

Rules to determine directors' remuneration: a case where Article 217(4) of the Companies Act applies

The Supreme Court applies the rules set out in Article 217(4) of the Companies Act to reach a decision concerning the contest of a board resolution that determined the remuneration of a company director.

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In December 2016, the remuneration in 2017 (90,000 euros) of a private limited company's sole director was approved in general meeting. The company's articles of association provided that the position of director would be remunerated and that such remuneration would be determined for each financial year by a general meeting resolution. Leaving aside other details of the dispute, the relevant point is that this resolution was contested by the minority shareholder (holding 49% of the share capital).

After such contest failing in the court of first instance and next succeeding at the Las Palmas de Gran Canaria Provincial Court, the Supreme Court (Judgement no. 194/2025 of 7 February [ECLI:ES:TS:2025:505]) allowed the defendant's appeal for breach of procedure after concluding that the Provincial Court made a prejudicial error in taking as the company's profits for 2016 the sum of 58, 306.22 euros (strictly speaking, this was the profit for 2014) instead of the correct figure of 2,879,090.86 euros. This error was, according to the Supreme Court, very relevant

in the Provincial Court's assessment of the justification of the approved remuneration and, in particular, the proper conduct of the proportionality test referred to in Article 217(4) of the Companies Act (LSC).

Vacating the appealed decision, a new judgment was given on the matter, in which the 'cassation' appeal lodged by the defendant company was rejected.

Given that the contest was based on harm to the company's interests for the benefit of the majority shareholder (who, as sole director, was the recipient of the remuneration), the Supreme Court focused its analysis on the legal criteria for determining directors' remuneration (Art. 217(4) LSC). In essence, it stated the following:

- a) The aforementioned article provides some guiding rules for the determination of remuneration, within the parameters of business judgment. These rules can also guide a court's examination in vitiated resolution contests.
- b) It must be assumed that, in principle, the board of directors is sovereign when it comes to determining the amount of directors' remuneration. Hence, in a scenario of a company resolution contest on the grounds of harm to the company's interests, a court's examination focuses on checking for any abuse that could distort the meaning of remuneration, which is nothing else than compensation for a role with the burden of responsibility that it entails (always, as the aforementioned ruling points out, under the legal guidance to "promote the company's long-term profitability and sustainability"). For these purposes, the formula provided by the aforementioned article is that of

reasonable proportionality between the remuneration and the importance of the company and its financial position at any given time, as well as the market standards of comparable companies, if any.

- c) In the litigious case, in order to evaluate the importance of the company and its financial position, the end of the 2016 financial year, when the contested resolution was passed, had to be taken as a reference, and not the situation two years earlier, when a profound renovation of the hotel was carried out.
- d) The importance of the company and its financial position at the relevant time were determined by the following circumstances:
 - 1) the company, in addition to other assets (two properties), was the owner of a hotel, in which it had carried out significant renovations that had allowed it to improve its operation, the management of which was entrusted to a hotel group;
 - 2) the hotel had grown from 110 to 150 units, a 56-space car park was built, three restaurants were added (there used to be one) and the company went from having 24 workers to more than 100;
 - 3) in 2016 the company's profits were 2,879,090.86 euros.
- e) In view of the above parameters, the Supreme Court did not find an excessive disproportion that would distort the meaning of the remuneration agreed for the directors (which is to reasonably remunerate the work

of directing the company), nor did it find that it became a spurious channel to divert the possible distribution of profits among the shareholders or that it negatively affected the company's capitalisation. In this regard, the judgement under consideration stated that the figure for profits achieved in 2016 (2,879,090.86 euros) was very significant, with respect to which the amount of

the director's remuneration for the following year (90,000 euros) does not appear disproportionate. To this it should be added that, according to the established facts, although the management of the hotel had been entrusted to another company, neither the role nor the liability of the position of company director had not been emptied of content.