

Again on directors' remuneration and abuse by majority shareholders

Madrid, March 2023

The Barcelona Court of Appeal (BCA) rendered on 7 December 2022 a judgement on directors' remuneration and abuse by the majority shareholder¹.

The judgment is about a company running a nursing home with 22 employees, an annual turnover of €1.5 million and some €100,000 of profit. It had a majority shareholder with 51.5 percent of the share capital (Miguel). Thanks to his votes, the general shareholders' meeting approved to pay him a remuneration of €95,000 in his capacity as director. Miguel justified his remuneration because he would act as manager of the company from then on. The two minority shareholders (Paloma and Genaro) challenged the GSM's resolution submitting that the amount was disproportionate, given that one of them (Paloma) had been the manager of the nursing home for some years with a salary of €40-45,000 and it was not necessary to have another manager.

The first instance judgment dismissed the challenge. However, the BCA upheld it for the following reasons.

Miguel had "unquestionably" a conflict of interests as he was the majority shareholder and the GSM's decision was "very favorable to his interests" and hence "could be" detrimental to the company and the rest of its shareholders.

According to article 190 of the Spanish Companies Act (SCA), in case of a conflict of interests like the one at hand, the majority shareholder has the burden to prove that the challenged decision is beneficial to the company's interest. In addition, pursuant to article 217.4 of the SCA, directors' remuneration must be reasonably proportional to the importance of the company, its economic situation and market standards.

Furthermore, every shareholder must be loyal to the company and the rest of shareholders and this is why courts control majority decisions from the perspective of abuse of right, precisely to avoid the "tyranny of the majority". An excessive remuneration of a director who is also the majority shareholder may disguise a disproportionate (unjust) distribution of profits among shareholders.

The BCA went on saying that, even though none of the parties had provided evidence of market standards in comparable companies, it was for the majority shareholder to prove that the decision was in the company's interest.

Without prejudice to the above, several circumstances led the appeal court to find that the remuneration was excessive, namely that Miguel had no remuneration at all while being a director in the past, that the salary of Paloma was much lower, despite

¹ Judgment of the Barcelona Court of Appeal 1723/2022 dated 7 December 2022.

the fact that her functions were broader than those of Miguel, and that Miguel's remuneration represented more than fifty per cent of the profits and was not proportionate to the annual turnover and number of employees. For these reasons the BCA declared the decision null and void.

The judgment only partially spells out the submissions of the parties, but it seems that had Miguel provided some support to justify the reasonableness of his remuneration the outcome would have been the opposite, for the reasons given by the appeal court to deem it disproportionate seem rather weak.