JUDGMENT OF THE COURT (First Chamber)

18 December 2008 *

In Case C-338/06,

ACTION under Article 226 EC for failure to fulfil obligations, brought on 4 August 2006,

Commission of the European Communities, represented by G. Braun and R. Vidal Puig, acting as Agents, with an address for service in Luxembourg,

applicant,

v

Kingdom of Spain, represented by F. Díez Moreno, acting as Agent, with an address for service in Luxembourg,

defendant,

* Language of the case: Spanish.

supported by:

Republic of Poland, represented by E. Ośniecka-Tamecka, acting as Agent,

Republic of Finland, represented by J. Heliskoski, acting as Agent, with an address for service in Luxembourg,

United Kingdom of Great Britain and Northern Ireland, represented by V. Jackson, acting as Agent, assisted by J. Stratford, Barrister,

interveners,

THE COURT (First Chamber),

composed of P. Jann, President of the Chamber, A. Tizzano (Rapporteur), A. Borg Barthet, E. Levits and J.-J. Kasel, Judges,

Advocate General: V. Trstenjak,
Registrar: R. Grass,

after hearing the Opinion of the Advocate General at the sitting on 4 September 2008,

gives the following

Judgment

1 By its application, the Commission of the European Communities requests that the Court declare that:

— by allowing the general meeting of shareholders to approve the issue of new shares without pre-emptive subscription rights, at a price below their fair value;

— by granting the right to pre-emptive subscription of shares in the event of a capital increase by consideration in cash, not only to shareholders, but also to holders of bonds convertible into shares;

— by granting the right to pre-emptive subscription rights for bonds convertible into shares not only to shareholders, but also to holders of bonds convertible into shares pertaining to earlier issues, and

— by failing to provide that the shareholders' meeting may decide to withdraw pre-emptive subscription rights for bonds convertible into shares,

the Kingdom of Spain has failed to fulfil its obligations under Articles 29 and 42 of Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article [48] of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent (OJ 1977 L 26, p. 1; 'the Second Directive').

Legal context

Community law

2 The second and fifth recitals in the preamble to the Second Directive, which are legally based on Article 54(3)(g) of the EEC Treaty (subsequently Article 54(3)(g) of the EC Treaty, and now Article 44(2)(g) EC), are worded as follows:

'Whereas in order to ensure minimum equivalent protection for both shareholders and creditors of [public limited liability companies], the coordination of national provisions relating to their formation and to the maintenance, increase or reduction of their capital is particularly important;

…

Whereas it is necessary, having regard to the objectives of Article [44(2)(g) EC], that the Member States' laws relating to the increase or reduction of capital ensure that the principles of equal treatment of shareholders in the same position and of protection of creditors whose claims exist prior to the decision on reduction are observed and harmonised'.

3 Article 29 of the Second Directive provides:

'1. Whenever the capital is increased by consideration in cash, the shares must be offered on a pre-emptive basis to shareholders in proportion to the capital represented by their shares.

…

4. The right of pre-emption may not be restricted or withdrawn by the statutes or instrument of incorporation. This may, however, be done by decision of the general meeting. The administrative or management body shall be required to present to such a meeting a written report indicating the reasons for restriction or withdrawal of the right of pre-emption, and justifying the proposed issue price. The general meeting shall act in accordance with the rules for a quorum and a majority laid down in Article 40 …

…

6. Paragraphs 1 to 5 shall apply to the issue of all securities which are convertible into shares or which carry the right to subscribe for shares, but not to the conversion of such securities, nor to the exercise of the right to subscribe.

…'

4 Article 42 of the Second Directive provides:

'For the purposes of the implementation of this Directive, the laws of the Member States shall ensure equal treatment to all shareholders who are in the same position.'

National law

5 Under Article 158(1) of Royal Legislative Decree 1564/1989 of 22 December 1989, which amends the Law on public companies (Real decreto legislativo 1564/1989 por el que se aprueba el texto refundido de la Ley de Sociedades Anónimas) (BOE No 310, of 27 December 1989, p. 679), in the version applicable to the present dispute ('the LSA'):

'Where the capital is increased by means of the issue of new ordinary or preference shares, the shareholders and holders of convertible bonds may … exercise their right to subscribe for a number of shares proportionate to the nominal value of the shares which they already hold or, in the case of holders of convertible bonds, which they would hold if, at that time, they exercised their right to conversion.'

6 Article 159 of the LSA provides:

'1. If necessary in the company's interest, the general meeting may, when deciding to increase the capital, resolve to withdraw the right of pre-emptive subscription entirely or partly. For this resolution to be valid, it must conform with the provisions of Article 144 and ensure that:

…

(b) at the time of convening the meeting, the shareholders shall be provided, in accordance with Article 144(1)(c), with a report drawn up by the directors in which they justify in detail the proposal and the issue price of the shares, giving the names of the persons to whom they are to be allotted, together with a report, for which the directors are liable, prepared by an auditor who is not the company's auditor and is appointed for that purpose by the Commercial Registry, on the fair value of the company's shares, the theoretical value of the rights to pre-emption subscription which it is proposed to withdraw and the accuracy of the information in the directors' report;

(c) the nominal value of the shares to be issued, together with the issue premium, as the case may be, shall correspond to the fair value shown in the auditor's report referred to in (b) above. In the case of a listed company, the fair value shall mean the market value of the company's shares, which shall be presumed to be the stock exchange quotation, unless the contrary is proved.

Nevertheless, in the case of listed companies, the general meeting of shareholders may, as soon as the directors' report and the auditor's report required under (b) above, which must indicate the net asset value of the shares, are available, freely determine the issue price of the new shares, provided that the price is higher than the corresponding net asset value shown in the auditor's report. The general meeting may also confine itself to laying down the procedure for determining the price. …

…'

7 Article 293 of the LSA is worded as follows:

‘1. The shareholders of the company shall have a right of pre-emption for the convertible bonds.

2. The holders of convertible bonds issued earlier shall have the same right in the proportion laid down by the rules on the conversion.

3. The provisions of Article 158 of this law shall apply to the preferential right of subscription for convertible bonds.’

Pre-litigation procedure

8 Since it considered that the Spanish legislation was not consistent with Articles 29 and 42 of the Second Directive, the Commission sent a letter of formal notice on 15 January 2004 to the Kingdom of Spain. The latter replied, by letter of 10 March 2004, in which it rejected all the claims of breach of the Second Directive.

9 Since it took the view that the explanations provided by the Kingdom of Spain were not satisfactory, the Commission sent a reasoned opinion to that Member State on 5 January 2005, to which it replied, on 4 March 2005, by sending it a report drawn up by the Ministry for the Economy and Finance.

10 Since the explanations provided were not entirely satisfactory, the Commission decided, on 4 August 2006, to institute proceedings under Article 226 EC before the Court.

11 By order of the President of the Court of 18 January 2007, the Republic of Poland, the Republic of Finland and the United Kingdom of Great Britain and Northern Ireland were granted leave to intervene in this case in support of the form of order sought by the Kingdom of Spain.

The action

The first complaint

Arguments of the parties

12 By its first complaint, the Commission submits that the second subparagraph of Article 159(1)(c) of the LSA infringes Article 42 of the Second Directive, read in conjunction with Article 29(1) and (4) thereof, in that it does not ensure equal treatment of shareholders in a listed public company.

13 According to the Commission, where capital is increased by means of the issue of new shares, under Article 159(1)(c) of the LSA the general meeting of such a company may approve the withdrawal of the pre-emption right laid down in Article 158 of that law, and freely determine the issue price of the new shares, provided that, in particular, the issue price is higher than the 'net asset value' of those shares.

14 This effectively means allowing the price of the new shares, from which the pre-emption right is excluded, to be set at an 'unfairly' low level. According to the Commission, the 'net asset value' of a share may be significantly lower than its 'market value', calculated on the basis of its stock market price, whereas under the first subparagraph of Article 159(1)(c) of the LSA the 'market value' of a share is to be understood as meaning its 'fair value'.

15 The Commission infers from this that the second subparagraph of Article 159(1)(c) of the LSA introduces discrimination in respect of listed companies between, on the one hand, shareholders who held shares prior to the capital increase of the company concerned ('existing shareholders'), who purchased their shares at their 'market value', and, on the other, shareholders who acquired their shares after the capital increase of that company ('new shareholders'), who might have acquired their shares at a price far lower than their market value.

16 The Kingdom of Spain challenges these arguments, maintaining, first, that the LSA lays down conditions for withdrawing the right of pre-emption which are stricter than those provided for in the Second Directive.

17 As the Republic of Poland, the Republic of Finland and the United Kingdom also submit, the LSA, contrary to the Second Directive, provides for a minimum threshold for determining the issue price of the new shares which must be higher than their 'net asset value'. Furthermore, under that law there is a requirement not only for the report provided for in Article 29(4) of the directive, but also for a second report, drawn up by an independent 'auditor', justifying the issue price of the new shares.

18 In addition, the Kingdom of Spain contends that the LSA in no way allows a price to be set which is unfairly lower than the 'market value' of the new shares. The first subparagraph of Article 159(1)(c) merely introduces a rebuttable assumption that the 'fair value' of the shares of a listed company corresponds to their 'market value'. However, the general meeting is able to set an issue price of less than the 'market value', the fairness of which is justified in the light of the two reports referred to in the preceding paragraph of this judgment.

19 In this regard, the Republic of Poland goes on to say that, in any event, the setting of the price of the shares at below their 'market value' has to be assessed by reference not only to the principle of non-discrimination but also to the principle that company organs must act in the company's interest.

20 The Kingdom of Spain, the Republic of Poland and the United Kingdom claim that no discrimination between existing and new shareholders is possible because those two categories of shareholders are not in the 'same position' within the meaning of Article 42 of the Second Directive. Due to fluctuations in the stock market price, each shareholder would have acquired his shares at a different price, depending on the date on which the shares were purchased.

21 Furthermore, the Kingdom of Spain and the Republic of Poland point out that Article 159(1) of the LSA precludes any possibility of discrimination by providing that withdrawal of the pre-emption right can be approved by the general meeting only where the conditions on majority and quorum necessary for altering the company's articles of association are met, and that, in any event, the minority shareholders who voted against the decision approving that withdrawal are able to challenge that decision where they consider it to be contrary to the company interest.

22 In addition, according to the United Kingdom, there can be no question of different 'treatment' because the price of a share is a purely economic factor. In any event, even if unequal treatment can be established, it is justified on account of the measures of additional protection laid down by the LSA and, as the Kingdom of Spain also points out, in the light of the need to ensure that increases in capital serve the company's financial interest.

Findings of the Court

23 In order to rule on the substance of the first complaint raised by the Commission, it should be borne in mind that the Court of Justice has already had occasion to hold that the Second Directive seeks, pursuant to Article 44(2)(g) EC, to coordinate the safeguards which, for the protection of the interests of members and others, are required of companies within the meaning of the second paragraph of Article 48 EC with a view to making such safeguards equivalent. According to the second recital in the preamble thereto, the Second Directive is therefore intended to ensure minimum equivalent protection for both shareholders and creditors of public limited liability companies (Case C-42/95 *Siemens* [1996] ECR I-6017, paragraph 13).

24 As regards more particularly the protection of shareholders when capital is increased by consideration in cash, Article 29(1) of the Second Directive provides clearly, precisely and unconditionally that the shares must be offered on a pre-emptive basis to shareholders in proportion to the capital represented by their shares (see, to that effect, Case C-381/89 *Syndesmos Melon tis Eleftheras Evangelikis Ekklisias and Others* [1992] ECR I-2111, paragraph 39).

25 It is therefore only by way of exception that Article 29(4) of the Second Directive provides for the general meeting to be able to limit or withdraw the shareholders' rights of pre-emption, subject to certain conditions expressly laid down in that provision.

26 It must be pointed out, however, that although the right of pre-emption granted to shareholders does not admit of any exception other than that expressly laid down in Article 29(4) of the directive (*Syndesmos Melon tis Eleftheras Evangelikis Ekklisias and Others*, paragraph 40), the fact remains that, as is apparent from the second recital and the judgment in *Siemens*, the Second Directive lays down minimum requirements for the protection of shareholders and creditors of public limited liability companies, by leaving the Member States free to adopt provisions that are more favourable to them, which provide, inter alia, for more restrictive conditions on withdrawing the right of pre-emption.

27 Clearly, in the present case, the effect of the national legislation is precisely to strengthen the protection afforded to shareholders of public limited companies under Article 29(4) of the Second Directive.

28 Under the first subparagraph of Article 159(1)(b) of the LSA, when the pre-emption right is to be wholly or partially withdrawn, there is a requirement not only for the report referred to in Article 29(4) of the Second Directive, but also for a second report on the fair value of the company's shares, the theoretical value of the pre-emption rights which it is proposed to withdraw and the accuracy of the information in the directors' report. According to that provision of national law, the second report, for which the directors are liable, must be prepared by an auditor who is not the company's auditor and is appointed for that purpose by the Commercial Registry.

29 Whereas Article 29(4) of the Second Directive is limited to requiring that the issue price of the new shares be justified in the report of the company's administrative or management body, and does not set any minimum threshold for this, the second subparagraph of Article 159(1)(c) of the LSA lays down, as regards quoted companies, a minimum issue price for the new shares, by requiring that that price be above the net asset value of the shares in question irrespective of the conclusions of the report.

30 This assessment of the national rules cannot, moreover, be undermined by the Commission's arguments to the effect that setting the issue price of the new shares at below their market value, as permitted by Article 159 of the LSA, is liable to lead to unequal treatment, for the purposes of Article 42 of the Second Directive, between existing and new shareholders.

31 First, it must be pointed out that the Commission has not provided any evidence to show, as is required under Article 42 of the directive, that those two categories of shareholders are in the same position, thus requiring the LSA to ensure them equal treatment.

32 Secondly, the effect of the Commission's interpretation would be to render Article 29(4) of the Second Directive redundant, since under that provision the issue price has to be justified by the directors' report, although it does not have to be set in accordance with the market value of the shares in question.

33 To require that the issue price of new shares must not be below their market value would have the effect that, even if that price were justified by the directors' report, the general meeting could not apply it without infringing the principle of equal treatment referred to in Article 42 of the Second Directive.

34 In the light of all the foregoing, the first complaint relied on by the Commission in support of its action must be rejected as unfounded.

The second and third complaints

Arguments of the parties

35 By its second and third complaints, which must be examined together, the Commission submits first that Article 158(1) of the LSA gives not only shareholders but also holders of bonds convertible into shares a right of pre-emption for new shares. Secondly, Article 293(2) of that law provides that when there is an issue of bonds convertible into

shares, a right of pre-emption for those shares is granted both to shareholders and to holders of earlier issues of convertible bonds.

36 These provisions of the LSA, it argues, infringe Article 29(1) and (6) of the Second Directive, since the directive requires new shares and convertible bonds to be offered on a pre-emptive basis to shareholders alone.

37 The Kingdom of Spain and the Republic of Poland dispute the Commission's claim, relying, in particular, on an interpretation of Article 29(1) and (6) on the basis of the directive's purpose and function, which is to protect the holders of convertible bonds as potential shareholders and thus to maintain the value of the shares reserved for them.

Findings of the Court

38 It is indeed the case, as the Kingdom of Spain submits, that Article 29(1) and (6) of the Second Directive does not provide that both the new shares and the bonds convertible into shares are to be offered exclusively to the shareholders and that they can thus also be offered to holders of earlier issues of convertible bonds.

39 It must be held, however, that it is apparent from the very wording of that article that the offer must not be made to both of them simultaneously, but 'on a pre-emptive basis' to the shareholders.

40 Thus, only in so far as the shareholders have not exercised their right of pre-emption can those shares and bonds be offered to other purchasers, including, in particular, the holders of convertible bonds.

41 Furthermore, if the legislature had wished to extend the right of pre-emption at issue to the latter, it would have done so expressly, in the same way as, in Article 29(6) of the Second Directive, it extended the right of pre-emption to other securities which are convertible into shares or which carry the right to subscribe for shares.

42 Such an interpretation also accords with the aims of the directive.

43 As the Advocate General pointed out in point 76 of her Opinion, and as is apparent from point 19 of the judgment in *Siemens*, one of the aims of the Second Directive is to afford shareholders more effective protection, by enabling them — in the event of an increase in capital — to avoid dilution of their stake in the capital represented by their shareholding.

44 Thus, in order to avoid such a risk, Article 29(1) and (6) of the Second Directive gives precisely to shareholders priority over all other potential purchasers of new shares or of bonds convertible into shares.

45 It is clear that the achievement of such an objective would be jeopardised if those new securities could also be offered on a pre-emptive basis to a category of purchasers other than that of shareholders, namely the holders of bonds convertible into shares.

46 It follows that, by granting a pre-emption right in respect of shares in the event of a capital increase by consideration in cash, not only to shareholders, but also to holders of bonds convertible into shares, and a pre-emption right in respect of bonds convertible into shares not only to shareholders, but also to the holders of bonds convertible into shares pertaining to earlier issues, the Kingdom of Spain has failed to fulfil its obligations under Article 29(1) and (6) of the Second Directive.

The fourth complaint

Arguments of the parties

47 By its fourth plea, the Commission contends that Article 293(3) of the LSA infringes Article 29(6) in conjunction with Article 29(4) of the Second Directive, as that article

does not provide for the general meeting to be able to withdraw the pre-emption right for bonds convertible into shares.

48 According to the Kingdom of Spain, a systematic interpretation of Article 293 of the LSA can lead to no conclusion other than that the general meeting can withdraw this right of pre-emption.

49 In this connection, the Republic of Finland observes that, in any event, even if Article 293 of the LSA precluded the possibility of withdrawing that pre-emption right, this would not be sufficient to establish failure on the part of the Kingdom of Spain to fulfil its obligations given that the purpose of the Second Directive is minimum harmonisation.

Findings of the Court

50 It must be pointed out that even though, as has been stated in paragraph 26 of this judgment, the Member States are free to adopt more restrictive conditions on withdrawal of the right of pre-emption at issue, the fact remains that Article 29(6) of the Second Directive, read in conjunction with Article 29(4), requires that, in certain circumstances, the general meeting of shareholders be able to decide to withdraw the right of pre-emption for all securities which are convertible into shares.

51 Clearly, as the Commission submits, the wording of Article 293 of the LSA makes no express provision for the possibility of such withdrawal.

52 Furthermore, whereas Article 293(3) provides that Article 158 of the LSA is applicable to the right of pre-emptive subscription, nowhere does it provide that Article 159 thereof, governing the right of pre-emption for new shares, is also applicable to the right of pre-emption for bonds convertible into shares.

53 Moreover, the systematic interpretation advocated by the Kingdom of Spain — to the effect that Article 293 of the LSA can only be interpreted as providing for the possibility to withdraw the right of pre-emption in question, since otherwise that article would be completely illogical — cannot be upheld.

54 In that regard, it must be borne in mind that, according to settled case-law, the need to ensure that Community law is fully applied requires Member States not only to bring their legislation into conformity with Community law but also to do so by adopting rules of law capable of creating a situation which is sufficiently precise, clear and transparent to allow individuals to know the full extent of their rights and rely on them before the national courts (Case 162/99 *Commission* v *Italy* [2001] ECR I-541, paragraph 22 and the case-law cited).

55 In the present case, even if Article 293 of the LSA could be interpreted contrary to its wording, as the Kingdom of Spain suggests, such an interpretation would be very unlikely to create a situation which is sufficiently precise, clear and transparent to allow individuals to know the full extent of their rights and rely on them before the national courts.

56 This is particularly the case since, as the Advocate General observes in point 89 of her Opinion, the Kingdom of Spain did not produce any specific evidence to show that Spanish courts interpret Article 293 of the LSA as providing for the possibility to withdraw the right of pre-emption for bonds convertible into shares.

57 It must therefore be held that, by failing to provide that the shareholders' meeting may decide to withdraw pre-emption rights in respect of bonds convertible into shares, the Kingdom of Spain has failed to fulfil its obligations under Article 29(6) of the Second Directive, read in conjunction with Article 29(4) thereof.

Costs

58 Under Article 69(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs, if they have been applied for in the successful party's pleadings. Under Article 69(3) of those rules, where each of the parties succeeds on some and fails on other heads, the Court may order that the costs be shared or that the parties bear their own costs. Finally, under the first subparagraph of Article 69(4) the Member States and the institutions which intervene in the proceedings are to bear their own costs.

59 In this case, the Kingdom of Spain, which has been unsuccessful in respect of three of the four grounds of complaint raised by the Commission in support of its application, must be ordered to pay three quarters of the costs, and the Commission, which has been unsuccessful in respect of its first ground of complaint, must be ordered to pay one quarter of the costs.

60 In accordance with Article 69(4) of the Rules of Procedure, the Republic of Poland, the Republic of Finland and the United Kingdom of Great Britain and Northern Ireland are to bear their own costs.

On those grounds, the Court (First Chamber) hereby:

1. Declares that the Kingdom of Spain:

— **by granting a pre-emption right in respect of shares in the event of a capital increase by consideration in cash, not only to shareholders, but also to holders of bonds convertible into shares;**

— **by granting a pre-emption right in respect of bonds convertible into shares not only to shareholders, but also to holders of bonds convertible into shares pertaining to earlier issues; and**

— **by failing to provide that the shareholders' meeting may decide to withdraw pre-emption rights in respect of bonds convertible into shares;**

has failed to fulfil its obligations under Article 29 of Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article [48] of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent;

2. **Dismisses the action as to the remainder;**

3. **Orders the Kingdom of Spain to pay three quarters of all the costs. The Commission of the European Communities is ordered to pay a quarter of the costs;**

4. **Orders the Republic of Poland, the Republic of Finland and the United Kingdom of Great Britain and Northern Ireland to bear their own costs.**

[Signatures]