The Corporate Governance Review

Seventh Edition

Editor
Willem J L Calkoen

The Law Reviews

THE CORPORATE GOVERNANCE REVIEW

The Corporate Governance Review
Reproduced with permission from Law Business Research Ltd.

This article was first published in The Corporate Governance Review - Edition 7
(published in March 2017 – editor Willem J L Calkoen)

For further information please email
Nick.Barette@thelawreviews.com

Chapter 19

LUXEMBOURG

Margaretha Wilkenhuysen and Steven van Waas[1]

I OVERVIEW OF GOVERNANCE REGIME

Luxembourg's main statutes on corporate governance include the 10 August 1915 Act on Commercial Companies (the Act), which was revamped in 2016 to modernise Luxembourg corporate law, the Market Abuse Regulation[2] and the Securitisation Act.[3] On 1 November 2007, Directive 2004/39/EC on Markets in Financial Instruments was implemented to introduce new provisions on transparency for shares and transaction reporting. Companies whose shares are admitted to trading on a regulated market in a Member State of the EU, including Luxembourg, may also be subject to the Act dated 19 May 2006 on Takeover Bids, as amended (the Takeover Bid Act). The Takeover Bid Act notably provides for minority shareholder protection, the rules of mandatory offers and disclosure requirements. Companies intending to admit their shares to trading on a regulated market or to make a public offer may also be subject to the Act dated 10 July 2005 on Prospectuses for Securities (the Prospectus Act), which in particular imposes the requirement for the publication of prospectuses. Transparency Directive 2004/109/EC was also transposed into Luxembourg legislation on 11 January 2008 through the Act on Transparency Requirements (the Transparency Act) in relation to information about issuers whose securities are admitted to trading on a regulated market, as amended. In addition, on 1 July 2011, the Act of 24 May 2011 came into force (the Shareholder Act). It implemented Directive 2007/36/EC on the Exercise of Certain Rights of Shareholders in Listed Companies, aiming to increase shareholder activism and setting out a number of shareholders' rights. Furthermore, the Act dated 21 July 2012 on Mandatory Squeeze-Out and Sell-Out of Securities of companies currently admitted or previously admitted to trading on a regulated market or having been offered to the public (the Squeeze-out Act)[4] came into force on 1 October 2012, introducing a squeeze-out right in favour of dominant shareholders and a sell-out right in favour of minority shareholders in companies whose shares are admitted to trading on a regulated market.[5]

1 Margaretha Wilkenhuysen is a partner and Steven van Waas is an associate at NautaDutilh Avocats Luxembourg S.à r.l.

2 Regulation (EU) No. 596/2014 as complemented by the Act of 23 December 2016 on Market Abuse implementing Regulation (EU) No. 596/2014, Directive 2014/57/EU and Directive 2015/2392/EU.

3 Act of 22 March 2004 on Securitisation, as amended.

4 See Elisa Faraldo Talmon, Ariane Mehrshahi and Jean-Michel Schmit, 'Présentation générale et réflexions sur la nouvelle loi du 21 juillet 2012 relative aux retrait et rachat obligatoires en dehors d'une offre publique d'acquisition', in *Ace: Comptabilité, Fiscalité, Audit, Droit des Affaires au Luxembourg*, No. 10 (Wolters Kluwer, 2012), pp. 3–12.

5 Until the Squeeze-out Act came into force, a squeeze-out and a sell-out right existed only in the context of a public takeover under the Act dated 19 May 2006 implementing Directive 2004/25/EC on takeover bids.

The Act of 6 April 2013 on Dematerialised Securities entered into force on 18 April 2013. It introduced a legal regime for dematerialised securities, inspired by existing regimes in Belgium, Switzerland and France. The Act of 12 July 2013 implemented into Luxembourg law Directive 2011/61/EU on Alternative Investment Fund Managers. This Act introduced a new partnership structure – the special limited partnership – into Luxembourg law and some technical amendments concerning limited partnerships by shares. It also modernised common limited partnerships. The Act of 30 July 2013 reformed the commission of accounting principles and modified certain rules regarding the annual accounts and consolidated accounts of companies. These rules were further modified by the Act of 18 December 2015, which will be discussed in Section III.

Furthermore, the Act of 28 July 2014 on the Immobilisation of Bearer Shares came into force on 18 August 2014, creating a new practical modality related to the bearer shares without renovating the legal status thereof. In short, this Act has instituted in Luxembourg the requirement to deposit bearer shares with a recognised depositary, which will be appointed by the board of directors or management board of the relevant public limited liability company or partnership limited by shares. The Act allows access to information about the identity of the shareholders holding bearer shares to public authorities while preserving the confidentiality of the information about third parties; indeed, the bearer shares register is not meant to be accessible to the public, but only to the judicial and fiscal authorities.

On 26 June 2015, the Fourth EU Anti-Money Laundering Directive[6] came into force. One of the most profound changes that will be brought by this directive is the obligation for Luxembourg to ensure that information on the beneficial ownership of Luxembourg companies will be held in a central register. Any person or organisation that can demonstrate a legitimate interest will then be able to consult the information on beneficial ownership. While Luxembourg is not yet obliged to have a central register in place, it is under the obligation to adopt the necessary legislation to comply with the directive by 26 June 2017.

Also worth mentioning is the Act of 10 March 2014, which implements Council Regulation (EC) No. 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society. This Act provides the possibility for a European Cooperative Society (SCE) to be formed *ex novo* by: five or more natural persons resident in at least two EU Member States; five or more natural persons and companies or other legal bodies formed under the law of an EU Member State and resident in (or governed by the law of) at least two different EU Member States; or by companies and firms or other legal bodies formed under the law of an EU Member State and governed by the law of at least two different EU Member States. SCEs can also be formed by more traditional methods, like a merger between cooperatives formed under the law of an EU Member State with registered and head office in the European Union, provided that at least two of the cooperatives are governed by the laws of different EU Member States or by conversion of a cooperative that was formed under the law of an EU Member State and has a registered and head office in the European Union, provided that it has had an establishment or subsidiary governed by the law of another EU Member State for at least two years.

Corporate governance in Luxembourg is statute-based, consisting primarily of the Civil Code, the Act and, for listed companies, the rules and regulations of the Luxembourg Stock Exchange (LuxSE) and the above-mentioned acts. However, the statutory law provisions

6 Directive (EU) 2015/849 of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing.

only give very general governance rules or principles. More specific corporate governance is generally based on a flexible 'comply or explain' system, enabling the specific circumstances of companies, such as their size, shareholding structure, activities, exposure to risks and management structure, to be accounted for.

As a supplement to the general statutory law, the LuxSE's 10 Principles of Corporate Governance (the LuxSE Principles), as modified in October 2009 and revised in March 2013 (3rd edition),[7] provide guidelines on best practice in corporate governance for all companies listed on the LuxSE and all Luxembourg companies whose shares are traded on a regulated market. The LuxSE Principles consist of general principles that must be complied with and recommendations that, although obligatory in principle, may be deviated from when justified in specific circumstances, provided that adequate explanation is provided. The recommendations are supplemented by guidelines on how a company should implement or interpret them. The obligation to comply or explain does not apply to the guidelines, which are indicative but not binding. All Luxembourg companies whose shares are admitted for trading on a regulated market operated by the LuxSE must follow the LuxSE Principles.

The LuxSE Principles refer to general corporate governance issues, such as duties of the managing board, the management structure, conflicts of interest provisions, remuneration and reporting issues. The LuxSE Principles are highly flexible and adaptable to the activity, size and culture of individual companies. Their stated objective is to provide guidance without being overly restrictive, aiming to encourage transparency and dialogue and to facilitate the exercise of power within companies without restricting freedom of enterprise. They also aim to enable the shareholders of listed companies to be actively involved in the company's activities.

Unlike certain neighbouring countries, in Luxembourg listed companies are often controlled by one or more major shareholders, rendering it impossible to rely solely on market monitoring to ensure that listed companies comply with the LuxSE Principles. Therefore, a system of monitoring involving the shareholders, the board and the LuxSE, at a minimum, is required to ensure proper observance of the principles of corporate governance.

The other main regulatory authority is the Luxembourg Supervisory Commission of the Financial Sector (CSSF). The CSSF has jurisdiction regarding matters for which the laws or regulations in force require disclosure, whether or not the information is dealt with in the LuxSE Principles, including the authority to impose sanctions. The LuxSE's role in the external monitoring of compliance with the principles of corporate governance does not affect the CSSF's legal responsibility as a regulator.

The CSSF is responsible for supervising credit institutions, financial sector professionals, collective investment undertakings, pension funds, stock exchanges, securities markets and so forth. The CSSF's internal committees are responsible for regulatory work, and it has nine departments charged with the supervision of the financial sector, one department dedicated to the participation of the CSSF in the Single Supervisory Mechanism and one department responsible for the public oversight of the audit profession. The supervision of securities markets department supervises the financial instrument markets and market operators, international and national investigations regarding stock market offences in cooperation with the foreign competent authorities and the Luxembourg Stock Exchange. The department also deals with issues concerning the authorisation of new markets, and is in charge of approving

7 www.bourse.lu/corporate-governance.

prospectuses drawn up for offers of securities to the public and admission of securities to trading on a regulated market, following up on the transparency requirements in relation to issuers of listed securities and handling files relating to takeover bids.

The CSSF's regulatory framework is in line with the relevant European Union directives and aims to promote prudent business policy complying with regulatory requirements, to protect the financial stability of the supervised companies and of the financial sector as a whole, to supervise the quality of the organisation and internal control systems and to strengthen the quality of risk management. The CSSF acts solely in the public interest, and ensures that all financial sector laws and regulations are observed and that international agreements and European directives in the fields of its responsibility are implemented and respected, notably through CSSF circulars concerning the application of legislation. The regulatory framework is continually updated through regular consultation between the government, the legislator and the private sector. EU Commission Recommendation 77/534/EEC of 25 July 1977 concerning a European code of conduct relating to transactions in transferable securities was published in the Luxembourg Official Administrative Gazette on 25 June 1997 and is applicable to companies listed on the LuxSE. However, on 23 September 2010, the Luxembourg Court of Cassation ruled that the recommendation has not been transposed into Luxembourg national law as a binding rule.[8]

As an operationally independent body, the CSSF has sufficient powers to conduct effective supervision and regulation of the Luxembourg securities market. It is funded by taxes levied from companies under its supervision. To conduct its tasks effectively, the CSSF has broad powers including the authority to attend meetings of LuxSE entities, to suspend rulings or to suspend market intermediaries' decision-makers if they fail to observe legal, regulatory or statutory provisions.

Other professionals in the financial sector and private-sector companies also have an indirect regulatory role through their consultative participation with the government and the legislator in the field of regulation.

Apart from listed companies, specific obligations tend to be market-driven commitments rather than legally binding duties as there are currently no codified mandatory rules inducing companies to take corporate governance principles or corporate social responsibility (CSR) issues into account in their internal decision-making procedures. The engagements undertaken so far, with the exception of the LuxSE Principles, are non-compulsory soft law with reputational rather than legal force, and are minor in comparison to other marketplaces.

Corporate governance is, however, gaining momentum. In September 2009, the Association of the Luxembourg Fund Industry (ALFI)[9] published a Code of Conduct for Luxembourg funds to provide their boards with high-level principles and best practice recommendations. The principle-based Code of Conduct was introduced to formalise and specify best practice in light of the implementation of Directive 2006/46/EC, aiming to facilitate cross-border investments and improve public confidence in financial statements and reports, notably through greater transparency and EU-wide comparability mechanisms. In June 2013, the ALFI published a revised version of the Code of Conduct, which addressed in particular the increased focus on the management of conflicts of interest, risk management and internal controls that have been major features of new regulations and developments in practice since the first version of the Code of Conduct was published in 2009.

8 Luxembourg Court of Cassation, 23 September 2010, No. 54/10.

9 www.alfi.lu.

Since 2003, the Labour and Employment Minister has aimed to bring government, labour and corporate sectors together to educate, inform and drive support for the development of CSR in Luxembourg. Although no CSR legal requirements are in place, a growing number of companies have undertaken commitments. In 2005 the Ministry of Labour and Employment and the ADT-Center,[10] an advisory body specialising in gender, diversity management and CSR issues, began working together under an agreement to promote CSR and to build partnerships between local stakeholders (including small and medium-sized enterprises, multinationals and non-governmental organisations) with the notable aims of promoting and developing CSR within corporations; informing about existing and future best practice; stimulating the debate on CSR in corporations; and raising awareness of CSR principles with the public and corporations. Under the agreement, the Ministry of Labour and Employment is charged with promoting employment for mature, disabled and gifted people, health and safety in the workplace and generating employment.

Additionally, Inspiring More Sustainability Luxembourg (IMS)[11] is a non-profit organisation created by six major Luxembourg firms to exchange, discuss and promote CSR policies; it now has over 100 member companies and associations based or operating in Luxembourg. IMS' aims include facilitating the relationship between businesses and the territories within which they operate (including sustainable development, dialogue with local communities and workplace welfare) and general diversity management aimed at preventing workplace discrimination. Since its formation in 2007, IMS has organised numerous conferences and workshops, attracting several thousands of participants.

In line with the above, the Luxembourg Bankers' Association (ABBL),[12] representing the major Luxembourg industry, highlights in its code of conduct[13] the criterion of diversity in relations between financial sector professionals and their customers.[14] In addition, 2012 saw the release of CSSF Circular 12/552 on central administration, internal governance and risk management, which has been applicable to banks and investment firms since 1 July 2013 and is aimed at ensuring that these entities have a formalised and robust internal governance framework; it also centralises in one single document all the main requirements referring to governance matters and implementing EU rules, including those of the Internal Governance Guidelines of the European Banking Authority.[15] The changes wrought by the circular are significant and of great importance to the internal organisation of banks and investment firms. The circular applies on both a stand-alone and a consolidated basis. CSSF Circular 12/552 has been amended on several occasions. Most recently it was updated further

10 www.adt-center.lu.

11 www.imslux.lu.

12 www.abbl.lu.

13 www.abbl.lu/download/19193/code-of-conduct-2016.pdf.

14 The first principle of the Code is loyalty, fairness and integrity: 'Professionals form an opinion on, and deal with, [. . .] without discrimination on grounds of origin, skin colour, gender, sexual orientation, family situation, age, state of health, handicaps, adherence to accepted principles of morality, political or philosophical opinions, trade union activities, ethnicity, nationality or religious creed.'

15 CSSF Circular 12/552 on central administration, internal governance and risk management, released on 11 December 2012.

to the adoption of the guidelines of the European Banking Authority on the management of interest rate risk arising from non-trading activities,[16] as well as on the limits on exposure to shadow banking entities that carry out banking activities outside a regulated framework.[17]

While CSR commitments displayed on the participating companies' websites have no legal basis, and therefore are not subject to legal enforcement, the unique nature and size of the Luxembourg marketplace has increased the effect of 'peer pressure' on companies.

More specifically, Directive 2006/46/EC of 14 June 2006, implemented by the Act of 5 December 2007, includes a provision on corporate governance practices that listed insurance companies should apply.[18] The Act requires listed companies in the insurance field to dedicate a specific section in their management report to their obligatory and voluntary adhesion to corporate governance codes, and all other information purporting to their corporate governance practice. Gradual legislative recognition of corporate governance practice may also follow in other areas in the future, especially as the European Commission adopted an action plan[19] in 2012, outlining initiatives to be implemented in the areas of company law and corporate governance. The key elements of the action plan include (1) increasing transparency between companies and their shareholders, (2) encouraging and facilitating long-term shareholder engagement and (3) improving cross-border initiatives and transactions. These elements may only be achieved through national legislation, therefore bringing corporate governance obligations to the fore (as these corporate governance rules are only applicable to companies listed on a stock exchange).[20]

Regarding listed companies, the Transparency Act, for example, requires LuxSE-listed companies to publish information regarding their share capital and all regulated information (including financial reporting and shareholding) on their websites, and the Market Abuse Regulation stipulates that complete and effective public disclosure of any inside information must be published on both the company's and the LuxSE's websites (i.e., whenever an issuer, or person acting on its behalf, discloses any inside information to a third party in the normal exercise of business (simultaneously in the event of intentional disclosure, promptly in the event of unintentional disclosure)). Listed companies must also publish their corporate governance charters on their websites. In practice, listed companies tend to publish not only regulated information, but also all past and present press releases and corporate information.

While corporate governance in Luxembourg is currently generally based on voluntary adherence, a growing number of institutional guidelines and codes are being developed. At the same time, the Luxembourg government is working towards promoting corporate governance responsibility on a national level. Of particular note are the dispositions relating to employee representation (see Section IV, *infra*).

The importance of CSR is gathering momentum, as demonstrated by the increasing number of companies opting to follow institutional CSR recommendations or drawing up and publishing their own guidelines. While the majority of CSR is still soft-law based, reputational risk is of increasing importance in the various markets. In addition, the

16 CSSF Circular 16/642.

17 CSSF Circular 16/647.

18 Article 85-1 et seq.: www.legilux.public.lu/leg/a/archives/2007/0211/a211.pdf#page=2.

19 Action plan adopted by the European Commission on 12 December 2012 in the context of its 'Europe 2020' strategy, which generally aims to improve the business environment in Europe by adapting EU company law and governance rules to the modern needs of society and the changing economic environment.

20 See for details: http://europa.eu/rapid/press-release_IP-12-1340_en.htm.

implementation of Directive 2007/36/EC into Luxembourg law by the Shareholder Act marked an important step in Luxembourg CSR legislation. The Shareholder Act applies to companies that have their registered office in Luxembourg and whose shares are admitted to trading on a regulated market in a Member State of the European Union, as well as to Luxembourg companies whose shares are traded on a regulated market outside the European Union if those companies have elected to opt into the rules of the Shareholder Act (see Section V, *infra*). The Shareholder Act goes beyond Directive 2007/36/EC's requirements, and aims to increase shareholders' active participation in their companies by enabling them to exercise their voting rights, ensuring their right to place items on shareholders' meetings' agendas and to ask questions.

II CORPORATE LEADERSHIP

i Board structure and practices

Structure

Although the Act of 25 August 2006, which introduced Article 60 *bis*-1 into the Act, provides the possibility for public limited liability companies to choose a two-tier board structure, the one-tier board structure remains by far the preferred option in Luxembourg, with the company being managed exclusively by a board invested with the broadest powers to act in the name and on behalf of the company.

In a two-tier system, the company is managed by two bodies: the management board, charged with the day-to-day management of the company, and a supervisory board. Article 60 *bis*-1 et seq. of the Act details the supervisory board's responsibilities, which include permanent supervision and appointment of the management board members, the right to inspect all company transactions. No person may at the same time be a member of both the management board and the supervisory board. Members of the supervisory board are liable towards the company and any third party in accordance with general law. However, there is no specific guidance relating to the exercise by members of the supervisory board of their duties.

Composition of the board

The board is composed of appointed members (the company's directors). The Act requires a minimum of three directors; the maximum number of directors is undefined (the LuxSE Principles advise 16 directors as a reasonable limit). While the directors are appointed by the shareholders of the company, the directors choose a chair from among their members. The Act does not provide any specific powers to the chair of the board, although companies may choose, for example, to grant a power of representation to the chair in the articles of association (AoA). However, unlike in other civil law jurisdictions, the chair of the board does not act on behalf of the company in his or her position as chair, but rather on the basis of his or her position as director of the company.

Article 51 *bis* of the Act provides that where a legal entity is appointed as director of a public limited liability company, it shall designate a permanent representative to exercise that duty in the name and for the account of the legal entity. Article 51 *bis* applies only to the public limited liability company. However, an interesting issue in respect of the applicability of Article 51 *bis* to a partnership limited by shares was indirectly raised by the District Court of Luxembourg on 11 December 2013. The question was to establish whether the obligation to appoint a permanent representative of a legal person to a board of a public

limited liability company also applies to the legal person of a general partner of a partnership limited by shares. In its interlocutory decision, the District Court recognised the applicability of Article 51 *bis* to a partnership limited by shares. This decision was implicitly upheld in the Court's judgment of 23 December 2015.[21]

Most AoA provide that any two directors can represent the company without evidence of a board resolution (although in practice the board may ratify actions taken previously by directors acting individually).

The Act provides for three mechanisms: the board can adopt a decision and give specific mandates (limited in time and scope) to one or more of its members, or other individuals, to act on its behalf;[22] the AoA may entitle one or more directors to represent the company in any legal proceedings, either individually or jointly;[23] and the appointment of a 'day-to-day' manager. The board may designate a director as a general representative of the company charged with its day-to-day business and individually or jointly representing the company towards third parties for that business (Article 60 of the Act). Power may be delegated to one or more directors, managers or other agents, who may but are not required to be shareholders, acting either individually or jointly. While their appointment, removal from office and powers may be specified, limited or extended by the AoA or the competent corporate body, the Act states that no restrictions to their representative powers may be validly opposed in relation to third parties, even if their appointment is published. The liability of the day-to-day management is based on the general rules relating to mandates. When a member of the board is appointed as day-to-day manager, the Act requires the board to report annually to the shareholders on the salary, fees and any benefits granted to that director.[24]

A company will generally be bound by acts of its directors or by the person entrusted with its day-to-day management, even if those acts exceed the company's corporate object, unless the company proves that the third party knew that the relevant acts exceeded the company's corporate object or could not, in view of the circumstances, have been unaware of it. The publication of a restriction to a director's powers in the company's AoA is deemed insufficient to constitute such proof.[25]

Regarding listed companies, LuxSE Principle 4 distinguishes between executive and non-executive managers: executive managers are defined as senior managers who are not board directors but who are members of a body of executives charged with the day-to-day management of the company. There is no other distinction under Luxembourg law, with all board members having the same rights and obligations. A more permanent division of tasks and responsibilities between board members is possible (e.g., by providing for different classes of directors), but any such division is purely internal and is unenforceable towards third parties. It is, however, possible for the board to delegate certain specific powers to individual board members or non-board members in the framework of a specific delegation of power.

Finally, the European Commission has proposed legislation with the objective of attaining a 40 per cent presence of women among non-executive board-member positions

21 Luxembourg District Court, 23 December 2015, Nos. 145 724 and 145 725.

22 Article 1984 et seq. of the Luxembourg Civil Code.

23 Article 53, fourth paragraph of the Act.

24 Article 60 of the Act.

25 Article 60 *bis* of the Act.

in publicly listed companies.[26] Luxembourg is currently reported as having an average of less than one in 10 female board members, with over half of the largest companies having no women on their boards at all.[27] In 2013, the European Parliament adopted a legislative resolution on this proposal, but the Council of the European Union was not able to reach a general approach on a directive improving the gender balance on company boards.

Separation of CEO and chair roles: chair's role and responsibilities

While the roles of CEO and chair tend to be separated in practice, there are no legal provisions or guidelines pertaining to a separation of roles or responsibilities.

For listed companies, LuxSE Principle Recommendation 2.4 requires that the chair prepares the board meeting agendas after consulting the CEO and ensures that the procedures for preparing meetings, deliberations, decision-making and the implementation of decisions are correctly applied. Under this non-compulsory guideline, the chair should ensure the proper application of the rules of governance and provide advice to the board.

Luxembourg law does currently not provide for a specific procedure for direct communication between the CEO or the chair and the shareholders.

For listed companies, under LuxSE Principle 10 companies should 'establish a policy of active communication with the shareholders' and allow shareholder dialogue with the board and the executive management.

Remuneration of directors and senior management

Directors, as such, are not employees of the company, and their remuneration falls under the general rules on mandates and corporate law. Generally, and unless otherwise provided by the AoA, services rendered by the company directors are considered to be provided remuneration-free. If the AoA authorise remuneration, the global amount to be paid to the directors will be fixed by the general meeting of shareholders, and the board will allocate that amount between board members as it deems fit. The rules on conflicts of interest forbid directors from taking part in or voting on resolutions relating to their own remuneration.

Senior managers are generally employees of the company, and the Luxembourg Labour Code will be applicable as regards their relationship with the company. Concerning listed companies, the LuxSE Principles recommend establishing a remuneration committee to deal with these issues; under LuxSE Principle 8, the company must 'secure the services of qualified directors and executive managers by means of a fair remuneration policy that is compatible with the long-term interests of the company', thereby introducing a sustainable aspect rather than concentrating on short-term gains.

26 Proposal for a Directive on improving the gender balance among non-executive directors of companies listed on stock exchanges and related measures of 14 November 2012, 2012/0299 (COD) (http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2012:0614:FIN:en:PDF). At the same time the European Business School's 'Women on Boards' Initiative published its 'Global Board Ready Women' list online, which contains 8,000 board-ready young graduate women, at http://europa.eu/rapid/press-release_IP-12-1358_en.htm.

27 http://ec.europa.eu/justice/gender-equality/files/womenonboards/impact_assesment_quotas_en.pdf.

Committees

The company's AoA may allow for the creation of committees appointed by the board to ensure that the directors' obligations are fulfilled. The LuxSE Principles advise listed companies to establish, from among the board's members, *inter alia*:

a a committee to assist the board in relation to corporate policies, internal control, financial and regulatory reporting, and risk management;[28]

b an audit committee;

c a nomination committee to nominate suitable candidates as directors; and

d a corporate governance committee to ensure compliance with corporate governance practice.

The AoA will outline the number of members of each committee, their function and scope of powers, and the committees themselves will be appointed by and under the supervision of the board.

LuxSE Principle 3 requires listed companies and their boards to establish such committees as are necessary for the proper performance of the company's tasks. The LuxSE Principles also recommend that the board appoint as many special committees as are needed to examine specific topics and to advise the board. The board itself shall remain responsible for decision-taking.

ii Directors

Although no general legal obligations are in place, the LuxSE Principles require that listed companies' boards have a sufficient number of independent directors (the number depends on the nature of the company's activities and share ownership structure), defining independent directors as not having 'any significant business relationship with the company, close family relationship with any executive, or any other relationship with the company, its controlling shareholders or executive managers which is liable to impair the independence of the director's judgement' (LuxSE Principle 3, Recommendation 3.5). While there are no specific legal provisions regarding independent directors, it is generally understood that all directors, including independent directors, should be provided with timely information for the proper performance of their duties.

Liability of directors

The directors' duties are owed to the company and as such they may be held liable towards the company both on civil and criminal grounds. They are jointly and severally liable in accordance with the general provisions on civil liability[29] and the provisions of the Act,[30] both towards the company and towards all third parties for any damage resulting from a violation of the Act or of the AoA of the company.

Directors must act in the best corporate interests of the company and are obliged to comply with the Act and with the company's AoA. This includes the obligation to act as reasonably prudent businesspersons. They must manage the company's business in good

28 Should the company not have an audit committee, LuxSE Principle 9, Recommendation 9.1 requires that the board reassess the need to create an audit committee annually.

29 Articles 1382 and 1383 of the Luxembourg Civil Code.

30 Article 59 of the Act.

faith, with reasonable care, in a competent, prudent and active manner, at all times in the company's best interests, and must refrain from doing anything that does not fall within the scope of the company's corporate objectives. The Act also imposes certain general duties on directors, including the general management of the company, representation of the company towards third parties and upholding their duty to avoid any conflict of interests.

The Luxembourg legislator has remained silent on what should be considered a company's best corporate interest. In its judgment of 23 December 2015,[31] the Luxembourg District Court made some observations on this notion. It explained that it is an adaptable concept the exact interpretation of which depends on the company concerned and the nature of its activities. For some companies, the corporate interest is aligned to the interests of a company's shareholders. For other companies, it includes the interest of the legal entity as a whole, including the interests of shareholders but also those of employees and creditors. The Court remarked that for companies that are used for purposes of financing and pure holding companies, the interest of the company's shareholders will be of overriding importance as the focus of the company's activities is on the rate of return of its investments.

However, it should be noted that directors of LuxSE-listed companies are held to a number of more specific duties under the Transparency Act and the Market Abuse Regulation, in addition to the LuxSE regulations and principles. Under LuxSE Principle 2, the board of a listed company is bound by a fiduciary duty to its company and shareholders, and must act in the company's best interests and protect the general interests of the shareholders by ensuring the company's long-term success.

In the event of misconduct, according to prevailing doctrine and case law, the shareholders' meeting must decide whether to make any claim against a director in connection with faults committed by the director in the performance of his or her functions. Creditors of a company may, under certain circumstances, institute action on behalf of the company if the latter fails to do so and if that failure harms the company's creditors (under Article 1166 of the Civil Code).

Directors' liability towards the company is exonerated further to cover the discharge granted to the board by the annual shareholders' meeting approving the annual accounts. This discharge is valid for the period covered by the accounts presented to and approved by the general meeting of shareholders, provided that they do not contain any omission or false statement of a material fact. Although a discharge given by the general meeting of shareholders extinguishes the board members' liability towards the company, it is important to note that proceedings initiated by third parties are not affected by such a discharge.

The company as well as third parties (including any shareholder or creditor with a legitimate interest) may bring an action against a director. Shareholders may, however, only seek compensation for a prejudice that is distinct from the company's collective damage, and that can be defined as an individual and personal damage. The possibility for a (minority) shareholder to sue a director has recently been given an explicit legal basis in Luxembourg law.[32]

If the shareholders have suffered collective damage, it is up to the shareholders' meeting to demand compensation, in which case an action must be brought by the shareholders' meeting on behalf of the company (an action initiated by a single shareholder will be dismissed). The legal basis for the action differs depending on whether the proceedings are invoked by the company or by third parties.

31 Luxembourg District Court, 23 December 2015, numbers 145 724 and 145 725.

32 See Section V, *infra*.

Any action by the company has a contractual basis, whereas an action by third parties will be brought on the grounds of tort liability. Whereas, under contractual liability, only reasonably foreseeable damage is to be repaired (except in cases of fraud), under tort liability all damage caused by the misconduct must be repaired. To elude collective liability, a director must prove that he or she has not taken part in the breach of the Act or of the AoA of the company, that no misconduct is attributable to him or her and that he or she reported the breach at the first shareholders' meeting following his or her discovery or knowledge of the breach.

For listed companies, the LuxSE rules and regulations provide a series of sanctions in the event its rules are breached, including fines or compensation for damage caused to the stock market.

The directors of a public limited liability company are appointed for a period that cannot exceed six years,[33] although they can be re-elected if the company's AoA do not provide otherwise. They may at any time be removed from office by the general meeting of shareholders[34] without cause, by simple majority. It is also possible to provide for stricter conditions in the AoA via a supermajority vote to appoint or revoke the directors. Another possibility is to authorise each category of shareholders to nominate candidates, among which the general meeting of shareholders will elect the directors.

Conflicts of interest of directors

Regarding the rules relating to conflicts of interest,[35] any director who has, either directly or indirectly, an interest pertaining to property law that is contrary to that of the company in a transaction submitted for approval to the board is obliged to inform the board of his or her conflict, refrain from taking part in the deliberations, abstain from voting and record his or her statement in the minutes of the meeting. A special report regarding the transactions in which one of the directors had a (potential) conflict of interest is then to be prepared and submitted at the next general meeting before voting on any resolutions. If, because of a conflict of interest, the number that is required by virtue of a company's AoA to deliberate and vote on a certain matter is not reached, the board of directors can – unless otherwise provided by the company's AoA – decide to defer the decision to the company's general meeting of shareholders. The above-mentioned obligations do not apply when a decision to be taken by the board relates to the company's normal course of business and is taken under normal conditions.

For listed companies, Principle 5 requires directors to show integrity and commitment. It is recommended that directors of LuxSE-listed companies:

- *a* inform the board of any possible conflict of interest;
- *b* take decisions in the best interests of the company;
- *c* warn the board of possible conflicts between their direct or indirect personal interests and those of the company or an entity controlled by it; and
- *d* refrain from taking part in any deliberation or decision involving such a conflict (unless they relate to current operations concluded under normal conditions).

33 Article 51, fourth paragraph, of the Act.

34 Article 2004 of the Luxembourg Civil Code.

35 Article 57 of the Act.

III DISCLOSURE

i Financial reporting and accountability

All companies must file all company accounts annually under the Act; Article 309 imposes consolidated accounting for all Luxembourg-based companies where the company has a majority of the shareholding or voting rights in another entity; is a shareholder or member in another entity and has the right to approve or appoint a majority of the members to the administrative, management or supervisory body of the entity; or is a shareholder or member of another entity and solely controls a majority of shareholders' or members' voting rights in the entity, further to a shareholder or member agreement.

On 18 December 2015, Luxembourg parliament passed an act implementing Directive 2013/34/EU. This act made various changes to the preparation of the annual accounts of Luxembourg companies. Among other things, it changed the rules that are used to determine the size of a company. Depending on whether a company can be categorised as 'small', 'medium' or 'large', various financial reporting obligations apply to it, such as the obligation to draw up consolidated annual accounts or the obligation to use a certain structure of balance sheet and profit and loss account. In addition, the disclosure requirements for small companies changed, and a principle of materiality was introduced (as a result of which information that is considered immaterial may be omitted in the annual accounts).

The LuxSE Principles additionally require that a set of rules be drawn up to regulate the behaviour and the notification obligations relating to transactions of the company's securities, and to specify which transaction information should be made public. These rules should also place the appointment of a compliance officer, charged with monitoring compliance to the rules, under the responsibility of the board. Principle 9 requires directors to 'establish strict rules, designed to protect the company's interests, in the areas of financial reporting, internal control and risk management'. This includes creating, where relevant, an audit committee to discharge the board from its responsibilities of risk management, internal control and financial reporting. The effectiveness of the company's financial reporting, internal control and risk management system must also undergo regular scrutiny.

LuxSE-listed and Euro MTF-traded companies are additionally subject to the internal LuxSE rules and regulations, which contain a number of disclosure rules primarily derived from the Transparency Act as well as the Market Abuse Regulation. Legal obligations do not specifically include impacts outside the jurisdiction, unless the impacts influence the financial reporting obligations, in which case they must be reported.

The CSSF is responsible for verifying LuxSE-listed companies' reports and may issue administrative and criminal sanctions in cases of failure to report or misrepresentation, in particular under the Transparency Act. The company's corporate governance charter should also be made available on its website. In practice, companies publish press releases and past information in addition to regulated information (see Section I, *supra*).

However, since reporting on non-listed companies' social impacts remains on a soft-law basis, there are few legal consequences in cases of misrepresentation or failure to report. Some companies have put internal procedures in place to address complaints that an employee failed to comply with an internal code of conduct.[36] It cannot be excluded that a violation of a CSR obligation may potentially be alleged by a third party if a company does not respect

36 See, for example, PricewaterhouseCoopers' corporate governance procedure at www.pwc.lu.

one of its publicly available CSR engagements. However, so far there is no case law or doctrine in the field, and such a claim would depend on the third party being able to prove its personal interest or damage in the claim.

Auditors' role and authority, and independence

The Act of 28 July 2016 on the Auditing Profession (the Audit Act) and Luxembourg legislation exclusively reserve, *inter alia*, statutory audits to statutory auditors and to audit firms that have been approved by the CSSF. Access to the auditing profession is regulated by the Audit Act, and the titles 'auditor' and 'audit firm' are exclusively granted by the CSSF to applicants upon fulfilment of certain criteria. The CSSF also administers a database of statutory auditors, approved statutory auditors, audit firms, approved audit firms, trainee statutory auditors and candidates to the audit profession, including third-country auditors and audit entities registered pursuant to Article 12 of the Audit Act. Registered auditors and registered auditing firms must also be members of the Luxembourg national auditing organisation, the Institute of Registered Auditors, which is charged with enforcing the strict application of the rules of the auditing profession and members' respect of their professional obligations.

The question and definition of the independence of auditors remain unresolved. Under the Luxembourg definition, the requirement for registered auditors and registered auditing firms to be independent from the entity they are reviewing translates as auditors being prevented from being directly or indirectly associated with the decision-making process of the entity reviewed. The auditor is also prevented from auditing the accounts if there is any form of direct or indirect relationship, be it financial, business, employment or other, including the provision of additional services other than audit, between the registered auditor, the registered auditing firm or its network and the entity under review.

The comply or explain model and mandatory disclosure

The LuxSE Principles were drafted to be highly flexible to be adaptable to the size, structure, exposure to risks and specific activities of each company. Their comply or explain system allows companies to deviate from the recommendations when justified by companies' specific circumstances, provided that adequate explanation is provided.

The comply or explain approach, recommended by the Organisation for Economic Co-operation and Development and the European Commission, is favourably received by company boards and investors. The LuxSE Principles consist of three sets of rules: general principles (comply), recommendations (comply or explain) and guidelines. The general principles form the structure upon which good corporate governance should be based and are drafted in a sufficiently broad manner to enable all companies to be able to adhere to them, whatever their particular features. Without exception, all Luxembourg-based listed companies must apply the principles.

Given the flexible comply or explain approach, shareholders (and in particular institutional investors) have a paramount role in the thorough evaluation of a company's corporate governance, should carefully examine the reasons provided by a company whenever it is found to have departed from the recommendations or failed to comply with them, and make a reasoned judgement in each case. The shareholders should be open to dialogue in cases where they do not agree.

Majority or controlling shareholders may see to the internal and external monitoring of the company, with the risks and advantages that this necessarily involves. The principles underline that the controlling or strategic shareholders make judicious use of their power and respect the rights and interests of the minority shareholders.

The possibility of one-on-one meetings of directors with shareholders is not regulated by Luxembourg legislation. While possible, in practice, such meetings will depend on, *inter alia*, the size of the company, its structure, and the number and geographic location of shareholders and directors.

IV CORPORATE RESPONSIBILITY

For listed companies, one of the guidelines in the LuxSE Principles suggests that the board appoint a compliance officer whose duties and responsibilities should be defined by the corporate governance rules. The compliance officer's mission is, *inter alia*, to monitor compliance with rules regarding transactions in the company's shares. The LuxSE Principles further suggest that the compliance officer has access at all times to the chair of the board and the audit committee. Principle 9 requires the board to draw up strict rules to protect the company's interests, notably regarding risk management, internal control and financial reporting. Principle 9, Recommendation 9.1 suggests the board to appoint an audit committee to assist in the board's discharge of liability in the areas of financial reporting, internal control and risk management (see Section III, *supra*).

i Compliance policies and whistle-blowing

Luxembourg's national commission for data protection (CNPD) published guidelines on the rules to be respected by Luxembourg entities putting a whistle-blowing policy in place. This guideline is largely based on the 'Article 29' Group's Opinion 1/2006 on the application of EU data protection rules to internal whistle-blowing schemes in the fields of accounting, internal accounting controls, auditing matters, fight against bribery, banking and financial crime. Notably, a company must notify the CNPD of the implementation of a whistle-blowing policy further to Articles 12 and 13 of the Act of 2 August 2002 on the Protection of Persons with Regard to the Processing of Personal Data.[37] The CNPD provides guidelines to ensure that the whistle-blowing policy is perceived to support rather than replace efficient management and CSR. In 2011, Article L271-1 was added to the Luxembourg Labour Code with the aim of encouraging whistle-blowing activities. Article L271-1 states that no disciplinary action may be taken against employees on the mere grounds of their protest against or refusal of something that they consider in good faith to constitute an unlawful taking of interest, corruption or undue influence as defined under Articles 245 to 252, 310 and 310-1 of the Luxembourg Criminal Code, whether committed by their employer, any other person senior in rank to them, their colleagues or any third party in relation to the employer.

37 www.cnpd.public.lu/fr/legislation/droit-lux/doc_loi02082002_en.pdf.

ii CSR for other stakeholders and employees

Non-shareholders

Under Luxembourg law, directors are neither legally required to take the company's impact on non-shareholders into account; nor are they prevented from doing so. One of the guidelines in the LuxSE Principles recommends that the board give proper consideration to its staff policy and code of business ethics in determining the company's values. This could therefore be applied to the board's decision-making process, although it is only a very general guideline.

In practice, an increasing number of private companies are taking social criteria into account in their decision-making and disclosing such information to the marketplace (e.g., the CSR commitments published on the websites of several major Luxembourg-established companies, such as SES and ArcelorMittal, which publicly declare that they will take the social and environmental impacts of the company's operations into account, both on a national and international level). This consideration may extend to other companies or business partners, but on a voluntary basis only.

Employees

Article L426-1 et seq. of the Luxembourg Labour Code introduced a legal requirement for employee representatives on certain company boards. This legal obligation is limited to public limited liability companies fulfilling two criteria: all companies established in Luxembourg and employing over 1,000 employees over a three-year period; and all companies established in Luxembourg in which the state retains a financial participation of over 25 per cent, or that exercise a state-awarded concession.

Despite the lack of a more general legal requirement concerning representation on company boards, it should be noted that employees in Luxembourg workplaces with more than 15 employees have a legal right to representation at work (Article L411-1 of the Luxembourg Labour Code). The central element of workplace representation is the worker's representatives concerned with workers' everyday concerns and directly elected by all employees. As a result of the adoption of the Act of 23 July 2015, workers' representatives saw their duties increased and were given a larger say in certain decision-making processes. The scope of their right to information was also enlarged.

In larger companies employing an average of 150 or more workers over a three-year period, Article L421-1 et seq. of the Luxembourg Labour Code provide for a joint company committee – a joint employer–employee body aimed at improving industrial relations in the workplace. The law requires the company's managing director to inform and consult the joint committee at least once a year on the company's current and prospective staffing needs and on any training, refresher training or retraining implications for employees. The law authorises the joint committee to deliver an opinion on economic and financial decisions that could have a serious effect on the structure of the company or on employment levels. The committee also has the right to take part in joint decisions on a number of issues concerning human rights, such as:

a the introduction or running of technical equipment intended to monitor the behaviour and performance of employees at work;

b the introduction of, and alterations to, measures relating to occupational health and safety and the prevention of workplace accidents;

c the drawing up of, and amendments to, general criteria affecting the selection of staff for promotion, transfer and dismissal and at the recruitment stage; and

d the drawing up of, and amendments to, general criteria used in staff assessments.

Unlike in some other European countries, there is no legally backed trade union workplace presence in Luxembourg, although trade unions have a substantial range of rights in the election and operation of employee delegations. Unions also have important rights in joint company committees, and to our knowledge the majority of employee representatives are union members.

Despite an increasing number of non-discrimination laws, including a new equal treatment chapter in the Luxembourg Labour Code[38] implementing Directive 2000/78/EC, there is no binding anti-discrimination legislation currently in place specifically targeting non-discrimination on company boards.

V SHAREHOLDERS

i Shareholder rights and powers

Equality of voting rights

The Shareholder Act came into force on 1 July 2011 aiming, *inter alia*, at strengthening the exercise of minority shareholders' voting rights in listed companies to improve the corporate governance of such companies. The Shareholder Act explicitly refers to a principle of equal treatment of shareholders. This principle is limited to the participation of shareholders at the general meeting of shareholders and the exercise of their voting rights at that meeting. The Shareholder Act has amended the previous rule that one vote is in principle attached to one share, henceforth allowing the company to provide for different voting rights for different shares.

The powers of shareholders to influence the board

Article 53 of the Act reserves the management of the company to its board. Should a shareholder be directly involved in the management of the company, he or she may be deemed a *de facto* director and face civil or criminal liability, or both, and generally be liable under the same circumstances as the appointed directors.

Shareholders do, however, control the appointment of the board (and therefore its composition) via a majority decision of over 50 per cent to appoint a new director. In addition, shareholders representing 10 per cent of a company's share capital may force the board to postpone a general meeting of shareholders for a period of up to four weeks.[39]

Furthermore, during the annual general meeting, the shareholders can question the board on all aspects of the company's management, accounting and so forth throughout the year, and may withhold the granting of discharge. Although previously, shareholders were in practice already allowed to ask questions during the meeting and to receive answers to their questions, the Shareholder Act now expressly lays down that shareholder right in relation to the items on the agenda of the meeting.

Under the Shareholder Act, in addition to the right to ask questions orally during a meeting, shareholders may have the right to pose written questions about the items on the agenda before the meeting is held. If provided for in a company's AoA, questions may be

38 Chapter V (equal treatment), Articles L241-1 to L254-1; see www.legilux.public.lu/leg/textescoordonnes/codes/code_travail/Code_du_Travail.pdf.

39 Article 67(5) of the Act.

asked as soon as the convening notice for the general meeting is published. The company's AoA will furthermore provide the cut-off time by which the company should have received the written questions.

Apart from several specific circumstances (e.g., in the case of confidential information), the company must answer any questions addressed to it. Should several questions relate to the same topic, the company may publish a detailed questions and answers document on its website, in which case the chair should draw the shareholders' attention to the publication.

The Act also allows shareholders to submit questions to management outside a meeting. Any shareholder representing at least 10 per cent of the company's share capital or voting rights, or both, can ask the board of directors or management body questions about the management and operations of the company or one of its affiliates, without the need for extraordinary circumstances. If the company's board or management body fails to answer these questions within one month, the shareholders may petition, as in summary proceedings, the president of the district court responsible for commercial matters to appoint one or more independent experts to draw up a report on the issues to which the questions relate.[40]

Certain matters must also be reported to the shareholders, such as any director's conflict of interest relating to voting on a resolution (see Section II, *supra*).

Furthermore, if a minority shareholder of a public limited liability company finds that directors and members of its management and supervisory boards are negligent or simply not diligent in the performance of their duties, it may sue them. Such an action may be brought by one or more shareholders or the holders of founders' shares, or both, representing 10 per cent or more of the company's voting rights.[41]

Decisions reserved to shareholders

Article 53 of the Act provides that a company's management board has the most extensive powers to perform all actions necessary or appropriate to fulfil the company's corporate objective, with the exception of the actions specifically reserved by law to the shareholders' meeting (*inter alia*, all amendments to the company's AoA, approval of annual accounts and allocation of the company's results are reserved to the company's shareholders).

Rights of dissenting shareholders

The Act currently recognises only a few rights of action on behalf of the company in favour of individual shareholders.

The extension of the protection of minority shareholders by stipulating provisions in the company's AoA (e.g., the right of a minority coalition to propose directors, provisions for a more stringent majority for certain decisions, approval clauses or share transfer restrictions) is well recognised insofar as the arrangement does not conflict with Luxembourg's public order rules.

The use of shareholders' agreements of a purely contractual nature is far more common than providing for relevant provisions in the AoA. The use of shareholders' agreements is now explicitly recognised in Luxembourg law. It is important to note that the Act does not state that these type of arrangements need to be limited in time. However, it does set out three types of voting arrangements that are null and void: (1) a shareholders' agreement

40 Article 154 of the Act.

41 Article 63 *bis* of the Act.

that violates the provisions of the Act or that is contrary to a company's corporate interest; (2) an undertaking by a shareholder to vote in accordance with instructions given by the company itself, a subsidiary or any corporate organ of those entities; and (3) an undertaking by a shareholder to those same companies or corporate organs to approve proposals made by the company's corporate bodies.[42] If votes are cast at a general meeting of shareholders pursuant to an invalid voting arrangement, the votes shall be considered null and void along with any resolutions taken, unless the votes did not affect the final outcome. While the use of shareholders' agreements does allow for discretion and flexibility, any compulsory implementation of this type of arrangement remains at risk.

Providing additional protection in favour of groups of minority shareholders, whether in the AoA or otherwise, is quite common in Luxembourg, particularly among international joint ventures and groupings that use a Luxembourg company structure to promote mutual business activities.[43]

As a last resort, dissenting shareholders may seek to invalidate a shareholder decision that has been taken on the basis of five grounds that are specified in the Act: (1) a procedural irregularity that influenced or could have influenced the outcome of the decision; (2) a violation with fraudulent intent of the rules governing general meetings; (3) an *ultra vires* act or abuse of power affecting the decision; (4) the exercise at a general meeting of voting rights that have been suspended by legislation other than the Act, provided the quorum or majority required to adopt the decision would not have been met but for the unlawful exercise of these voting rights, and (5) any other cause provided for by the Act.[44]

Also of note is the sell-out right in favour of minority shareholders. Under the Squeeze-out Act, in the event of an individual or legal entity acquiring at least 95 per cent of the share capital of the company and subject to certain conditions being met, the remaining minority shareholders are entitled to exercise a sell-out right within three months of the required notification and publication of the acquisition.[45]

Benefits for long-term shareholders

The Act does not provide for any specific benefits (e.g., extra votes or dividends) for long-term shareholders, although such facilities may be agreed upon in a shareholders' agreement or incorporated into the AoA, or both.

Shareholder approval of board decisions

While the Act does not set out any specific areas in which board decisions must be approved by the shareholders, the AoA of the company may provide that all or certain board decisions must be ratified by the shareholders.

42 Article 67 *bis* of the Act.

43 For further analysis on minority shareholders rights, see also Marc Elvinger, 'Les minorités en droit des affaires: rapport luxembourgeois', *Annales du droit luxembourgeois*, No. 15 (2005).

44 Article 12 *septies* of the Act.

45 See footnote 4, *supra*.

ii Shareholders' duties and responsibilities

Controlling shareholders' duties and liability

All shareholders have certain obligations by law, including the payment of shares, a proportional contribution to any losses suffered by the company and an obligation of loyalty.

In addition, the controlling shareholders are notably prevented from dictating or imposing an increase of the other shareholders' obligations without their prior consent, although this principle has been considerably attenuated by the Squeeze-out Act,[46] which granted the right to force the acquisition of shares held by minority shareholders to shareholders controlling at least 95 per cent of the share capital.

Institutional investors' duties and best practice

While institutional investors must bear in mind potential reputational repercussions relating to their investments, there are no particular duties imposed specifically on institutional investors and no requirement for institutional investors to specifically consider third-party impacts in their investment decisions. However, a number of Luxembourg-based investors have signed the United Nations-supported Principles for Responsible Investment[47] (an investor initiative in partnership with the United Nations Environmental Programme Finance Initiative and the United Nations Global Compact). The first of these six principles is to incorporate environmental, social and corporate governance considerations into investment analysis and decision-making processes. Furthermore, a growing number of investors – while not being signatories to the Principles for Responsible Investment – are taking the private initiative to take such risks into account.

Code of best practice for shareholders

Luxembourg has no official code of best practice for shareholders, although companies may draw up internal codes of best practice for their shareholders.

iii Shareholder activism

Shareholder activism is not a defined notion under Luxembourg law, and neither derivative actions nor proxy battles are common practice in Luxembourg.

iv Takeover defences

Takeover bids are covered by the Luxembourg Takeover Act of 19 May 2006 (transposing Directive 2004/25/EC). The scope of this Act is limited to companies whose shares are traded on a regulated market in one or more member states of the European Union. Although Luxembourg law admits the principle of defensive measures, there has been no case law specifically covering the question as yet. In implementing any defensive measures, the board has an obligation to act in good faith with respect to the shareholders' interest.

In the absence of a specific provision in a company's AoA requiring shareholder approval, the board may adopt defensive measures (e.g., issuing new shares within the limits of authorised capital or selling key assets) without the approval of the shareholders, provided that these measures are taken in the best interests of the company. The board may not

46 Ibid.

47 www.unpri.org.

prohibit the shareholders from accepting an offer. It should be noted, however, that measures aimed at frustrating bids in the long term are not generally deemed to be admissible under Luxembourg legislation. It would, therefore, not be possible to repeat defensive measures whenever the bid is repeated or to take defensive measures that have a long-term effect.

Shareholder and voting rights plans, and similar measures

As a general rule, any increase of a Luxembourg company's share capital is decided upon by the general meeting of shareholders. However, the articles of association of a Luxembourg public limited liability company may authorise the board of directors to increase the share capital up to a designated amount in one or more instalments.[48] The authorisation to do so is only valid for a period of five years, but may be renewed by the general meeting of shareholders. As an inducement for an existing shareholder to purchase more shares, it may be decided to abandon any payment of share premium. Beyond that, there is no possibility for a company to offer a discount on the par value of shares to be issued.

White-knight defence

In Luxembourg practice, the board of any company that is the subject of a takeover bid may seek out a third party with the purpose of the third party making a counter-offer that is more favourable to the company. It can do so without the need for approval by the company's shareholders.

Staggered boards

Directors of a Luxembourg public limited liability company shall be appointed for a term of office that may not exceed six years. However, directors may be removed from office by the general meeting of shareholders at any time and without stating reasons. As a result, a staggered board does not constitute a major obstacle for a hostile acquirer holding sufficient shares to make changes to the composition of the board.

v Contact with shareholders

Pursuant to the Shareholder Act, listed companies must give at least 30 calendar days' notice before holding a meeting (notwithstanding particular requirements under the Takeover Bid Act). By doing so, Luxembourg's parliament has imposed a longer notice period than the 21-day notice period required under Directive 2007/36/EC. Should the quorum not be met at the first meeting, a second meeting must be convened at least 17 calendar days before the meeting is held. The convening notice must be published in the electronic compendium of companies and associations, a Luxembourg newspaper and other media in a manner that ensures the effective distribution of the information to the public throughout the European Economic Area. In the event that all the shares are registered, convening notices may be sent by registered letter to the shareholders, members of the board (or the management board

48 As a result of the entry into force of the Luxembourg Act of 10 August 2016, the AoA of Luxembourg private limited liability companies may now also include an authorisation to the board of managers to issue shares, provided that the shares so issued are either issued to existing shareholders or to a third party that has been approved in accordance with the law.

and the supervisory board) and the statutory auditors. The Shareholder Act requires that, in addition to the agenda, date and place of the general meeting to be held, convening notices must also include:

a a clear description of the shareholders' rights to put items on the agenda and to table draft resolutions, the procedure for voting by proxy and a form to be used for that purpose and, if provided for in the company's AoA, the procedure to vote by electronic means;

b postal and email addresses that can be used to obtain documents in relation to the meeting;

c where applicable, a copy of the 'record date' as defined by the Shareholder Act (i.e., the date by which shareholders must register their shares to participate and vote at the general meeting). The date for listed companies is set at midnight CET on the 14th calendar day before the meeting. The shareholder must notify the company at the latest by this date of its intention to participate in the meeting; and

d the company's website address, which must contain all of the above information, as well as a full copy of the draft resolutions.

The Shareholder Act allows distance voting by shareholders in advance of the meeting, provided that the company expressly recognised this possibility and has outlined the related requirements in its AoA. The Shareholder Act details the content of the ballot paper, which must include, *inter alia*, the full identity of the shareholder, the content of the vote cast in advance, the agenda of the meeting and the deadline before which the ballot paper must be received.

The Shareholder Act requires proxy voting to be offered to shareholders, under certain conditions, with the proxy holder having the same rights as the shareholder. The company has no obligation to verify that the proxy holder votes in accordance with the shareholder's instructions.

VI OUTLOOK

While corporate governance is currently, in general, voluntary, a growing number of institutional guidelines and codes are being developed, and the Luxembourg government is working towards promoting corporate governance on a national level.

Notably, Luxembourg is required to bring into force the laws, regulations and administrative provisions necessary to comply with the Fourth EU Anti-Money Laundering Directive by 26 June 2017. Luxembourg is currently working on legislation implementing this directive, which will have a profound influence on beneficial ownership identification.

Furthermore, the second Markets in Financial Instruments Directive and the accompanying Regulation on Markets in Financial Instruments are expected to enter into force in January 2018 and will further improve the functioning of financial markets and reinforce investor protection.

Appendix 1

ABOUT THE AUTHORS

MARGARETHA WILKENHUYSEN

NautaDutilh Avocats Luxembourg S.à r.l.

Margaretha (Greet) Wilkenhuysen is a partner in the corporate practice of NautaDutilh Avocats Luxembourg. She specialises in cross-border corporate transactions, with a particular focus on mergers and acquisitions, joint ventures and international corporate restructurings and corporate finance. Her clients include major international corporations and she has represented both domestic and international clients in a variety of high-end transactions. Her extensive experience and knowledge resulted in her being nominated from 2011 through 2017 as a 'Leading Lawyer' in the *IFLR1000*.

Ms Wilkenhuysen received her law degree from the Katholieke Universiteit Leuven in 1991, a master's degree in business and tax law from the Free University of Brussels in 1993, and an LLM from Duke University School of Law in 1996. She joined NautaDutilh in 1997 and became a partner in 2007.

Ms Wilkenhuysen is a frequent writer and speaker and has published various books and articles (e.g., *Due Diligence* (2011 – new edition), *Cross Border Mergers* (2011) and *Capital Directive* (2014)). She also published an article on cross-border mergers in 'Un siècle d'application de la loi du 10 août 1915 concernant les sociétés commerciales' (2015). She is also a member of the International Bar Association, the European Private Equity and Venture Capital Association and the Duke Alumni Association.

STEVEN VAN WAAS

NautaDutilh Avocats Luxembourg S.à r.l.

Steven van Waas is an associate in the corporate practice of NautaDutilh Avocats Luxembourg. He assists clients on various corporate matters including M&A, private equity, corporate finance and general corporate and commercial advice.

Mr van Waas graduated from Utrecht University in 2010 with an LLM degree in Dutch civil law and an LLM degree in corporate, social and economic law. In 2011, he obtained an LLM degree in European law from Panthéon-Assas University (Paris II).

NAUTADUTILH

NautaDutilh Avocats Luxembourg S.à r.l.
2 rue Jean Bertholet
1233 Luxembourg
Tel: +352 26 12 29 1
Fax: +352 26 68 43 31
ndlux@nautadutilh.com
www.nautadutilh.com