses, executive equity schemes and "golden hellos". Against the context of these amendments, together with the ASX Corporate Governance Guidelines and the Productivity Commission Report on Executive Remuneration, companies should expect to make substantial changes to their recruitment, retention and retirement strategies for company officers and senior executives if they are to achieve efficient "exits" of senior executives. For company officers it should also highlight the need for scrupulous compliance with their statutory and fiduciary duties.

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