Corporate Governance

Contract or pre-contract agreement for the appointment of an obligee as CEO of a listed company

On the validity of a pre-contract agreement for the appointment of a director of a listed subsidiary.

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1. The facts

The claimant XXX had been engaged until 2014 and for 27 years in the professional activity of senior management of the Swiss HOLCIM Group and chairmanship of the board of directors of the Group's subsidiary in Spain and of other subsidiaries. The HOLCIM Group was listed on the Zurich Stock Exchange in 2014 and in said Group the claimant, in addition to his operational responsibilities of supervision and management of the Group's wholly-owned or investee companies in the Africa and Middle East region, held the position of director, director-chairman or chairman of the Board of several subsidiaries of the Group in several countries. FCC, the defendant, is the controlling company of a major Spanish corporate group, focused mainly on construction and related businesses, including cement, in which it is involved through its subsidiary Cementos Portland Valderribas, S.A. (CPV), which in turn is the principal or controlling company of its own corporate group (GCPV). FCC holds 71.58% of the share capital of CPV; consequently, as the controlling shareholder, it exercises control over the decisions adopted in CPV, including those relating to the appointment and removal of the members of the Board of Directors of CPV. Since the end of 2013, YYYY was Vice-Chairman of the Board of Directors and managing director of FCC, positions he held throughout 2014. Previously, from 16 February 2012 until

27 February 2013, he had held the position of Chairman of the Board of Directors of CPV. In 2012, YYY proposed to XXX that he assume the position of managing director of GCPV. The offer was initially not accepted, but was reiterated at the end of 2013, at which point the claimant was willing to accept it. A series of conversations and negotiations thus began for the appointment of XXX, which was to take place effectively at the end of 2014 or beginning of 2015 because at that time the CEO of the CPV Group, Mr. Evaristo, was leaving due to the termination of his contract. The rest of the members of the Board of Directors of CPV, as well as the principal shareholders (controlling shareholders or shareholders with significant influence) of FCC, also took part in these conversations and negotiations. Thus, on 29 July 2014, Mr. Evaristo informed the claimant by email of the willingness of the FCC Group and CPV to appoint him as board member and managing director of CPV, with the intention that the claimant succeed Mr. Evaristo upon leaving office. The appointment was to hold the position of member of the Board of Directors of a commercial company, which required a prior resolution of the Board of Directors, subsequently ratified at the general meeting of shareholders and additionally, in order to be appointed managing director, the agreement of at least two thirds of the members of the Board of Directors, all in accordance with the Spanish Companies Act and CPV's articles of association. These decisions depended on FCC in its capacity as majority and controlling shareholder. Prior to the passage of these resolutions, a favourable report or proposal was required from the Appointments and Remuneration Committee of the Board of GCPV (the body responsible for informing or proposing to the Board of Directors the resolutions to be passed in relation, among others, to the appointment, re-election, ratification and removal of directors, establishment and control of the company's directors and senior management remuneration policy).

The Committee discussed the appointment of the claimant as new board member and managing director at its meeting of 24 September 2014. Finally, the Committee agreed to propose to the Board of Directors of CPV the appointment of XXX as managing director with effect from 1 December 2014, while setting the financial terms of this appointment. That same day, this proposal was reported to the Board of Directors of CPV, which agreed to take note of it, pending the appointment of XXX to be proposed on the agenda of a new Board meeting. This matter was also discussed at the Board of Directors of FCC held on 25 September 2014.

On 26 September 2014, YYYY, in his capacity as vice-chairman and managing director of FCC, sent a letter to the claimant in which he welcomed him to the Group, while informing him of the financial terms approved for his entry; among them FCC undertook to contribute to the claimant's pension funds the amount of 120,000 euros, and in the event of compensation, to the gross contribution for 5 years to the pension scheme, decreasing as each year passed the proportional part of the same. As regards the date of payment, it was noted that it was pending confirmation by XXX.

Once this had been done, it was necessary for the claimant to terminate his relationship with the HOLCIM group. Mr Juan María's contract with Holcim contained the stipulation that, if he decided to leave the Group for any reason, he should give at least twelve months' notice. However, when the claimant informed the Holcim Group of his decision in October 2014, the Holcim Group accepted the termination of the relationship without the need to wait for the notice period, and an agreement was reached to set 31 December 2014 as the effective termination date. To this end, a “Mutual Termination Agreement” was signed between the claimant and Holcim, which was sent by the company on 25 November 2014 and signed by the claimant on 3 December 2014. This termination was to be notified to the Zurich Stock Exchange, which delayed the actual signing of the agreement.

Once the above formalities had been completed, it remained to convene the Board of Directors of Cementos Portland Valderribas (CPV) at which the appointment of Mr. Juan María was to take place, an appointment that also had to be accepted by the Board of FCC. The date set for this purpose was 12 January 2015, as the appointment could not take place on the initially scheduled date of 1 December 2014.

Notwithstanding the foregoing, at the end of November 2014, the negotiations that had begun some time earlier between FCC and Control Empresarial de Capitales S.A. de CV, a company wholly owned by Inmobiliaria Carso, S.A. de CV, which in turn is controlled by the DDD family, were concluded. As a result of these negotiations, the Board of Directors of FCC passed on 27 November 2014 the resolution to implement the capital increase agreed at the General Meeting held on 20 October 2014. Control de Capitales SA de CV proceeded to subscribe a total of 66,794,810 new FCC shares, which led to the entry of a new investor in the group, and as a result of the negotiations held, a new balance in the composition of the Board of Directors of FCC, with the entry of new directors proposed by the new investor, which ultimately also led to the entry of new directors in the companies in which FCC has holdings, including CPV. This ultimately determined that the person appointed as managing director of CPV was not the claimant but Mr. Braulio, which took place on 26 February 2015.

XXX filed a lawsuit against FCC requesting that it be held liable for the harm caused to the claimant for breach of contract and ordered to pay compensation in the amount of 6,754,801 euros, plus legal interest, concluding with Judgment of the Supreme Court no. 913/2021 of 23 December.

2. The Law

The lower court judgments concluded that the parties had reached a pre-contract agreement that gave rise to obligations for both parties, whereas FCC claims that these were merely preliminary or preparatory agreements that did not materialise into a binding agreement. The Supreme Court confirms that it is a “perfect” pre-contract agreement that generates an action to request its fulfilment, because all the elements of the relationship were determined.

> The fact that the Board of Directors of CPV is sovereign to adopt its decision on the appointment of its managing director does not affect the above, since, as stated above, FCC was obliged through the pre-contract agreement to actively collaborate so that this appointment would actually take place, which was within its sphere of decision-making power as it holds the position of majority and controlling shareholder.

Of course, if that is the case, what is the point of the pre-contract agreement? It would have been the same to say that XXX and FCC had concluded a definitive contract whose subject matter was the appointment of the former as managing director of the company's subsidiary.

XXX does not seek performance of the contract, but compensation. On what account? If the contract with FCC was "perfect", the compensation would have consisted of what XXX has ceased to earn as (failed) CEO of CPV. But this is not the case. Although all the lower courts engage in an unintelligible discourse on the grounds and limits of the compensation, which would merit a separate comment, the final result is that "the basis for the settlement of the compensation requested must consist of the amounts lost by the claimant as a result of the termination of his contractual relationship with the Holcim Group, from which must be deducted those that he may have received for any other professional activity that he could not have carried out if he had been hired by CPV and that have been proven". The latter refers to the amounts that XXX received in a new position as CEO in another company that he joined after the failure of the negotiation with FCC.

If XXX had been given the position promised by FCC, nothing would prevent him from being removed the next day. His financial claim for the "perfect contract" would then have been the compensation stipulated in the previous agreements in the event of termination, which, it seems, had also been agreed. And no account would have to be taken of the remuneration he no longer received at HOLCIN or the remuneration he actually received from a third company he joined as managing director. In other words, if there really is a "perfect" agreement, even if it is called a pre-contract agreement, then it will mean that CPV's final corporate refusal was not a "breach" of the pre-contract agreement, but a removal of director.

However, the reasoning of the judgement is flawed on a more important point. No company (and even less so a listed company) can bind itself (by means of a declaration by its directors) to a third party so that the latter is appointed managing director of that company. This is not only for obvious regulatory reasons, but also for the simple fact that appointment pre-agreements made in this way do not bind the company, the shareholders' meeting or the controlling shareholder. The "pre-contract agreement" has an impossible purpose, which is therefore void, without prejudice to any *culpa in contrahendo* (fault consistent in not acting in good faith during negotiations) that the offering directors may have incurred.

But what is way out of line is that the controlling shareholder (FCC) can oblige the subsidiary (CPV), by means of a non-commercial contract with a third party, to appoint such third party as a director of the said subsidiary. There cannot be an appointment contract (or pre-contract agreement), other than the CEO contract itself, as referred to in Art. 249.3 Companies Act. And if such a contract exists, it is void.

Does this mean that FCC (not CPV) "committed itself" in vain? I think so. It is something of a market-cleaning rule that no candidate is deemed entitled to a directorship until he is actually appointed. And in the meantime he acts at his own risk, barring some special malice on the part of the counterparty. But even if it were a perfect contract, FCC could only be forced to vote in favour of XXX, and always, as happened with the entry of a new shareholder, subject to *rebus sic stantibus* (unforeseeability).

However, I do not believe that it is a voting contract, but a *promise of performance by a third party,* which binds the promisor vicariously to the performance (where possible) or to compensatory redress for loss of the benefits of performance (again, the agreed compensation for termination).

And these are the options. Either XXX acted at his own risk, as FCC argued, or FCC breached a contract that contained a third-party performance promise. If in doubt, the first option is preferable.