Spain’s New Companies Act Amendments Strengthen Corporate Governance Framework

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After an extensive parliamentary process, a Reform Bill of the Spanish Companies Act (Ley de Sociedades de Capital) to improve corporate governance was passed on November 17, 2014 (the “Reform”). Spain’s Official Gazette published Law 31/2014, on December 3, 2014 and it entered into force on December 24, 2014, although certain provisions (transitional law rules) applicable to listed companies have been postponed until the present year for their approval in the first general shareholders’ meeting of 2015, including, inter alia, those referring to directors’ remuneration and the configuration and duties of the board of listed companies.

The Reform changes substantial aspects of Spanish corporate law and it affects both listed and non-listed companies, including public limited liability companies (sociedades anónimas “SAs”) and private limited companies (sociedades limitadas “SLs”).

Some of the amendments introduced by the Reform come from the recommendations issued by the Codification General Commission on June 2013 ("Propuesta de Código Mercantil") and, in general terms, the Reform converts into legal rule what was “soft law” so far.

Essentially, the changes are in two areas: on one hand, general meetings and rights of shareholders; and, on the other, company boards and Directors Statute.

General meetings and rights of shareholders

- **Need of shareholders’ approval for relevant transactions**: Shareholders’ powers are widen, including, in respect of the acquisition, disposal or transfer of essential assets. Assets representing over 25% of the total assets shown in the last existing balance sheet merit qualification of essential assets.

- **New system for challenging company resolutions in order to avoid abusive actions**: The Reform removes the difference for challenging between types of resolutions (null, void and voidable) and establishes a
single one-year statute of limitations, excluding the ones contrary to public policy, which are not subject to any time limit.

In general terms, resolutions can only be challenged by those shareholders who have entered into the share capital before the resolution is adopted. In listed companies a holding of a 1 x 1000 in the share capital is required to challenge resolutions for the shareholders’ general meeting.

- **More minority protection rights**: The Reform tries to reinforce rights and gives additional protection to the minority.
  - Regarding the challenge of company resolutions, a specific reference to resolutions adopted abusively by the majority is expressly included as harm to company’s interest.
  - Simply majority is defined as “more votes for than against the resolution among the share capital present or represented at the general shareholders’ meeting”. Thus, these shareholders who do not vote at the shareholders’ meeting will not support the majority.

- **Shareholders’ information rights**: The consequence for breach of information rights has been lowered.

In general, the Reform adds more reasons for the companies to refuse to provide information requested prior to the general shareholders’ meeting to be held. In this case, the affected resolution may only be challenged if the information requested is considered essential to exercise the voting rights. Moreover, the directors are also entitled to refuse when considering that the requested information is not necessary for shareholders’ rights protection or in case that the directors have an objective reason to consider that it may be used for unsocial objectives or its publicity may harm the company or affiliated companies.

In listed companies, shareholders will not be entitled to challenge the resolutions adopted during the general shareholders’ meeting in case of any breach of information rights, but having right to exercise legal action to obtain damages to compensate for harm done.
Company boards and Directors Statute

- **New transparency rules on Directors’ remuneration**: mainly it is considered the most important amendment since it clarifies the different types of Directors’ remuneration and it introduces new transparency rules. In relation to the remuneration of the directors “in their capacity as such”, the maximum amount must be approved by the shareholders, and be reasonable in proportion to the company’s importance, solvency and comparables. In relation to the remuneration for the directors’ performance of executive duties, the director must sign a contract with the company with a two-thirds majority approval among its members (the director concerned withdrawing from discussions and not voting). Such remuneration must be in accordance with the remuneration policy approved by shareholders every three years.

- **Director’s duties, specially the “business judgment rule”**: The due diligence and loyalty fiduciary duties of directors are further detailed.

Regarding due diligence duties, the business judgment rule is enshrined in law for first time in Spain, after being often admitted by the most insightful Spanish case law. Thus, regardless of the final result for the company, the judgments made in business decisions are correctly adopted if only take a minimum standard of diligence established by legal elements (good faith, absence of conflict, sufficient information and compliance with due process).

Likewise, regarding loyalty duties, the Reform expressly states its obligatory nature and improves the text by adding new basic obligations (for example, abstaining from voting in situations of conflicts of interest and independent actions without third-party interference), above all in respect of conflicts of interest (for example, the use of corporate assets). However, the Reform adds exemption cases subject to specific requirements. The exemption may be given by the board of directors, except in the most relevant cases, where the shareholders’ meeting is entitled to give, exclusively, specific authorization (in particular regarding competitive activities).

Directors breaching their duty of loyalty must not only compensate the company for the damages caused but return their unjust enrichment. Responsibility action is compatible with other legal actions (inter alia, objection and cessation actions).
• **Directors’ liabilities:** As the Spanish case law has been ruling in the past years, the Reform extends the liability to shadow (ones under whose instructions the directors of the company act) and *de facto* directors. What is a very controversial change is that the individuals acting as representative of legal persons who are Directors who represent the company and the most senior executives (defined as “individual, whatever definition, who has the most executive duties in the company” provided that there are no managing directors) will also be jointly and severally liable.

**Additional amendments for listed companies**

• **Mandatory appointment of at least two independent directors:** listed companies must have in place not only the auditing committee but also the remuneration and appointment committee, which are regulated in detail. The composition must be comprised of non-executive directors, placing particular emphasis in the fact that at least two should be independent directors (in any event, the Chairman will be one of the independent directors elected).

• **Legal definition of the different category of directors:** Up to now the different category of director’s definitions were defined in minor rules but are now incorporated in the law. Furthermore, the maximum term of directors’ appointment is reduced from six to four years, with the right to be re-elected, except for independents, whose term is limited to twelve years.

• **Directors’ remuneration:** regarding the new director’s remuneration, the General Shareholders’ Meeting must approve, each three years, the directors’ remuneration policy, which must include the global amount of the remuneration of the directors “in their capacity as such” and for the directors’ performance of executive duties.

The approval at the 2015 general meeting of the annual remuneration report will be considered an approval of the company’s remuneration policy for the coming three-year period.

• **Minority shareholders:** Associations of shareholders are regulated in detail, which will have the right, among others, to know the identity of all shareholders. Furthermore, the Reform tries to preserve its independence through legal requirements (for example, shareholders holding more than
0.5% are forbidden to join this kind of associations). Finally, the company will not be entitled to ask for more than 1,000 shares to attend general shareholders’ meetings.

- **Exercise of certain rights**: The percentage required to exercise minority rights in listed companies is lowered from the standard 5% to 3%, which makes the exercise of such minority rights more accessible.

The time limit for challenging company resolutions is reduced to three months and it is required a minimum stake of 0.1% (the minimum may be lowered by company’s articles of association), except resolutions contrary to public policy (where there is no minimum stake).