When borrowing money needs to be approved by the shareholders?

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It is generally undisputed that important borrowings are to be approved by the company's directors as a matter of due diligence. However, the Spanish Supreme Court (SSC)[1] has recently dealt with this question in regard to a dispute about a EUR 70 million financing granted by a syndicate of lenders to La Zaragozana, a Spanish company that brews and markets beer.

The board of directors of La Zaragozana approved by majority the financing, but a dissenting director filed a claim challenging the decision on the grounds that the borrowing was much higher than 25 per cent of the value of the company's assets (EUR 132 million). He submitted this was equivalent to selling or buying an "essential asset" within the meaning of article 160.f of the Spanish Companies Act (SCA), which requires "the acquisition, disposal or contribution to another company of essential assets" to be approved by the shareholders and provides that "an asset is presumed to be essential when the amount of the transaction exceeds twenty-five per cent of the value of the assets shown in the latest approved balance sheet".

The claim was dismissed by a first instance commercial court, by the Court of Appeal of Zaragoza and, finally, by the SSC.

The SSC noted that article 160.f SCA vests in the shareholders the power to take certain decisions (acquisition, disposal or contribution of "essential assets") that, although "by their business nature could in principle be formally taken" by the directors, have an "equivalent effect" to that of other decisions "typically" reserved to the shareholders (such as *changes of the corporate structure*, amendments of the by-laws or the company's winding-up), as they "substantially affect the shareholders' legal and economic position or the company's structure or activity".

Bearing this in mind, the SSC added that borrowing money cannot be considered an acquisition or a disposal of "essential assets" unless (i) repayment is secured by "relevant company's assets" or (ii) it "jeopardises the viability of the company or substantially alters the conduct of its activity, the shareholders' initial risk assessments or their positions of control".

The SSC found that the financing provided to La Zaragozana did not meet any of these criteria and, therefore, did not have to be approved by the shareholders because:

- No collateral was created on any asset "devoted to a line of business of the company".

[1] Judgment of the SSC 1045/2023 dated 27 June 2023.

- Although the financing was very relevant (EUR 70 million), a large part of it was meant to replace a previous financing and, thus, did not significantly increase the company's financial debt.

- The financing was aimed at providing liquidity that was necessary to preserve the company's activity, pursuant to a new business plan that had been previously agreed and not challenged.

We find that the two last criteria are questionable, but in any event directors should be wary of this type of financings, for, had the SSC found that the borrowing should have been decided by the shareholders, the consequence could have been the annulment of the financing.

We say *could* because two different interpretations of article 160.f SCA have been held so far: (i) while some understand that any transaction approved in breach of this legal provision is null and void, (ii) others consider that it can only be annulled if the other party -in this case, the lenders' syndicate- acted in bad faith or with gross negligence, meaning to know or should have known that the assets at hand were essential with the meaning of article 160.f SCA. And in both cases directors may be liable for the damages caused to the company or to third parties.