GLOBAL FORUM ON LAW, JUSTICE AND DEVELOPMENT (GFLJD)

COMMUNITY OF PRACTICE

QUESTIONNAIRE ON INSOLVENCY LAW AND COMPANY LAW

This questionnaire addresses the issues affecting the interface between insolvency law and company law, and should be answered providing a) references to the statutes and provisions quoted; b) relevant cases, if any; c) any other supporting information, such as references to books or articles.

As an introduction to the questionnaire, consider the following examples of interaction and conflicts between insolvency law and company law (the examples, that assume certain characteristics of some legal systems, should be understood as having only illustrative purposes):

1) A company is under a reorganization procedure. Its directors have prepared a reorganization plan that, inter alia, provides for the conversion of creditors’ claims into equity of the company. In more detail, the plan would provide for the cancellation of the existing shares and the issuance of new shares to be allotted according to the plan, exclusively to the company’s creditors, except if the shareholders make a new contribution into the company.

The plan also provides for the transfer of a substantial part of the business to a third party. The shareholders oppose the plan. However, the creditors and the board, with the support of a due diligence analysis, have reason to believe that the opposition is unreasonable, as the value of the company’s liabilities clearly exceeds the value of the assets, and in a liquidation the shareholders would not receive any proceeds.

See questions 19, 34, 37

2) In a company under a reorganization procedure, the plan foresees the issuance of new shares to be allotted to the company’s creditors, diluting the existing shares but without cancelling them. The new shares would have prevailing voting and governance rights over the existing shares. The shareholders oppose the plan.

See questions 13, 34

3) A reorganization plan foresees, inter alia, a capital increase structured in such a way to ensure that a substantial share in the company would be acquired by an external investor, whose resources/business strategies would help save the long-term operation of the company. However, the shareholders opposing the plan decide to exercise their pre-emption rights in the capital increase, thereby defeating the plan’s strategy based on the stepping-in of the significant investor.

See questions 18, 20
4) A company is under a reorganization procedure and the board of directors is designing a plan that, while ensuring the viability of the business, would adversely affect the rights of the shareholders. A minority shareholder requests that a general meeting of the company be held, seeking the approval of several proposals by the meeting, including the removal of the directors of the company in reorganization.

See questions 10, 31

5) A reorganization plan is approved with the decisive support of intra-group (insider) creditors, with the result that unsecured creditors suffer a loss, whereas shareholders retain value in the reorganized company.

See questions 21, 22, 25, 26

These stylized examples, drawn from a number of real cases in different jurisdictions around the world, illustrate the tension between the shareholders, the creditors and, in general, company law and insolvency law.

The purpose of the following questionnaire is to identify how shareholder rights are affected by the insolvency of the company (including in cases of imminent insolvency), and the interaction between shareholder rights and the normal operations in an insolvency process (either a liquidation or a reorganization process). Although some general questions are also relevant for insolvency procedures applicable to special regulated companies (i.e., for example, financial institutions), the questionnaire is designed to analyse the conflicts between insolvency law and company law, and therefore, reference should be made to the ordinary insolvency procedures as applied to the corporate forms which are generally used in your jurisdiction for both “close” and “open” companies.

The main issues can be summarized as follows:

- The respective powers of the board and the shareholders’ meeting in insolvency proceedings;

- The substantive and procedural rights of shareholders in a company subject to insolvency proceedings;

- The possibility of using the old/same corporate entity as a vehicle for the reorganization of the company;

- The possibility of the shareholders to retain a participation in the reorganized company, and, if they are allowed to retain a participation, the allocation of value between creditors and shareholders.

---

For instance, the questionnaire for the UK will include references to both limited liability companies (LLCs) and public limited companies (PLCs); the questionnaire for Germany will cover both AGs and GmbHs; and the questionnaire for Italy will cover SAs and SRLs.
All of these issues are structured around two principal areas of conflict between company law and insolvency law: the individual rights of shareholders and the role of the shareholders' meeting in an insolvent company.

Dealing with the preceding issues implies, inter alia, addressing the question of the legal position of the shareholders in companies, e.g. the question of whether and to what extent the law considers shareholders as owners of the company in a legal sense. The effects on the legal position of shareholders of an insolvent company may in fact create a conflict with special -even constitutional- safeguards for the protection of property rights. These safeguards, in turn, may be less or more stringent, depending on whether the company is insolvent in the balance-sheet sense (i.e., whether the value of its liabilities exceeds the value of its assets) or not, and whether a liquidation or a reorganization procedure is used.

In addition, the preceding issues may present further variables according to the characteristics of the company involved. Outcomes could be different depending on the fact that the company is closely held or is a listed company, or is a specially regulated company, such as a financial intermediary.

***

SPAIN

* Responses to the questionnaire: José M. Garrido (IMF) with the assistance of María Luisa Sánchez Paredes (Antonio de Nebrija University, Madrid)

I. Introductory questions on the insolvency procedures available in the relevant jurisdiction.

1. What insolvency procedures – either liquidation or reorganization procedures – are available for distressed or insolvent companies?

Spanish insolvency law is based on a unitary insolvency procedure – the concurso de acreedores- that applies to all kinds of debtors (natural persons and legal persons) and that includes a compromise (convenio) which may be used for reorganization, and also a liquidation mechanism (liquidación). These are two different alternatives which can be selected within the unitary insolvency process. The insolvency regime is embodied in the Insolvency Act (Ley Concursal, Ley 22/2003, July 9th 2003), successively reformed. The latest reform of the Ley Concursal was introduced by the Royal Decree-Law 4/2014, March 7th 2014, which was revised and passed by Parliament as Ley 9/2015, May 25th, on urgent measures on insolvency matters).

---

2. Are there special insolvency procedures available for financial institutions or for other special classes of companies?

There is a special regime for credit institutions, in force since 2005 (Ley 6/2005, April 22nd 2005, sobre saneamiento y liquidación de las entidades de crédito – Act on reorganization and liquidation of credit institutions), but this regime was recently complemented by a new act, which has been introduced in accordance with the development of international standards in this area, and with the objective of increasing the possibilities of resolution of banks and other financial institutions: (Ley 9/2012, November 14th 2012, de reestructuración y resolución de entidades de crédito – Act on restructuring and resolution of credit institutions). What is important is to bear in mind that there is just one regime for the insolvency of companies, but the intersection of the insolvency regime and the company law regime requires the analysis of two different types of companies: the sociedad de responsabilidad limitada (limited liability company, or private company) and the sociedad anónima (public company), because there are substantial differences in the contents of the rights of shareholders (or members), and the role and functions of the general meeting. The responses will indicate those differences. In any case, the analysis is made easier by the fact that a legal text has consolidated the regime of limited liability companies and public companies into the Ley de Sociedades de Capital (Corporate Enterprises Act – see Real Decreto Legislativo 1/2010, July 2nd, Ley de Sociedades de Capital, which was reformed in 2013; and again in 2014, by the Ley 31/2014, December 3rd, on corporate governance).

3. Are there any specific legal provisions that apply to debt restructurings achieved without a full formal insolvency process?

There are specific provisions regulating restructurings with minimal court intervention. The law foresees that the debtor will issue a notification to the competent court of the start of negotiations for a refinancing agreement or a pre-packaged plan (article 5 bis of the Insolvency Act). The competence to initiate negotiations rests with the board or the directors of the company. There is a public registry of such petitions (article 198 of the Insolvency Act). From the moment the court is notified, the debtor has three months to negotiate a refinancing agreement or a pre-packaged plan. If negotiations do not succeed, the debtor will be declared insolvent by the end of the three-month period. During the three-month period, creditors will not be able to initiate enforcement actions on the debtor’s assets that are necessary for the operation of the business, and ongoing enforcement actions will be subject to a stay. Financial creditors will be subject to a general stay of enforcement actions, as long as it can be evidenced that at least holders of 51 per cent of financial claims support the negotiations and have agreed to a standstill. Restructuring agreements are protected from potential avoidance actions in a subsequent insolvency process if a number of requirements are met (article 71bis of the Insolvency Act). For a refinancing agreement to be protected, the following conditions need to be met:

---

- The agreement should increase credit to the debtor or, at least, reduce or reschedule its liabilities in support of a viability plan to ensure the continuity of the business in the short and medium term;

- The refinancing agreement must have been signed by creditors representing at least 3/5 of the total claims against the debtor at the date the agreement was reached. If the agreement involves a corporate group, the percentage must be reached both individually and at the group level, excluding inter-group loans;

- A certificate of the auditor of the debtor evidences that the relevant majority has been reached;

- The agreement is notarized.

The law also protects the acts undertaken in accordance with a restructuring agreement, even if the previous conditions have not been met, but the following requirements are applicable:

- the acts must increase the assets/liabilities ratio of the debtor;

- the resulting current assets are at least equal to the resulting current liabilities;

- the value of the resulting security interests in favour of the creditors does not exceed 9/10 of the value of the outstanding claims held by those creditors, and does not alter the ratio between the value of securities and the value of claims precedent to the agreement;

- the interest rate applicable to the restructured claims does not exceed in more than 1/3 the interest rate applicable before the agreement;

- the agreement is notarized.

A refinancing agreement can be validated by a court (see 4th additional disposition of the Insolvency Act) to extend its effects to dissenting creditors. A validation request can only be submitted by the debtor. An agreement needs to have been supported at least by holders of 51 per cent of the financial claims to be validated, in addition to other requirements described above. The quorum does not include financial claims held by related persons, and trade creditors and tax claims are outside the scope of this provision. The law includes complex rules to determine the effects of refinancing agreements over secured and undersecured financial creditors.

The regime of validation of refinancing agreements was introduced in 2013 (see 4th additional disposition of the Insolvency Act, as modified by article 31 of the Law 14/2013, September 27th, on supporting measures for entrepreneurs. However, the system has been reformed successively by the Royal Decree-Law 4/2014, of March 7, and by the Law 9/2015. The modifications introduced by these reforms aim at the creation of strong incentives for out-of-court solutions to the financial difficulties of businesses in Spain. This has included the provision that the shareholders of a company may become liable for the company’s debts if they refuse to enter into a refinancing agreement based on a debt/equity swap that has been considered reasonable by an independent expert, and that recognizes their pre-emption rights (see article 172.2.1 of the Insolvency Act, in connection with article 165.2 of the Insolvency Act). There is some uncertainty about how this new provision will work in practice, but it seems that it would naturally refer to situations in which a shareholder is decisive in the failure of an
agreement and, as a consequence, the company is declared insolvent. It could be argued that the law is extending the regime of personal liability applicable to directors also to shareholders who are capable to exercise influence over the company (as a matter of fact, there is a reference to shadow directors in the new provision). The goal, therefore, is to punish the obstructive behaviour of those persons who, not being subject to the strict regime of directors’ duties, are nevertheless capable of determining the availability of restructuring options for the distressed company.

4. What are the commencement criteria for insolvency procedures?

The commencement criteria are broad: the general principle is a cash flow test, based on the inability of pay debts as they fall due (article 2.2 of the Insolvency Act). Imminent insolvency also satisfies the insolvency test for debtor-filed applications (article 2.3 of the Insolvency Act) – imminent insolvency is defined as the situation in which the debtor itself foresees that it will be unable to pay its obligations as they fall due. For creditor-filed applications, the rules change substantially: a creditor has to show that an enforcement action over the debtor’s assets has been unsuccessful, the main criterion is a cessation of payments test, and alternatively, a series of presumptions based on the existence of default of certain obligations (see article 2.4 of the Insolvency Act).

5. Who can propose a restructuring plan? (e.g. corporate bodies, insolvency representatives, creditors)

Proposals for insolvency plans can be presented both by the debtor company and by creditors (article 113 of the Insolvency Act). The debtor company is represented by the directors for this purpose. The argument in favour of granting this competence to the directors of the company is based on the analogy with article 3.1 of the Insolvency Act, which establishes that the directors (or the liquidators, as the case may be) have the power to file for an insolvency process, without the need of the authorization of the shareholders’ meeting.

Creditors presenting a proposal must represent at least one fifth of the total claims included in the creditors’ list (article 113 of the Insolvency Act).

6. Please describe whether and to what extent shareholders’ rights can be affected by a situation of distress/insolvency of a company before and/or irrespective of the opening of a formal insolvency proceeding (e.g., are there any fiduciary duties of the shareholders to approve corrective measures/plans proposed by the board?)

This is a controversial question. In principle, fiduciary duties extend to directors only, who are under a regime of strict liability if they do not react promptly in an insolvency situation, by calling a meeting and proposing corrective measures, or and there is no consistent doctrine about the shareholders being under the duty to recapitalize the company. There are doctrines of undercapitalization developed by academics, but it is by no means clear that these theories have
been accepted by the courts. Undercapitalization can be material – where the company has no resources to perform the activities for which it was created; or formal – where the company has resources to perform its activities, but those resources do not come from capital but, rather, from loans, generally granted by insiders. The way Spanish law reacts against formal undercapitalization – which is, by far, the most worrying form of undercapitalization – is by automatically subordinating the loans granted by insiders to the company (see article 95.5 and article 93 of the Insolvency Act).

II. Shareholders’ Rights in Companies Subject to Insolvency Proceedings

As a general comment, it is possible to indicate that rights of shareholders are not affected by the insolvency process, unless there is a specific rule – and there are several – that changes those rights. However, Spanish law has a general codified doctrine of “abuse of right”, and it could well be that that doctrine could be invoked to stop shareholders from abusively exercising some of their rights (especially, when they are trying to create obstacles for the insolvency process). The concept of “abuse of right” is included in article 7.2 of the Spanish Civil Code, and it represents a fundamental legal doctrine, applicable to all areas of private law.

Although the Spanish Insolvency Act contains specific solutions to some of the most important problems, it does not have all the responses to the complex set of questions that the interface between insolvency law and company law raises. The approach of the insolvency act is piecemeal, and reflects a preoccupation with the questions related to the exercise of the rights of shareholders – and the competences of the shareholders’ meeting – that have been more problematic in the past. However, there are signs in the Act of an emerging general approach, and this is evidenced by a rule whereby the company’s bodies need the approval of the insolvency representatives to adopt any decisions that have an economic impact (article 48 of the Insolvency Act – see responses to questions 28 and 29 below).

The basic rights of shareholders are defined in the Ley de Sociedades de Capital (Corporate Enterprises Act – see Real Decreto Legislativo 1/2010, July 2\textsuperscript{nd}, Ley de Sociedades de Capital). Article 93 states that shareholders and members\textsuperscript{4} have the following basic rights:

\begin{itemize}
\item a) Share in the earnings of the company; and in the corporate assets when the company is wound up;
\item b) Pre-emption rights;
\item c) Attending and voting at the general meeting and challenging the general
\end{itemize}

\textsuperscript{4}In the correct terminology, “shareholders” is the term that describes those who have shares in “sociedades anónimas”, whereas “members” is the term that applies to the persons who participate in “sociedades limitadas”. For ease of reference, the responses to this questionnaire use the word “shareholders” in a broad sense.
meetings’ decisions;
d) Information rights.

A very important qualification needs to be made regarding the exercise of these rights by shareholders. The denial of the exercise of those rights by directors can constitute a criminal offence (article 293 of the Criminal Code). There are examples, for instance, of directors being convicted of this crime for having denied unjustifiable the right of information of shareholders (see AAP Barcelona (Sec. 2) 49/1999, March 22, ARP\1999\1773). This crime can be committed by directors, but also by "de facto directors", so potentially also persons who perform functions similar to those of directors, such as insolvency representatives, could potentially be responsible for this crime, if the rest of the elements of the criminal conduct are present.

7. Are shareholders notified of the initiation of an insolvency process? If notification is individualized, what are the mechanisms used to identify shareholders?

Shareholders are not notified of the initiation of the insolvency process. In the case of a listed company, this would be classified as relevant information according to the Securities Market Act (Act 24/1988, of 28 July)\(^5\). The concept of relevant information is defined in article 82 of the Securities Market Act.\(^6\) Relevant information regarding the insolvency process will have to be disclosed through the securities commission, and also in the company's webpage (article 82.3 of the Securities Market Act).

8. Are shareholders required to file claims in the insolvency proceeding? What are the consequences of not filing a claim?

Shareholders are not considered claimants. Shareholders cannot participate in the insolvency process as if they were creditors (not even potential creditors). But shareholders can challenge claims admitted to the process (see article 96 of the Insolvency Act). Therefore, shareholders are recognized as holding a residual interest, which justifies their standing to challenge the admission of claims that could eliminate the value of their interest, but that interest is conceptually different from a credit claim. The right of shareholders to receive their residual interest in proportion to their participation in the company is recognized in article 93 a) of the Corporate Enterprises Act.

9. Can shareholders continue to trade and transfer shares after the initiation of an


\(^6\)Article 82.1 of the Securities Markets Act establishes that: "Relevant information shall mean information the knowledge of which may reasonably encourage an investor to acquire or dispose of securities or financial instruments and which, therefore, may have a significant influence on the security's or financial instrument's price in a secondary market".
insolvency proceeding affecting the company?

Shareholders can continue to trade and transfer shares in the same way and with the same conditions as existed before the initiation of the insolvency process. There is a different and separate regime for suspension of trading in official markets (article 33 of the Securities Markets Act), but it does not necessarily establish that shares cannot be transferred during an insolvency process – rather, the suspension is based on considerations that the market regulator appreciates in the market, such as lack of information. A suspension of trading, in any case, does not prohibit or render void transactions of shares conducted outside the market (in the so called “grey” market). The regime is different for limited liability companies and for public companies. In limited liability companies there are always restrictions in the articles (see art. 107 of the Corporate Enterprises Act). In unlisted public companies there may be limits to transfers (art. 123 of the Corporate Enterprises Act). In listed companies, there cannot be any restrictions in the articles of association that affect the transferability of shares.

10. Do shareholders have the right to request that a shareholders’ meeting is held, even if the company is insolvent? (If there are separate reorganization and liquidation procedures, does this affect the response?)

Shareholders have the right to request that a shareholders’ meeting is held under general company law. The competence to call a meeting rests with the directors or the liquidators of the company (article 166 of the Corporate Enterprises Act), but the directors must call a meeting when it is requested by shareholders representing 5% of the legal capital (article 168 of the Corporate Enterprises Act). If the shareholders’ meeting requested is a compulsory one (typically, the annual shareholders’ meeting – see article 159 of the Corporate Enterprises Act), any shareholder, even acting individually, can request to a court that the meeting is held (article 169 of the Corporate Enterprises Act). In public companies, it is also possible to request that new items are added to the agenda of the meeting (“complemento del orden del día”, see article 172 of the Corporate Enterprises Act, and article 519 of the Corporate Enterprises Act, for listed companies), if the request is made by shareholders representing at least 5% of the capital of the company. General company law also recognizes the possibility that, when all are shareholders present, they decide to hold a meeting (“junta universal”, article 178 of the Corporate Enterprises Act), but this possibility is expressly denied to companies which have been declared insolvent, unless the insolvency representative is also present7 (article 48.2 of the Insolvency Act). The competence to call a shareholders’ meeting corresponds to the directors, and, in the case they replaced by the insolvency representatives, to the insolvency representatives. In any case, the general principle according to which any act that has economic consequences must be approved or authorized by the insolvency representatives means that it is understood that calling a meeting is such an act, if only because calling a meeting has economic costs, apart from the obvious and more important fact that the decisions of the meeting may have

---

7The insolvency representative must be present. The question is whether the insolvency representative needs to agree with the idea of holding a shareholders’ meeting or if the shareholders can go ahead and hold the meeting with the mere presence of the insolvency representative, even if the representative does not lend its consent to the meeting. See response to question 28 below.
economic consequences (see AJM Madrid 29.3.2007 [AC 2075, 571]). However, there are other decisions in which the courts have ruled that calling a general meeting is not affected by the insolvency, and that there may be reasons to call a meeting, like the approval of accounts, or other decisions, that do not have an economic impact (SAP Madrid [28a] 13.7.2010 (JUR 2010, 310613)). The courts have recognized the possibility of the court calling a shareholders’ meeting during insolvency (AJM 1 Bilbao 5.6.2009 [JUR 2009, 331263]).

11. Do shareholders have the right to request information in an insolvent company? Do they have information rights as to the progress of a reorganization procedure? Can they exercise that right vis-à-vis the directors of the company -if they remain in charge of the company-or vis-à-vis the insolvency representative?

General information rights are regulated under article 196 of the Corporate Enterprises Act (for limited liability companies). In a limited liability company, all members are entitled to request and receive information in connection with the items included in the agenda of the members’ meeting. Members can request that information in writing, before the meeting, or verbally during the meeting itself. Directors can only refuse to answer the information request if they consider that disclosing the information would damage the interests of the company. However, if the information is requested by members representing 25% of the capital of the company, the directors cannot avail themselves of the argument that releasing the information could damage the company’s interests.

The regulation for public companies (“sociedades anónimas”) is similar (article 197 of the Corporate Enterprises Act), although there are some interesting differences. The recent reform of this article has restricted the scope of the information right to the items in the agenda of the shareholders’ meeting. In addition, the law indicates that the right can be denied when it serves no role in the protection of the shareholders’ rights, or where there are objective grounds to consider that the information could be used for purposes alien to the company, or that publicity may damage the company or other related companies. As in limited companies, if the shareholders exercising the information right hold 25% of the capital of the company, it is not possible to deny the exercise of the information right. A very important rule states that the infringement of the information right only entitles the shareholder to receive compensation for damages, but it does not provide a justification for the annulment of the company's decision. This is extremely relevant, since there has been a long history of decisions being annulled by violation of the information right of shareholders.

Rules for the exercise of information rights in listed companies are similar to those in article 197 but, in addition, there are special rules entitling shareholders to ask questions regarding the auditor’s report and any publicly available information issued by the company, within five days before the shareholders’ meetings of the listed company is held (see article 520 of the Corporate Enterprises Act). Listed companies have shareholder meeting regulations, and the exercise of information rights is contemplated in those regulations.

The Spanish Supreme Court has stated that the right to obtain information is one of the fundamental rights of a shareholder and therefore such right must be interpreted in the broadest terms (STS [1st] 26 september 2001 ( RJ 2001,
The right of shareholders to obtain information is so fundamental that, if it is ignored, the resolutions of the shareholders’ meeting can be avoided (STS [1st] 29 July 2004 (RJ 2004, 5469)). The courts have clarified that the important right of shareholders to request information also exists in an insolvent company, but the courts have added that the disclosure of data cannot prejudice the interests of the company, and especially, that the exercise of the right to receive information cannot be used to create unnecessary obstacles for the company (STS [1st] 31 July 2002 (RI 2002, 8437); SAP Madrid (Sec. 28) 16.2.2009 [AC 2009, 858]). The Supreme Court has indicated in several important cases that the right to information cannot be used “as an instrument to obstruct the corporate activities, to overcome corporate interests in favour of the special interests of the shareholder seeking the information, where there is no true and real necessity” (STS [1st] 13 April 1962 (RJ 1962, 2025) and 26 December 1969 (RJ 1970, 496)). Therefore, the exercise of the right to request and obtain information must not create situations that block or hinder the normal functioning of the company, and the right must be exercised in good faith (STS [1st] 4 October 2005 (RI 2005, 6911)). The courts have developed a doctrine that bans “abuse of right” in the exercise of the shareholders’ right to receive information (STS [1st] 31 July 2002 (RI 2002, 8437), 8 May 2003 (RI 2003, 3888), 10 November 2004 (RJ 2004, 6722), inter alia). The general concept of “abuse of right” is found in article 7.2 of the Civil Code, which is generally applicable to all private law, including company and insolvency law.

An interesting case, specifically connected with insolvency law, was resolved in the judgment of the Audiencia of Vizcaya (SAP Vizcaya (Sec. 4), 292/2011, 15 April 2011 (JUR\2011\302243)). In this case, the court restated the principle that underlies the importance of the right of information for shareholders, and its trascendence for corporate life. In this case, the right of information of shareholders was not respected and the agreements adopted by the shareholders’ meeting were declared void by the court. Interestingly, the information missing and requested by the shareholder referred to the audit and accompanying information of the last accounts produced by the company just before the company entered into an insolvency process, and the general meeting was held when the company was already insolvent. Therefore, this is perfect example of the validity of information rights and the need to respect those rights even in the case of companies that have been formally declared insolvent and are undergoing a formal insolvency process.

12. Can shareholders make proposals for nomination of directors, if the directors continue managing the company?

In the Spanish insolvency process, it is perfectly possible that directors continue managing the insolvent company. The Spanish legislator embedded incentives in the insolvency process for its early initiation, and, as a result, the legal design privileges the debtor who files for its own insolvency process. The general rule, therefore, is that in “voluntary insolvencies” (i. e. insolvencies initiated by debtors – see article 22 of the Insolvency Act) the directors of the debtor company are allowed to continue managing the company, under the supervision and control of the insolvency representative, who is appointed by the court as an examiner of the activities of the directors, and to fulfil the rest of functions that the law assigns to insolvency representatives (article 40.1 of the Insolvency Act –
the term “intervention” is used to refer to this situation). Thus, the default rule is that the directors continue managing the company in “voluntary insolvencies”, and that insolvency representatives are appointed with managing functions over the debtor’s businesses in cases of “involuntary insolvencies” (i.e., insolvency processes initiated at the request of creditors –see article 22 of the Insolvency Act and article 40.2 of the Insolvency Act), and therefore directors of an insolvent company will be removed from their management functions in those cases (this situation is described by the term “suspension”). To summarize, “intervention” refers to the situation in which the company directors continue to manage the company under the supervision of the insolvency representative; whereas “suspension” defines the situation in which directors are removed from their management functions and the insolvency representative takes over the management of the company.

This general rule admits different solutions: first of all, the court retains a general discretion to give managing powers to directors, even in the case of involuntary insolvencies, and the discretion of removing directors even in cases of voluntary insolvencies. This discretionary power of the court must be exercised judiciously, and the court must give the reasons for its decision, expressly stating the risks it tries to avoid and the advantages it intends to produce with such decision (article 40.3 of the Insolvency Act). The court may change this situation at any time during the process, after a motion of the insolvency representative, and after having heard the directors (article 40.4 of the Insolvency Act).

An important point that needs to be highlighted is that, even in the case of suspension, the directors of the company continue to be directors. What the law does is to remove management powers from them, but directors continue to perform a role as a corporate organ (see article 48.3 of the Insolvency Act; see also article 145.3 of the Insolvency Act). This is particularly important because the directors continue to represent the company and can challenge numerous decisions taken within the insolvency process. In essence, and regarding the question addressed here, there is no difference under Spanish law regarding the appointment and removal of directors of an insolvent company: whether the company is managed by the directors or not, directors will continue to exist, and the issue of appointing and removing directors can arise in the insolvency process. Even when the company enters the liquidation phase, directors will continue to represent the company in the process (article 145.3 of the Insolvency Act).

Regarding the appointment of directors, the general rule, under company law, is that the shareholders’ meeting appoints directors (article 214 of the Corporate Enterprises Act). However, the law is silent on the process whereby the shareholders’ meeting decides on the appointment of directors, especially on the issue of the proposals for appointment. In application of the general rules, it is the board, in preparing the agenda of the shareholders’ meeting, who introduces the names of the persons who are formally proposed to be appointed. It is possible, however, that shareholders that represent 5% or more of the capital of the company present alternative proposals for appointment of different persons as directors.
These rules are unaltered by insolvency law, and it is fair to conclude that the regime for appointment of directors in an insolvent company would be exactly the same. This means that, in an insolvent company in which, for whatever reason, there would be vacancies in the board, the board would make a proposal for appointment to the shareholders’ meeting, and shareholders representing at least 5% of the capital would have the opportunity of presenting alternative proposals (i.e., alternative candidates for the position of director).

There are several exceptions to the general rule explained above, such as the “co-optation rule”, whereby, in public companies, it is possible that the board appoints interim directors until the next shareholders’ meeting is held (article 244 of the Corporate Enterprises Act). The second and more relevant exception is the so-called “proportional system”, that allows a shareholder or a number of shareholders representing a certain percentage of the capital to select a proportionate number of directors to their holdings in the company. For instance, in a company where there is a board formed of 20 directors, a shareholder possessing a 5% of the capital has the right to appoint a director (see article 243 of the Corporate Enterprises Act). Once this right is exercised, the shares grouped for it cannot be used to elect or to vote for any other directors.

In a company where a shareholder or a group of shareholders has exercised the right to elect one or several directors according to the proportional system, the same shareholder or shareholders would be entitled to continue exercising that right even if the company is declared insolvent. It is also possible that a shareholder or several shareholders announce their intention to exercise this right once the company is insolvent. In such a case, the shareholder or group of shareholders reaching the requisite threshold in the capital of the company would be entitled to appoint a director, or several directors, in proportion to the participation in the capital, and assuming that there are vacancies in the board of directors.

The conclusion of the analysis above is that Spanish law recognizes the possibility that the directors of an insolvent company continue managing the company, but there are no special rules for the appointment of directors in insolvent companies. Therefore, the general corporate law rules apply, and these rules recognize an important role to the shareholders’ meeting and to individual shareholders with relevant holdings in the appointment of directors.

13. If special categories of shares exist whose holders are granted additional governance rights, are these additional rights affected by the opening of an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?)

According to Spanish corporate law, all shares and stakes\(^8\) in companies grant

---

\(^8\) Under Spanish law, there are legal differences between “shares” (acciones), i.e. the instruments representing portions of the capital of a public company (sociedad anónima); and “stakes” (participaciones), i.e. the interests of members in a limited liability company (sociedad de responsabilidad limitada).
their holder the status of member of the company and grant the same rights
(article 91 and article 94 of the Corporate Enterprises Act; see also article 97 of
the Corporate Enterprises Act, which includes the general principle of equality of
treatment of members of companies). Obviously, there are numerous rights that
are linked to the possession or grouping of a determinate percentage of the
capital of the company, but it must be remembered that all shares and stakes
equally qualify for the exercise of those so-called “minority rights” in company
law. Most importantly, Spanish law incorporates an equalitarian system in the
distribution of governance rights, in which special privileges are strictly
forbidden. In terms of voting rights, there is a strict “one share, one vote”
principle that forbids the issuance of multiple voting shares or stakes (see article
96.2 and 96.3 of the Corporate Enterprises Act). The only deviation from this
principle refers to the issuance of non-voting shares and non-voting stakes. Both
are very rarely used in practice anyway, as these shares must receive special
economic privileges and safeguards (see article 98 ff., Corporate Enterprises
Act).

To sum up, there are no special or additional governance rights attached to
shares or stakes under Spanish company law, and therefore, there is no question
about the effect of an insolvency process over such rights.

14. Can shareholders challenge the decisions of the shareholder meeting, if it is still
active? Do they retain the possibility of taking action against the acts of the
directors? And against the acts of an insolvency representative? Is any authorization
by a judicial or administrative body required to do so or, more generally, to exercise
corporate rights? (If there are separate reorganization and liquidation procedures,
does this affect the response?)

The shareholders’ meeting remains active even if the company is declared
insolvent and a formal insolvency process is initiated (See the response to
question 28).

The right to challenge decisions of the shareholders’ meeting is a fundamental
right of shareholders and members of companies, and therefore all shareholders
and members who have a legitimate interest have standing to sue. However, the
recent reform on corporate governance has established that decisions can only
be challenged by shareholders holding, separately or jointly, 1% of the capital
(article 206 of the Corporate Enterprises Act). Shareholders below that threshold
can only sue for damages, but cannot obtain the annulment of the decision.
Articles of association can lower the statutory threshold, and, in any case, when
decisions are against the public order, any shareholder can request their
annulment. The general grounds to challenge a decision of the shareholders’
meeting are the following:
- The decision is contrary to the law;
- The decision is contrary to the company’s articles of association; or
- The decision is detrimental of the interests of the company, and benefits the
  interests of some shareholders or members, or of third parties.

limitada). The main difference is that shares are transferable securities, whereas stakes do not possess
those qualities (article 92 of the Corporate Enterprises Act).

See also question 28.
If there is a decision of the shareholders’ meeting of the insolvent company where these grounds can be validly asserted, shareholders can challenge the decision in the same way as they would when the company was solvent.

Under Spanish corporate law, it is also possible for shareholders and members to challenge the actions and decisions of directors of the company. This is only possible where decisions are taken by a board of directors, and requires that the shareholder or shareholders challenging the decision of the board represent at least 1% of the capital of the company (article 251 of the Corporate Enterprises Act).

There are no rules in the Insolvency Act that would indicate that shareholders lose their rights to challenge the decisions of the shareholders’ meeting or the board of directors. The Insolvency Act does not establish a distinction based on the fact that the board of directors in the insolvent company may have the function of managing the company in the interests of the insolvent estate, and, therefore, in the interests of the company’s creditors. It is fair to conclude that shareholders preserve their rights to challenge decisions in the insolvency of the company, notwithstanding the change in functions and status of directors.

There are numerous decisions of the courts where it is admitted that shareholders have the power to challenge decisions, despite the fact that the company is insolvent. See, for instance, SAP Madrid (Secc. 28) Judgment no. 34/2009, 16 February (AC\2009\858) (challenging the approval of the company’s accounts); or SAP Vizcaya (Secc. 4) Judgment no. 292/2011, 15 April (JUR\2011\302243).

Under general company law, shareholders have also the possibility of suing the directors for damages. However, actions for liability of directors are subject to a special regime in case of the insolvency of a company. The Insolvency Act contains an explicit special rule whereby only the insolvency representative has standing to sue the directors (article 48 quater of the Insolvency Act); and another special rule in the Insolvency Act establishes that the court, on its own motion or at the request of the insolvency representative, can seize the assets of directors who may be liable (article 48 ter of the Insolvency Act). These provisions are extraordinarily important in view of the extremely strict regime that Spanish insolvency law imposes on directors, and which results, in a large number of cases, in the personal liability of directors for the debts of the company.

Regarding the actions and decisions of the insolvency representative, the response is different. The Insolvency Act does not foresee a specific procedure designed to challenge the acts or decisions of the insolvency representative.

In essence, a person who disagrees with the decisions of the insolvency representative may try to seek its removal. Any person with standing to initiate insolvency proceedings can ask for the removal of the insolvency representative with cause (articles 33 and 37 of the Insolvency Act). However, according to article 3.1 of the Insolvency Act, only the board or the directors of the company have standing to initiate the insolvency process, so from this follows that individual shareholders, or even the shareholders’ meeting, lack the competence to dismiss or even to request the removal of the insolvency representative.
Shareholders do not have any legal tools to react against the acts or decisions of the insolvency representative.

15. Do shareholders have the right to call a special investigation of the affairs of the insolvent company?

Despite recommendations in reports and other official documents of the European Union, the right to call a special investigation does not exist as a matter of general company law in the Spanish legal system. Therefore, there is no question about its applicability in the case of an insolvent company.

16. Does the law provide for the establishment of a shareholders’ committee (or several committees, in case of different share classes)? What are their powers? Who bears the related costs?

There is no provision in the Insolvency Act for the creation of a shareholders’ committee. If such committee is created, it will be entirely the result of a private agreement and there are no functions allocated to it under company law or under insolvency law.

17. Can shareholders voluntarily transfer shares of the company undergoing insolvency proceedings against any provisions in the articles/bylaws restricting transfers of shares?

In principle, the rules on restriction of transfer of shares and of participations in limited liability companies would continue to apply during insolvency. Therefore, shareholders and members would be bound by restrictions to transfer, and can only transfer shares or stakes in respect of the rules established in the law and in the articles of association (article 106 ff. (stakes); and article 120 ff. (shares) of the Corporate Enterprises Act).

18. Can outstanding shares of the company undergoing insolvency proceedings be assigned to third parties without the consent of the relevant shareholders? If yes, under what conditions? Are existing shareholders entitled to compensation? What other safeguards are provided? (e.g., does the law include a principle according to which the affected shareholders should not receive less than in a liquidation procedure?)

Under general company law and general insolvency law, shares cannot be cancelled or expropriated to shareholders without their consent. Shares are the property of their holders and a cancellation or expropriation would amount to an illicit taking of property.

However, it is possible to undertake a capital reduction to adjust for losses, which can reduce the capital to zero, followed immediately by a capital increase (so-called “operation accordion”). Reductions of capital for losses must adhere to the principle of equality of shareholders (article 320 of the Corporate Enterprises Act). The interests of existing shareholders may be wiped out if the company is insolvent in a balance-sheet sense. However, it must be noted that

---

the capital reduction requires the agreement of a majority of shareholders, and that shareholders will retain their pre-emption rights over the shares issued in the capital increase (article 343 of the Corporate Enterprises Act).

19. Can outstanding shares of the company undergoing insolvency proceedings be cancelled without the consent of the relevant shareholders? If yes, under what conditions? Are existing shareholders entitled to compensation? What other safeguards are provided? (e.g. does the law include a principle according to which the affected shareholders should not receive less than in a liquidation procedure?)

Shares cannot be cancelled or expropriated to shareholders without their consent. As explained in the response to question 18 above, what is possible is to operate a capital reduction to adjust for losses and that capital reduction may eliminate the interests of shareholders if the company is balance-sheet insolvent.

Expropriation of shares would require the public interest justification that characterizes lawful expropriation under Spanish administrative law (see Expropriation Act, Ley de Expropiación Forzosa, December 16th, 1954, successively reformed). Expropriation for the protection of competing private interests is illegal.

20. Do shareholders of the company undergoing insolvency proceedings have pre-emption rights over new issues of shares? (11) Are there special conditions for the suppression of pre-emption rights if the company is insolvent (if there are separate reorganization and liquidation procedures, does this affect the response?).

In principle, shareholders retain pre-emption rights irrespective of the fact that the company is undergoing an insolvency process. However, the insolvency of the company –or, even, the financial difficulties of the company- would provide a suitable justification for the suppression of the pre-emption rights in a particular issue of shares. The suppression of the pre-emption rights in a capital increase requires the agreement of the majority of shareholders, but a capital increase may be delegated to the board of directors in public companies, and therefore the board of directors would also have the power to issue new capital without pre-emption rights for existing shareholders.

The question of the conditions for the suppression of pre-emption rights in issues of shares has been a particularly controversial topic in Spain, especially in the domain of large listed companies. There have been multiple revisions of the law, and extensive litigation, including a well-known case at the European Court of Justice (see below).

In general, the courts have been favourable to capital increases with suppression of pre-emption, whenever it has been possible to establish that the capital increase was in favour of the interests of the company as a whole. In this regard, it is extraordinarily interesting the case of the Supreme Court (STS [1st], Judgment no. 183/2009, 27 March (R)\2009\3288) where the capital increases

---

(11) Please, note that the power to decide new issues or conversions of shares, as well as the power to decide operations that affect the structure of the corporate entity (e.g., by merger, spin-off, or change of the legal form) are dealt with in Questions 33 and 34 below.
in Banesto, a listed banking company under the regime of banking supervision and under a regime of special administrative receivership, were analyzed. In this particular case, the administration of the bank considered that the best way forward for the company was a capital increase with suppression of pre-emption rights. The Court held that the suppression of pre-emption rights was justified, as the capital increase benefitted the interest of the company as a whole.

The Spanish regime for the suppression of pre-emption rights was examined in the European case of the ECJ of European Commission vs. Government of Spain (judgment of 18 December 2008, TJCE\2008\322). In this judgment, the European Court of Justice found that the Spanish regime was compliant with the requirements of the Second Company Law Directive. In the case, the rule under exam was article 159 of the then in force Public Companies Act (LSA), which set the following conditions for the suppression of pre-emption rights in the interest of the company. According to the article, when the shareholders meeting takes a decision of increasing the company's capital, it can also decide to suppress pre-emption rights in the interest of the company, provided that at the time the shareholders’ meeting is called, a report drafted by the directors is available to shareholders. This report must justify the proposal and the price at which the shares will be issued, it must indicate the persons to whom the shares will be allocated. An additional report by an auditor (different from the auditor of the company, and appointed by the Companies Registrar) must be attached, and it must give an opinion on the “reasonable value” of the shares of the company, on the theoretical value of the pre-emption rights that are to be suppressed, and on the reasonableness of the data included in the directors’ report. In addition, it is necessary that the amount of the nominal value (or par value) of the shares to be issued plus, if applicable, the amount of the issuance premium, corresponds to the “fair value” determined in the auditor’s report. If the company is a listed company, “fair value” is assumed to be equivalent to “market value”, and market value is presumed to correspond to the value reflected in the stock trades, unless there is a justification to the contrary.

For a listed company, the shareholders’ meeting, once it has received the directors’ report and the report drafted by the auditors –which must also refer to the net asset value of the company and its shares, can issue new shares at any price determined at a later stage by a specified procedure, provided that the price would be higher than the price resulting from the net asset value analysis.

This has been a very controversial procedure, and one of the most complex rules ever to appear in Spanish corporate law. In examining this article, the ECJ reached the conclusion that the reports included in the Spanish regime were additional safeguards to the regime of the Second Company Law Directive (article 29.4 of the Secon Company Law Directive, which only requires the directors’ report), and therefore found that the regime was compliant with European law.

The current rules for the suppression of pre-emption rights are included in

---

article 308 of the Corporate Enterprises Act, which coordinates the regime for limited liability companies and public companies. The general principle, again, is that the shareholders’ meeting can suppress, wholly or in part, pre-emption rights if the suppression is in the best interests of the company. In all cases, directors will have to prepare a report specifying the value of shares or stakes in the company and justifying the proposal in detail, including the price to be paid for the new stakes or shares to be issued, and the persons who will acquire them. In public companies (but not in limited liability companies), an auditor who is not the auditor of the company must prepare a second report on the “fair value” of the shares, the theoretical value of the pre-emption rights to be suppressed, and the soundness of the data included in the directors’ report.

The par value of the new shares or stakes (including a potential premium) must be in line with the fair value resulting from the directors’ report –and also the auditor’s report, in the case of public companies.

The regime also includes important procedural safeguards: the announcement convening the meeting must refer to the proposal to suppress pre-emption rights, the right to access to the relevant reports at no cost, among other procedural requirements.

For listed companies, similar rules apply, but the regime has some important specifications. The main qualification is that “fair value” corresponds to market value according to the trades executed in the market, unless a different value can be justified (article 504 of the Corporate Enterprises Act). In addition, there are a number of rules applicable to listed companies only (article 505 of the Corporate Enterprises Act):

- the directors’ and the auditor’s report must specify the net value of the shares of the company;
- the auditor will base the calculation of the net value of the shares on the last audited accounts of the company, and those accounts cannot be more than six months old; in the case of corporate groups, consolidated accounts will be used;
- a listed company can issue shares at any price higher than the net value indicated in the auditor’s report;

The suppression of pre-emption rights can be delegated to the board of directors in listed companies (article 506 of the Corporate Enterprises Act). In every increase, it is necessary to have a separate directors’ and auditor’s report, and the par value of the new shares must correspond with the fair value of the shares in the auditor’s report. The shareholders will be informed of the increases done at the first shareholders’ meeting held.

There are no special requirements for the suppression of pre-emption rights in the case of an insolvent company. First, the shareholders’ meeting continues to have the competence of the decision to suppress pre-emption rights. It is important, in this regard, to acknowledge the important precedent set by the jurisprudence of the European Court of Justice, which decided that the suppression of pre-emption rights is a competence of the shareholders’ meeting, and that the modalities of delegation, and the reasons for the suppression of the
pre-emption rights are those included in the Second Company Law Directive. A situation of economic crisis would not justify a special regulation that deprives the shareholders' meeting of its competence to decide on the suppression of pre-emption rights: see ECJ, Judgment of 24 March 1992, Syndesmos Melon tis Eleftheras Evangelikis Ekklisias / Greek State and others (C-381/89, ECR 1992 p. I-2111).

The question of the proposal to suppress pre-emption rights is more complicated. The company law regime is not prepared for the intervention of a third party, such as the insolvency representative, in the internal operation of the company. However, in companies where directors have been removed from office and the insolvency representatives has the managing powers, it seems logical that a proposal to suppress pre-emption rights would be presented by the insolvency representative, and that the insolvency representative would have to draft the report justifying the proposal. The fact that the company is insolvent is of course very relevant in the justification to suppress the pre-emption rights, and it would also affect the consideration of the fair value of the shares and stakes and of the pre-emption rights themselves. In many cases, the value of the shares or stakes, and the value of the pre-emption rights will be zero.

The delicate issue is to assign the responsibility of the proposal when the directors of the company continue managing it. This is a central issue of division of competences between the directors and the insolvency representative. The general principle of the Spanish insolvency Act is that the directors need the approval of the insolvency representative to perform any act that may have economic implications for the company. As this is clearly the case, the directors would have the responsibility of making the proposal and drafting the accompanying report, but they will require the authorization of the insolvency representative. The proposal will have to be approved by the shareholders’ meeting in any case. Spanish law does not recognize a different mechanism whereby pre-emption rights can be suppressed without the intervention of shareholders or members of the affected companies.

21. Can shareholders retain a participation in the company that has emerged from an insolvency process (or in the company to which the insolvent company’s assets have been transferred) even if the company was insolvent according to a balance-sheet test? (i.e., where the value of its liabilities exceeds the value of its assets) If yes, under what conditions? (If there are separate reorganization and liquidation procedures, does this affect the response?)

Shareholders can retain an interest in the company only under certain circumstances. If the company is liquidated, shareholders can only receive a payment after all claims have been satisfied, including subordinated claims (among the subordinated claims, Spanish law lists claims for interest accrued after the initiation of the insolvency process). It is therefore highly unlikely that shareholders will receive a payment in liquidation proceedings of an insolvent company. If the company is insolvent in the balance-sheet sense, and is liquidated, payment to shareholders is impossible.

The alternative is to adopt an insolvency plan. An insolvency plan can be proposed in any insolvency procedure, since the insolvency process is unitary
and therefore there is no formal differentiation of liquidation and reorganization. The insolvency plan provides a solution to the insolvency process that allows the company to be preserved. Once -and if- the company fulfils the payments established in the insolvency plan, the company will survive and the shareholders will retain whatever value is left in the reorganized company. This “pure payment plan” assumes, of course, that the company will be able to generate future income in a sufficient amount to make significant payments to creditors. In many cases, however, the plan can be a mixture of payment through the generation of future income and the sale of some strategic assets, or any other combination of operations to provide for payment. In these other cases, the division of value between creditors and shareholders may be complex. The fundamental rule, although it is not expressed in totally explicit manner in the law, is that the insolvency plan should respect the ranking of claims in establishing the returns to the different claims. The law mentions the possibility that some creditors receive special advantages (article 152 of the Insolvency Act)

The question mentions the possibility that a new company is created to which the assets of the original company are transferred. This typical “hive-down” scheme requires a separation of the profitable assets and lines of business; and the transfer, to a different legal person, of those assets, isolated from liabilities. In this context, if the company were balance-sheet insolvent, shareholders would not be entitled to receive a percentage of the shares in the new company holding the assets.

The distribution of shares in the new company would be part of the insolvency plan. The insolvency plan would include a distribution of shares to creditors, possibly together with other payments to be made to creditors. The plan would have to respect the ranking of claims under the law (see article 89 ff. of the Insolvency Act). This does not mean that an insolvency plan cannot include advantages for existing shareholders, but these advantages have to be freely conceded and accepted by the affected creditors in approving the plan. As a matter of fact, the Insolvency Act only refers to advantages given to a class of creditors, which have to be accepted by the creditors not comprised in the class benefited by the special treatment (article 125 of the Insolvency Act, which establishes that it is necessary that a majority of claims in the non-benefited classes votes in favour of the special treatment)\textsuperscript{13}. However, it is not inconceivable to apply this same provision by analogy and determine that shareholders can receive advantages if all classes of creditors accept that advantageous treatment\textsuperscript{14}.

An insolvency plan can also consist of a mix of a liquidation of some assets, and a debt/equity swap, so creditors would receive a partial monetary payment and shares in the company as in-kind payment. These are the most complicated

\textsuperscript{13}It is remarkable that the law refers to the classes not benefited by the special treatment, instead than referring to the classes of creditors prejudiced by granting special advantages to other creditors.

\textsuperscript{14}However, individual creditors lack defense mechanisms against the advantages potentially awarded to shareholders, as the law does not include a baseline protection measure in the form of a comparison between what the creditor would obtain in a liquidation of the company and what the creditor is obtaining under the insolvency plan.
cases, since it is possible that the existing shareholders retain some value in the company. If the company's capital is reduced to offset losses, and the company is insolvent, it would be necessary to reduce the capital to zero. However, there have been cases in which the original shareholders have retained a percentage of the capital of the company, despite the dilution operated by the issue of shares granted in exchange of debt.

In some cases, it may be doubtful whether the company is insolvent or not in a balance-sheet sense. If the company is clearly insolvent, the existing shareholders have no right to retain a percentage of capital. Creditors can deny shareholders the right to preserve a participation in the company: this can be done by rejecting all proposals for an insolvency plan, and thereby forcing the company into liquidation. It is also possible to present alternative insolvency plans, provided these alternatives plans are supported by at least one fifth of the claims in the creditors’ list (article 106 of the Insolvency Act). An alternative plan could deny any advantages to shareholders.

It must be remarked that Spanish law presents the peculiarity that there is no absolute freedom in the design of an insolvency plan. An insolvency plan can include a reduction in the amounts to be paid to unsecured creditors and/or a reschedule of payments, but in any case the reduction cannot be higher than fifty percent and the reschedule cannot last longer than 5 years (article 100.1 of the Insolvency Act). The insolvency plan may also include alternative proposals, such as conversion of loans into capital, or into hybrid instruments (article 100.2 of the Insolvency Act). It follows, from the tenor of the law, that the conversion of the loan into another type of instrument, especially into capital, requires the individual consent of the creditor, and it is not an option that can be forced on creditors (although the plan may establish the consequences in the case that creditors do not exercise an option –article 102 of the Insolvency Act).

The law is silent on the issue whether there can be a proposal in which the shareholders retain value but impose a reduction of debt and/or a rescheduling of debt at the same time. In any case, the law mentions explicitly that an insolvency plan cannot alter the ranking of claims (article 100.3 of the Insolvency Act). The ranking of claims (articles 89-92 of the Insolvency Act) does not even refer to the position of shareholders, who are only entitled to receive the residue of the liquidation once all creditors, including the subordinated creditors, have been paid in full. The idea of an insolvency plans that contains special advantages for certain persons has only been contemplated for advantages to creditors, and not to other parties, such as shareholders (see article 125 of the Insolvency Act).

In these circumstances, it is possible to assert that an insolvency plan that would contemplate advantages for shareholders could be challenged by any creditor (see article 128 of the Insolvency Act).

Another issue would be the execution of an insolvency plan by merger with another company, which is also foreseen as a possibility in the law.

The insolvency plan is presented by the debtor or by creditors representing 1/5
of the total claims (article 113 of the Insolvency Act). The proposal presented by the debtor is put first to the vote of creditors (article 121.2 of the Insolvency Act). The necessary majority is at least half of the unsecured claims (amount, not creditors) (article 124 of the Insolvency Act – there is a limited exception for insolvency plans that provide for immediate payment of 80 percent of the unsecured claims, or full payment of unsecured claims within a 3-year term: in these cases, it is possible to have an insolvency plan by simple majority).

22. Are the ranking of classes of shares and the preferential rights of classes of shares affected (and if yes, to what extent) by the fact that the company is undergoing an insolvency process? (If there are separate reorganization and liquidation procedures, does this affect the response?)

The ranking of classes of shares – in case there is one – is not affected by the insolvency process. The insolvency process does not rank shares, but only claims. Claims are ranked according to the rules in the Insolvency Act (articles 89-92 of the Insolvency Act). Regarding shares, the general rules on ranking apply: there is a general principle of equality of shareholders, and the only exception refers to non-voting shares and stakes. Such non-voting shares and stakes enjoy a priority for their value or the paid-up amount in the event of the liquidation of the company, over the proceeds of the liquidation, once all claims have been fully satisfied (article 101 of the Corporate Enterprises Act). In the case of an insolvent company (in the balance-sheet sense) none of the shareholders, whether they have voting shares or non-voting shares, will be able to receive any payment at all. In the case that there would be a residue after the liquidation of the company, the ranking of shareholders would be fully applicable.

23. Can shareholders, in the course of an insolvency procedure, supply goods, services or financial resources to the company? If yes, under what conditions (e.g., judicial authorization)? What would their ranking position be towards other creditors?

Shareholders can supply goods, services, or financial resources to their company undergoing an insolvency process. There are no special circumstances in insolvency law that justify a different treatment from the treatment which is applicable under general contract and company law. In this regard, the only consideration that comes into play is whether the directors contracting with the shareholders in the name of the company may found themselves in a conflict of interest, because of their condition of shareholders or because of their relationships with the shareholders contracting with the company. In such cases, the directors affected by the conflict of interest should reveal the conflict and abstain from acting (article 229 of the Corporate Enterprises Act). This rule would apply equally in a situation in which a company is insolvent, but continues trading under the management of its directors. The recent corporate reform has introduced the requirement of the authorization of the shareholder meeting for related party transactions where the value of the transaction is higher than 10% of the company’s assets. This would raise the interesting issue, of an insolvent company, of the shareholder meeting authorizing this type of transaction. If that threshold is not reached, the transaction can be authorized by members of the
board who are not affected by the conflict (art. 230 of the Corporate Enterprises Act).

In the case that the insolvent company is managed by the insolvency representative, there are no rules that subject the insolvency representative to stricter controls if the representative decides to sign contracts for the delivery of goods or services with shareholders of the company.

24. Can shareholders, in their capacity as counterparties, be under a duty to continue a contractual relationship with the insolvent company during an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?).

Shareholders are like any other contractual parties – they must comply with their contractual obligations and, if they do not perform, they will be liable for damages to the insolvent company (article 61 of the Insolvency Act). There is no implied or enhanced duty for shareholders as opposed to other contractual parties.

25. Can shareholders (or companies of the same group) holding credit claims against the company under insolvency procedure participate in the creditors’ meeting and vote on the insolvency plan without restrictions? (If there are separate reorganization and liquidation procedures, does this affect the response?)

Shareholders who are also creditors can participate in the insolvency process. However, shareholders who have a substantial interest (10% in unlisted companies, 5% in listed companies) will be automatically subordinated (article 92.5 and article 93.2 of the Insolvency Act). Companies belonging to the same group will also be automatically subordinated if they have claims against the insolvent company (article 93.2.3 of the Insolvency Act).

When creditors are subordinated, they lose the right to cast a vote at the creditors’ meeting (article 122.1 of the Insolvency Act), although these creditors still have the right to attend the meeting (article 118 of the Insolvency Act).

26. If shareholders (or companies of the same group) do not hold credit claims against the company under insolvency procedure, must/can they participate in the creditors’ meeting? If that is the case, what rights or duties do they have in that meeting? (If there are separate reorganization and liquidation procedures, does this affect the response?)

Shareholders do not have a right nor are under a duty to attend the creditors’ meeting (argument ex article 118 of the Insolvency Act). The debtor who is a natural person is under the duty to attend the creditors’ meeting (article 117 of the Insolvency Act), but the law does not provide anything regarding the right or duty of shareholders to attend the creditors’ meeting. In the absence of a specific rule, it seems that shareholders would not have a right –or a duty- to attend the creditors’ meeting.
27. Do shareholders in an individual company have information rights as to the filing of insolvency proceedings by the parent or other related companies?

Shareholders have no specific right to receive notice of such procedures, but of course they can exercise their right to request information (see response to question 11 above). In particular, the exercise of the right to request information may be particularly relevant in the case of listed companies, where the law refers to the possibility of inquiring about the information that has been publicly disclosed by the company (article 520 of the Corporate Enterprises Act). Given the fact that the insolvency of subsidiaries or other related companies can represent, in many cases, material information, it follows that the company must inform through the channels contemplated in the securities regulation regime, and shareholders will both gain access to that information and the possibility of formulating questions on the issue at the shareholders’ meeting (see response to question 7 above).

III. The Role of the Shareholders’ Meeting in Companies Subject to Insolvency Proceedings

28. Does the shareholders’ meeting continue to exist in insolvency proceedings? (If there are separate reorganization and liquidation procedures, does this affect the response?)

Spanish insolvency law is among the few insolvency systems that explicitly address this question: article 48 of the Insolvency Act states that during the insolvency process, the organs of the debtor who is a legal person will continue to function, “notwithstanding the effects over their functioning that are caused by the regime of intervention or suspension”\(^1\). Aside from this general rule, according to which the shareholders’ meeting will continue to exist even if the company is insolvent, there is a fundamental precision introduced by article 48.2 of the Insolvency Act. According to that provision, any agreement of the general meeting that “may have an economic content or implications for the insolvency process” has to be authorized or confirmed by the insolvency representative to be effective (see response to question 29 below).

Therefore, in Spanish law there is no question that the shareholders’ meeting continues to exist. As a matter of fact, the continuity of the shareholders’ meeting is taken for granted in numerous legal rules and judicial decisions.

The shareholders’ meeting needs to meet according to the requirements of generally applicable company law. This means that there has to be at least an annual shareholders’ meeting (article 159 of the Corporate Enterprises Act) and also that for any relevant transaction that requires the intervention of the shareholders’ meeting (for instance, a merger, or a capital increase), the shareholders’ meeting needs to be convened (see article 160 of the Corporate

---

\(^1\) “Intervention” refers to the situation in which the company directors continue to manage the company under the supervision of the insolvency representative. “Suspension” is the situation in which directors are removed from their management functions and the insolvency representative takes over the management of the company (see article 40 of the Insolvency Act, and response to question 12 above).
Enterprises Act). In addition, the shareholders’ meeting preserves its internal functioning rules, including its own chairperson. The insolvency administrator has the right to attend the shareholders’ meeting (article 48.1 of the Insolvency Act), but the insolvency representative cannot act as chairman of the shareholders’ meeting, otherwise the decisions taken by the meeting are null and void (see SAP Madrid (sec. 28), judgment no. 34/2009, 16 February (AC\2009\858) confirmed by STS [1st] 24.4.2012 [R] 2012, 6099]). The insolvency representative has the right to attend and the right to speak at the shareholders’ meeting, but that does not mean that the insolvency representative can perform the role of chairman of the meeting or otherwise influence its functioning. The shareholders’ meeting preserves its internal organization, and the insolvency representative should respect it. The insolvency representative can only attend and participate (see STS [1st] 24.4.2012 [R] 2012, 6099]).

Another important point refers to the “universal shareholders’ meeting”. Under general company law (article 178 of the Corporate Enterprises Act) this is the shareholders’ meeting that can be held without a prior announcement, when all shareholders are present and decide to hold a shareholders’ meeting. In Spanish jurisprudence, there has already been a case in which it was debated whether shareholders of an insolvent company could hold a universal shareholders’ meeting. Case law determined that a universal shareholders’ meeting can be held without the authorization or consent of the insolvency representative (SAP Madrid (sec. 28), judgment no. 321/2012, 26 October (JUR\2012\378444)\(^{17}\)). The rationale was that the impact of the insolvency process over the company law regime is limited to the managing and liquidation of the estate, but it should not go beyond what is necessary to ensure that the acts of the corporate organs do not interfere with the economic aspects of the insolvency process. Because the law establishes that any decision with an economic impact requires the authorization or consent of the insolvency representative, it follows that the shareholders’ meeting is free to take any decision, but decisions will only be effective, when they have economic consequences, when those decisions are authorized or consented by the insolvency representative. In this regard, the system should not impose a “preventive mechanism” whereby the shareholders’ meeting cannot take a decision just because the insolvency representative does not approve of it. On the contrary, shareholders should be able to decide to meet and take a decision on any particular issue, and it may be that the decision will be ineffective because it has economic implications and the insolvency representative does not agree with it. But this would not stop the shareholders from formally taking a decision. The court stated that it must be accepted that shareholders of an insolvent company may have a legitimate interest in adopting decisions that are consistent with the strategy that they consider the company should follow in the insolvency process, in such a way that, even if those decisions are ineffective, they can at least produce evidence of what the shareholders’ will was; and this could be useful, for instance, in litigation before the insolvency judge on the appropriateness of taking certain measures, or in litigation with the insolvency administrator demanding its liability for actions.

\(^{17}\) The issues addressed in this particular judgment were considered to be particularly complex, and that is the reason why the court did not award costs and fees to the winning party in the litigation.
contrary to the decisions of shareholders in the management of the company. The courts also mentioned that there are numerous situations in which a decision by the shareholders’ meeting is part of a legal obligation of the company (for instance, the approval of the accounts – see response to question 30 below). The act of deciding to meet as a universal shareholders’ meeting could not be considered a fraud on the law (article 6.4 of the Civil Code; (SAP Madrid (sec. 28), judgment no. 321/2012, 26 October (JUR\2012\378444)), and the agenda of the shareholders’ meeting, by itself, could not be considered illegal, although the decisions adopted on the points in the agenda could be ineffective due to the lack of consent of the insolvency representative and their impact on the company’s estate.

The reform of the Insolvency Act in 2011 (Law 38/2011, 10 October), introduced a new version of article 48.2 of the Insolvency Act, which states that shareholders cannot meet, whether as a regular shareholders’ meeting or as a universal meeting, without the presence of the insolvency representative. Because the law only refers to the “presence” of the insolvency representative, there is some debate as to the possibility of calling a meeting without the consent of the insolvency representative. In the case of a regular meeting, it seems that it would be possible to announce the meeting, but if the insolvency representative does not agree, it suffices for the insolvency representative not to attend the meeting in order to make it entirely void. Naturally, that course of action is also problematic, since the shareholders would attend the meeting and they could adopt decisions with the appearance of validity, and the meeting itself would create costs for the company, and it is not clear who would be responsible for such costs. In the case of a universal meeting, the presence of the insolvency representative equals consent. It is not conceivable that an insolvency representative would decide to stay at the meeting and at same time disagree with the idea of holding the meeting itself. At the same time, the decision of the shareholders to constitute themselves in shareholders’ meeting is not an illegal act, and there cannot be a preventive action to avoid a shareholders’ meeting being called or held, even if the points of the agenda may suggest the adoption of decisions that would impact the economic situation of the company (SAP Madrid (sec. 28), judgment no. 321/2012, 26 October (JUR\2012\378444)). Those decisions would be, in any case, ineffective without the consent of the insolvency representative.

One of the arguments that has been used against the possibility of convening shareholders’ meetings without the authorization of the insolvency representative is that convening the shareholders’ meeting may have already economic consequences for the company (the cost of the announcements and the organization of the meeting, which can be substantial in the case of listed companies) – although that argument would not operate to support a prohibition of holding a universal shareholders’ meeting.\(^\text{18}\).

The courts have taken the view that convening a shareholders’ meeting does not represent, per se, abusive conduct (SAP Madrid (sec. 28), judgment no. 321/2012, 26 October (JUR\2012\378444)). It is submitted that additional

\(^{18}\) That argument was dismissed in the case SAP Madrid (Sec. 28) 13 July 2010 (JUR 2010, 310613). But, naturally, the judgment has been overruled by the reform of the Insolvency Act introduced in 2011.
factors or circumstances should be present to consider that their shareholders are abusing their right of holding a meeting. The main element to understand that there is an abuse of right ("abuso de derecho") is the existence of a damage to an interest of a third party which is not protected by a specific legal provision (SSTS [1st] 4 February 1991 (RJ 1991\704); 21 December 2000 (RJ 2001\1082); 28 January 2005, ( RJ 2005\1829); 25 January 2006 (RJ 2006\612); 21 September 2007 (RJ 2007\5079). In addition, the damage must be "anti-social" or "immoral", and this quality of the damage can be appreciated by means of a subjective or objective test. The shareholders' meeting will continue even if and when the company undergoing the insolvency procedure enters the liquidation phase. In such situation, the company enters a dissolution phase (article 145.3 of the Insolvency Act; article 361 of the Corporate Enterprises Act), but, as in general company law, the dissolution and liquidation of the company does not imply that the shareholders' meeting disappears (article 371.3 of the Corporate Enterprises Act). The shareholders' meeting will only cease to exist with the completion of the insolvency liquidation, by judicial order (see article 178.3 of the Insolvency Act).

29. Does the shareholders' meeting preserve all of its competences, generally? (If there are separate reorganization and liquidation procedures, does this affect the response?)

The shareholders' meeting has the following competences, generally (article 160 of the Corporate Enterprises Act):

- a) Approval of the accounts, distribution of earnings and approval of management;
- b) Appointment and dismissal of directors, liquidators, and, where necessary, auditors, and the exercise of liability actions against them;
- c) Amending the articles;
- d) Increase and reduction of capital;
- e) Suppression or limitation of pre-emption rights;
- f) Transformation, merger, scission or global cession of assets and liabilities, and transfer of the registered office to a location abroad;
- g) Dissolving the company;
- h) Approval of the final liquidation balance;
- i) Any other matters stipulated by law or by the by-laws.

In addition, and according to article 161 of the Corporate Enterprises Act, the members or shareholders meeting can also issue instructions to the directors on how to conduct the company's business, or subject some management decisions to the authorization of the general meeting. The recent corporate governance reform has extended this possibility to all companies, since previously these instructions could only be issued by the members' meeting at limited liability companies.
In the case of insolvent companies, the general rule is that the shareholders’ meeting will retain all of these competences\(^{19}\). However, the main impact over the exercise of these competences comes from the rule in article 48.2 of the Insolvency Act, according to which, any decision of the shareholders’ meeting that “\textit{may have an economic content or implications for the insolvency process}” has to be authorized or confirmed by the insolvency representative to be effective. Therefore, although the shareholders’ meeting retains its competences, most of the decisions will require the authorization or confirmation of the insolvency representative. Another important conclusion stemming from this analysis is that the insolvency representative, on its own, cannot take the decisions that fall under the competences of the shareholders’ meeting. Therefore, it is imperative that the insolvency representative and the shareholders reach agreements if certain operations are necessary to restructure the company (for instance, a capital increase, or a merger).

30. Does the shareholders’ meeting need to approve the accounts of the distressed/insolvent company?

The Insolvency Act expressly states that, in case of intervention, the directors of the company still have the obligation to draft the accounts and subject the accounts to audit, under the supervision of the insolvency representative (article 46.1 of the Insolvency Act). In case of suspension, the legal obligation to draft the accounts and subject them to audit will correspond to the insolvency representative (article 46.3 of the Insolvency Act); the insolvency representative must also draft the accounts in the case that the directors have not performed that action in the months preceding the opening of the insolvency case (article 75 of the Insolvency Act). In all cases, the regime for the approval of the accounts is the generally applicable regime (see SSJM 1 Málaga 2 July 2007 and 10 April 2008)\(^{20}\), and therefore it is clear that the shareholders’ meeting needs to approve the accounts (article 160 a) of the Corporate Enterprises Act, see response to question 29 above). The courts have made it clear that the shareholders’ meeting of the insolvent company is competent to approve the accounts (see SAP Madrid (secc. 28), judgment no. 34/2009, 16 February (AC\,2009\,858))\(^{21}\).

Lack of approval of the company’s accounts may have a series of legal consequences, specially regarding the liability of directors (lack of approval of the accounts is frequently motivated by the lack of trust in the performance and

\(^{19}\) A possible exception is the competence to approve the final balance of the liquidation. Arguably, this competence only applies to liquidation of solvent companies, and not to the liquidation of a company subject to an insolvency process, where there are other control mechanisms in place.


\(^{21}\) In principle, when accounts are not approved and they are not deposited in the commercial registry, a “block” operates whereby it is not possible to register any act referred to the company (except the appointment and dismissal of directors, and the dissolution of the company). However, directors can remove the “block” if they prove that the accounts have been submitted to the shareholders’ meeting and have been rejected (article 378.5 and 7 of the Commercial Registry Regulation – see Royal Decree 1784/1996, July 19\(^{19}\), successively reformed).
actions of directors, and it may be followed by liability actions against directors). The lack of approval of accounts may also result in the consequence that the companies registry is blocked for any corporate transaction (with the exception of the dismissal and appointment of directors), for lack of deposit of the accounts in the companies’ registry (see article 378.7 of the Commercial Registry Regulation, Royal Decree of July 19, 1996, successively reformed). However, this harsh sanction can be avoided with the production, by the directors, of a certificate stating that the accounts were presented to the shareholders’ meeting but were rejected (article 378.7 of the Commercial Registry Regulation). This would be enough for the company to regain access to the registry, which may be absolutely crucial in a distressed situation, in which a capital increase, a merger or other corporate transactions may represent the best possibility for the survival of the company. For an insolvent company, the Insolvency Act includes some special rules regarding the lack of approval of the accounts. The insolvency representative may authorize the company to delay the fulfilment of the legal obligation of drafting the accounts for the financial year prior to the judicial declaration of insolvency to the month following the presentation of the inventory of the insolvency estate and the list of creditors (article 46 of the Insolvency Act). Approval of the accounts must take place in the three months following the expiry of the extension. This will be notified to the court and to the companies’ registry. With this notification, a delay of the deposit of the accounts shall not give rise to a block of the registry for the company, if the terms for deposit are fulfilled from the expiry of the said extended period to approve the accounts. The law indicates that all the documents forming the annual accounts must mention the legitimate cause for the delay (article 46 of the Insolvency Act).

31. Does the shareholders’ meeting have the power to dismiss directors – if directors are still in charge of the insolvent company? Can the shareholders’ meeting request the removal of the insolvency representative? (If there are separate reorganization and liquidation procedures, does this affect the response?)

The general power to dismiss directors at any moment is an essential competence of the shareholders’ meeting (article 223 of the Corporate Enterprises Act). In a limited liability company, it is possible to limit this right by establishing a supermajority requirement to dismiss the directors, but the supermajority requirement cannot be higher, in any case, than two-thirds of the capital of the company. In any case, there does not seem to be an obstacle for the shareholders’ meeting to remove the directors, even if those directors are managing the company under the supervision and control of an insolvency representative. The shareholders’ meeting could also remove the directors when they have been suspended and, therefore, do not perform any management functions in the insolvent company. Although that removal will be less useful, it is conceivable that the shareholders could want to replace their directors even when they do not have any managing functions in the company, as directors continue to represent the company in the process. The new directors appointed by the shareholders’ meeting will be subject to the same regime of suspension or intervention as those who were dismissed, but the insolvency representative

What the shareholders cannot do is to initiate liability actions against the directors (see article 48 quarter of the Insolvency Act; and response to question 14 above).
may apply to the court for a change of their situation (see article 40.4 of the Insolvency Act).23

The solution for the dismissal of the insolvency representative is totally different. An interesting rule in the Corporate Enterprises Act states that the shareholders’ meeting can dismiss the liquidators, except in the case in which the liquidators have been appointed by the court (article 380 of the Corporate Enterprises Act). From this rule, it follows, logically, that the shareholders’ meeting cannot dismiss the insolvency representative.

32. Is a shareholders’ meeting authorisation required to start an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?)

The rules for the initiation of the insolvency process determine that the persons or organs with representative powers are the only ones who can present an insolvency petition on behalf of a legal person, such as a company (article 3.1 of the Insolvency Act). Therefore, it is for the directors to present a petition for the initiation of an insolvency process, and the shareholders’ meeting does not have the competence to initiate the process, and not even the role of confirming the directors’ decision.

33. Does the shareholders’ meeting need to approve an insolvency or reorganization plan? Can shareholders, even individually, challenge an insolvency or reorganization plan?

An insolvency plan is approved solely with the votes of creditors (article 124 of the Insolvency Act).

However, article 117.2 of the Insolvency Act indicates that the debtor needs to attend the general meeting, or a representative with power enough to negotiate and accept compositions.

Article 128.3 of the Insolvency Act allows the debtor to oppose the approved insolvency plan for breaches of the rules regarding content of insolvency plans or for breaches of the procedural rules for the composition (article 128.1 of the Insolvency Act). This challenge is only admissible when the debtor has not expressed approval for the composition at the creditors’ meeting, and the challenge involves a request to liquidate the company. Therefore, consent of the debtor is not necessary.

The law is silent on how and who can consent in the name of the debtor, when the debtor is a company; and on whom and how can challenge the composition, in the case of the insolvency of a company. In principle, it seems that the directors, as the persons representing the company, would be the ones competent to agree to compositions or to challenge compositions. However, it is

---

23 So, for instance, if the shareholders’ meeting decides to remove the directors who have been managing the company in a satisfactory way, and replace them with directors that have been, in the past, responsible for the deterioration of the finances of the company, the insolvency representative could apply to the court to seek the suspension of the newly appointed directors and therefore the transfer of managing powers to the insolvency representative.
possible that the shareholders decide to remove the directors if they disagree
over these or other decisions (see response to question 31 – this may be one of
the reasons why the shareholders could decide to remove the company directors
even in a situation in which those directors are not managing the insolvent
company).

34. Is a shareholders' meeting decision required to issue new shares of the company
undergoing insolvency proceeding? Can a new share issue be decided by the board?
Can a new share issue be decided by the insolvency representative? (24) If a capital
increase has to take place through the conversion of claims into new shares, does
this affect the response?

A new issue of shares will require a modification of capital in the articles, and all
modifications of the articles belong to the competence of the shareholders’
meeting (articles 285 and 296 of the Corporate Enterprises Act) (25). Capital
increases require reinforced majority vote, as all modifications of the company
statutes (articles 288 and 199 of the Corporate Enterprises Act). The Insolvency
Act expressly refers to the need of the shareholders’ meeting decision for a plan
that includes a debt/equity swap (article 100.2 of the Insolvency Act).

The limited exception to the principle of competence of the shareholders’
meeting over capital increases is the possibility of a delegation to the directors of
the power to execute capital increases, in public companies (26). Absent that
delegation, a decision of the shareholders’ meeting is absolutely necessary to
increase the capital of the company. The fact that the company is undergoing an

(24) These questions are aimed at understanding whether the fact that the company is subject to
insolvency proceedings allows or causes deviations from the company law rules determining the body
competent to take decisions on the issue of new shares of the company and/or establishing the criteria
and purposes with which such decisions must comply.

(25) European law establishes, for public companies, that only the shareholders’ meeting is competent to
issue shares: see article 29 of the Second Company Law Directive (Directive 2012/30/EU of the European
Parliament and of the Council of 25 October 2012): "Any increase in capital must be decided upon by the
general meeting".

The exception would be the case in which the shareholders’ meeting had delegated the capital increase
to the directors, in which case the directors can take the decision to execute that capital increase, within
the limits and conditions set by the shareholders’ meeting (article 297 of the Corporate Enterprises Act).
The delegation is only applicable to public companies (not to limited liability companies) and cannot last
for more than five years since the shareholders’ meeting decision. The Insolvency Act does not mention
the delegation and the effects of the procedure over it. However, if the directors are removed from
management, the questions is whether the insolvency representative would be able to use this power (I
am inclined to say no, because the insolvency representative manages the company, but does not take the
corporate position of the directors, and there is a fundamental change of circumstances that may affect
the validity of the delegation). The other possibility is that the directors would continue to manage the
company even after the insolvency process is initiated. In this case, the directors could decide to use the
power to issue new shares – but presumably this would require the authorization of the insolvency
representative, since the capital increase represent a decision of an organ of the company (the board, in
this case) and has obvious economic consequences over the company. It is irrelevant that those
consequences may be positive– the system is based on the principle that the insolvency representative
needs to authorize any decision with economic consequences, and it is for the insolvency representative
to assess whether the consequences would be negative or not, and that would determine the use of its
authorization power.
insolvency process does not alter the balance of power and the distribution of competences between the corporate organs. Of course, it would be possible that the shareholders’ meeting decides to grant a delegation to the directors to increase capital, but that delegation would be the same delegation that would be used outside insolvency, with the sole difference that the insolvency representative should authorize or confirm this delegation, and also authorize or confirm any of the decisions taken under this delegated power from the shareholders’ meeting.

In the case of suspension of the directors, it is not clear whether the shareholders’ meeting could delegate the power to issue shares to the insolvency representative. Although the insolvency representative has the power to manage the assets of the insolvency estate, its appointment does not give the insolvency representative a position within the internal organization of the company, and therefore the insolvency representative can only perform the duties assigned to it by the Insolvency Act, without becoming a director of the company. Therefore, it would not be possible to delegate the power to issue shares to the insolvency representative, even in the case of suspension of powers of the directors of the company.

It is interesting to note that, as described in the response to question 3 above, recently Spanish law has introduced the possibility that shareholders are personally liable for their contribution to the failure of a restructuring agreement that includes a debt/equity swap (see article 172.2.1 of the Insolvency Act, in connection with article 165.2 of the Insolvency Act). In fact, the shareholders of a company may become liable for the company's debts if they refuse to enter into a refinancing agreement based on a debt/equity swap that has been considered reasonable by an independent expert, and that recognizes their pre-emption rights. The liability of shareholders can be determined according to their respective contribution to the formation of the majority that refused the plan. In the insolvency context, no such provision exists— as there are distinguishing factors— but there is a chance that the existence of this new rule will influence the judicial analysis of the behaviour of shareholders in the context of insolvency plans.

35. Can an insolvency/reorganization plan affect the structure of the corporate entity (e.g., by merger, spin-off, or change of the legal form)? Is a shareholders’ meeting authorization required for this?

The law refers explicitly to plans with the conversion of claims into equity (article 100.2 of the Insolvency Act). Mergers and spin-offs are also mentioned in the Insolvency Act (article 100.3 of the Insolvency Act). It is possible to conclude that an insolvency plan may affect the structure of the corporate entity, but it

---

27 The main difference is that, once the company has been declared insolvent, the behavior of shareholders does not create the type of damage that is typically covered is the damage derived from the delay in the initiation of the insolvency process. Therefore, to establish the liability of shareholders from not entering into a debt/equity swap within the insolvency process, liability would have to be defined and justified in a different fashion.
would be necessary to follow the prescribed procedures for each of the relevant structural changes (capital increase, merger, spin-off, etc.). A change of the legal form is not mentioned in the law, but there is no fundamental objection to a transformation of the company in another legal form as part of the arrangements included in the insolvency plan.

Therefore, a shareholders’ meeting authorization as such is not required, since what is required only, for the approval of the plan, is the assent given by the representatives of the company or at least, that the representatives of the company do not object the insolvency plan approved by the creditors’ meeting (see response to question 33). However, what could happen is that, after an insolvency plan has been approved, the shareholders’ meeting of the company fails to adopt the necessary decisions to implement the structural changes contemplated in the plan. If that is the case, the debtor would have defaulted on the insolvency plan and the liquidation phase of the insolvency proceedings will be opened (see articles 140, 142 and 143 of the Insolvency Act).

36. On what conditions can the company carry on business during an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?). Is a shareholders’ meeting authorisation required?

The general rule is that the company continues its activities despite the opening of the insolvency process (article 44 of the Insolvency Act). There is no need of an authorization of the shareholders’ meeting to continue trading.

The activities of the company are discontinued in the case that an “accelerated” or “early liquidation” is opened (article 142bis of the Insolvency Act), and in the situation in which an insolvency plan is not passed and the liquidation phase opens (article 142 of the Insolvency Act).

37. In the course of an insolvency procedure, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business operation of the company? Is a shareholders’ meeting authorisation required? (If there are separate reorganization and liquidation procedures, does this affect the response?)

Insolvency law gives priority to the sale of the business as a going concern (article 149.1 of the Insolvency Act). Sales of assets—other than sales in the ordinary course of business—have to be done in the context of the liquidation phase of insolvency proceedings, or as part of an approved insolvency plan. As such, the liquidation process is directed by the insolvency representative, and controlled by the creditors and the court. There is no recognized role for the shareholders’ meeting in the liquidation process.

Under general company law, the authorization of the shareholders’ meeting is not required to sale corporate assets. The exception is the so-called “cesión global de activo y pasivo”, which represents a bulk sale of all the corporate assets and a transfer of all corporate liabilities. This amounts to a de facto structural alteration of the company and, consequently, requires the authorization of the shareholders’ meeting (articles 160 and 195 of the Corporate Enterprises Act). However, it is not logical to request this authorization in the case of a liquidation of the company within an insolvency process. Contrary to corporate
transformations (see response to question 35), the liquidation of the company's estate does not require any action on the part of the company's organs.

In the case of listed companies, there are recommendations in the corporate governance code that important transactions are submitted to the consideration of the shareholders' meeting. Indeed, the Spanish Unified Corporate Governance Code (recommendation number 3) recommends that the shareholders' meeting votes on the acquisition or sale of key operating assets that would effectively alter the corporate purpose. This is merely a “comply or explain” recommendation, and it is unlikely that it would have any effect in the context of the insolvency of a listed company (as a matter of fact, the company could offer the valid explanation of the existence of the insolvency process as the justification for not compliance with the recommendation).

38. Does the shareholders’ meeting have any power in relation to a decision of the board or the insolvency representative to continue or reject any favourable, unfavourable or essential contract during an insolvency procedure? (If there are separate reorganization and liquidation procedures, does this affect the response?).

The shareholders’ meeting has no power regarding the continuation or rejection of executor contracts in insolvency. Under the Spanish Insolvency Act, a motion to terminate a contract can be put before by insolvency court by either the insolvency representative –in the case of suspension- or by the administrators of the company –in the case of intervention-. The decision to terminate the contract belongs to the competence of the insolvency court (article 61.2 of the Insolvency Act).

39. If an insolvency plan can be presented for a whole corporate group, must that plan be approved by the shareholders’ meetings of each company of the group, including of those that are balance-sheet insolvent? How are the different meetings’ decisions coordinated? Are there specific safeguards (e.g., any veto power or other remedy) for the minority shareholders of the companies that are not insolvent?

As stated before (see response to question 33), the shareholders’ meeting does not vote or approve the insolvency plan. This applies to other insolvent companies of the same group.

Spanish law does not contemplate the existence of group-wide insolvency plans. It would be possible, however, that separate plans would be coordinated, or that a general plan is drafted for a group of companies, and the creditors for each company would be able to decide to adhere to this general plan. In this regard, there are some special rules that are applicable: most importantly, it is possible to include conditions in the insolvency plan of a company based on a certain content being included and approved in the insolvency plan of another company of the same group (article 101.2 of the Insolvency Act). This facilitates the coordination of insolvency plans within groups of companies.

As with the situation in a single company’s insolvency, the shareholder’s meeting of each of the affected insolvent companies does not have to vote on the plan, but the company may agree to the insolvency plan, or may challenge the insolvency
plan. Those decisions belong to the competences of the representatives of the companies. There are, however, ways in which the actions of the different companies can be coordinated, including solvent and insolvent companies: A rule in the Insolvency Act establishes that the insolvency representative can request the court to be attributed the voting rights that the company has in other companies, inasmuch as the economic rights of the insolvent company are affected (article 48.5 of the Insolvency Act). This is also relevant for the response to the question on solvent companies belonging to the same corporate group. Indeed, participating in an insolvency plan for one of the companies of a corporate group (whether it is the parent company or one of the subsidiaries) is a decision that can be taken by the representatives of the relevant company. Insofar as the participation in the plan requires a structural transformation of the company, a decision of the shareholders’ meeting may be required, and it is in that scenario that the control of the votes by the insolvency representative of the parent company may be decisive in the company reaching the decision. On the question of the protection of minority shareholders, those shareholders can sue the representatives of the company for liability of their actions have prejudiced the interests of the company, and they can challenge the decisions of the shareholders’ meeting for breaching legal rules or for damaging the interests of the company. There is no explicit rule that provides a defence based on the concept of the “interest of the corporate group as a whole” in Spanish law.

40. If companies belonging to the same group file separate insolvency proceedings, are there specific requirements/mechanisms to provide for coordination of those proceedings? Are shareholders’ meetings of the relevant companies involved in the coordination mechanisms, if any?

There coordination mechanisms applicable to the insolvency of corporate groups, such as the possibility of joint petitions for insolvency (article 25 of the Insolvency Act) and the possibility of accumulating insolvency cases of companies belonging to the same group (article 25 bis of the Insolvency Act). In both cases, the insolvency procedures will be coordinated, although the insolvency estates will normally be kept separate. Exceptionally, in cases of confusion, there may be a joint inventory and a joint list of liabilities (article 25 ter of the Insolvency Act).

The coordination of the procedures is ensured by having the same competent court (article 25.4 of the Insolvency Act) and the possibility of appointing the same insolvency representative for all procedures (article 27.5 of the Insolvency Act). The insolvency representative may be assisted by other staff in other companies of the group.

The shareholders’ meetings of the relevant companies are not involved in these coordination mechanisms. The role of the shareholders’ meeting of each company is the one described for the general meeting in the responses to the questions of this part of the questionnaire.

IV. Other Obstacles for Insolvency Procedures Found in Company Law
41. Please list any other legal provision in company law that, in your opinion or in your experience, may interfere with the insolvency procedure of a company in your jurisdiction.

A problem may exist in the regulation of convertible bonds, since these hybrid securities may give their holders some of the rights that shareholders enjoy. This may have an impact in the case of the regulation of pre-emption rights. As a matter of fact, one of the aspects of the Spanish Company Law regime that was declared contrary to European law by the European Court of Justice was the regime of the suppression of pre-emption rights for convertible bonds. The regime for such suppression was, paradoxically, more protective of bondholders than the general regime was for shareholders.

The application of the general regime to challenge the decisions of companies (See response to question 14 above, and articles 204-208 of the Corporate Enterprises Act) to complex corporate transactions, such as mergers, spin-offs, or a transformation of the company, creates significant risks for such transactions in the context of a delicate restructuring process. It is perhaps too easy for shareholders to sue the company and obtain leverage in a negotiation, even resulting in situations in which the whole insolvency process is held hostage.

Outside the scope of company law, an important obstacle was removed by the exemption from a compulsory takeover bid in the context of insolvency process. The Takeover regulation establishes that acquisitions of control that are done in a company in crisis, whether insolvent or not, and whether by way of debt/equity swap or not, are exempt from the obligation to launch a takeover bid if they are done to safeguard the viability of the company (article 8 d) of the Royal Decree 1066/2007, on Takeover Bids. The exemption had to be granted by the Securities Commission (CNMV), but it was not automatic and the Commission retained certain discretion. Obtaining the exemption is crucial for an insolvency plan to succeed in the situation described. That is the main reason why the Royal Decree-Law 4/2014 has introduced a system in which acquisitions of control as a result of restructuring arrangements are exempt from a compulsory takeover bid without the need of authorization of the CNMV (see Final Provision Number 8 of the Royal Decree-Law 4/2014).