CONFUSION SURROUNDS STATUS OF COMPANY DIRECTORS SERVING AS EMPLOYEES - BDO

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Category: Employment

Under Spanish law the status of a company executive officer who holds the position of general manager, or of senior executive (*"alto directivo"* in Spanish) and, at the same time, is a member of the board of directors of the company that employs them, can be confusing for foreign investors.

This confusion stems from the criteria of Spanish judges, which can be summarised as the "*sole relationship theory"* (in Spanish: "*La teoría del vínculo único")*. This makes it very difficult for a company director to be bound to said company with two different and simultaneous relationships: Firstly, as a member of the board of directors, subject to company law, and secondly as an employee, subject to Spanish employment law.

Consequently, the "*sole relationship theory"* forces us to conclude that it is very difficult for an executive officer of a company operating in Spain to be a member of the board of directors and simultaneously, to have a valid contract of employment with the same company.

Therefore, when confronted with these cases, both parties, that is the executive officer and the company, have to decide whether to define their relationship solely as a mercantile relationship or alternatively, as an employment relationship. If the parties agree that they are bound solely by a contract of employment, then the executive officer cannot be a member of the board of directors of the company. However, in practice those decisions are not easy.Since on many occasions shareholders want the chief executive officer of the company to hold the position of managing director (that is member of the board of directors with full executive powers), but with remuneration and bonus terms stipulated in a contract of employment.

In December 2014 certain substantial changes were introduced into Spanish company law in relation to remuneration, incentives and bonuses, and severance pay – in cases of termination – to be paid to the executive members of boards of directors, and particularly to managing directors. A significant number of lawyers in Spain interpreted that the new legal framework (especially art. 249 of the Capital Companies Law) allowed executive officers to be members of company boards of directors and simultaneously be bound by a valid contract of employment.

However, the consequences of the above legal changes in company law are complex since they conflict with the above mentioned criteria of Spanish labour judges who, in the end, and under Spanish law, are the only authority entitled to decide whether any relationship can be classified as a contract of employment. In relation to this matter, we must indicate that judgements from Spanish labour courts (including the Supreme Court), issued after the 2014 changes in company law came into force, have not modified their points of view and they continue to reject the possibility of an executive officer, who is a member of the board of directors of a company, to be simultaneously linked to the same company by a contract of employment as a general manager.

However, we are of the opinion that this issue is not a closed matter and that Spanish labour courts could change their criteria in the future and accept the possibility that, according to article 249 of the Spanish Capital Companies Law (in force since December 2014), an executive member of the board of directors of a company could also be bound by a valid contract of employment to the same company. This change might even be enforced by a judgement from the European Court of Justice.

Whilst we are aware that a change in criteria may occur in the future, we must now draw attention to

a very recent judgement, dated June 2017, from a Madrid labour court which declares that the president of a bank who started his career many years ago in the bank as a normal employee, and then benefited from several promotions to said position of president, cannot be bound by a contract of employment to the bank since he was holding simultaneously the position as an executive member of the board of directors. This judgement, obviously reaffirms the "*sole relationship theory.*" But the relevant point of this judgement is that since said claimant had been promoted to the position of an executive member of the board of directors of the bank, he cannot later ask for his former contract of employment to be revived. The legal grounds on which the judge based his decision in said judgement are that both parties did not formally agree, at the very time of the promotion, for the contract of employment to be suspended during the period when said employee was to be a member of the board of directors.

The practical conclusion of said case is that, if the general manager or the senior executive is bound to the company by a contract of employment, and he is then promoted to the position of member of the board of directors of the same company, before the promotion is effective, the parties must agree to suspend the contract of employment for the period while the executive officer holds the position of member of the board of directors. If said suspension is not formally agreed, then the contract of employment will terminate automatically as a consequence of the employee´s promotion to the board of directors.

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