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Countdown to the end of the Luxembourg Companies Law transition period

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Authors: **Christophe Balthazard**, **Vincent Naveaux**, **Alix van der Wielen**

The transition period for the Luxembourg companies law (as amended by a law dated 10 August 2016) will end on 23 August 2018. Do you need to update your articles of association to comply with the new provisions of the law?

The Luxembourg law governing commercial companies dated 10 August 1915, as amended (the **Companies Law**), was substantially amended by a law dated 10 August 2016 which entered into force on 23 August 2016 (the **2016 Law**).

While the 2016 Law was meant to codify certain existing practices and provide additional flexibility, a limited number of amendments resulted in new obligations or additional formalities to comply with.

Companies incorporated prior to the entering into force of the 2016 Law benefit from a twenty-four (24) month transition period to comply with these new obligations, which will end on 23 August 2018.

Measures to be taken to amend the articles of association

Articles of association of Luxembourg companies which, as a result of the 2016 Law, no longer comply with the Companies Law should be amended in the manner required for amendments of articles of association generally.

However, where the amendments are limited to reflecting the new numbering of the provisions of the Companies Law, the 2016 Law allows the management bodies of Luxembourg companies to proceed with the requisite formalities.

Any clause of the articles of association that is not amended to comply with the new provisions of the Companies Law shall be disregarded, and the mandatory provisions of Luxembourg law shall apply in its stead.

Changes of note in the 2016 Law

Distribution of interim dividends by SARLs

Prior to the 2016 Law, the Companies Law did not contain any explicit provisions allowing private limited liability companies (**SARLs**) to distribute interim dividends. Practitioners had accepted that such distributions could be made provided that they were authorized in the articles of association. Market practice had evolved to require a set of recent interim accounts to evidence that the funds available for distribution were sufficient, but the exact date of the interim accounts and the involvement of an independent or statutory auditor were a matter for each board of managers to determine according to their assessment of their potential liability.

Article 710-25 (previously article 198*bis*) of the Companies Law now explicitly authorizes managers of SARLs to distribute interim dividends subject to the following conditions:

1. Interim accounts must be drawn up showing that the funds available for distribution are sufficient;

2. The amount to be distributed may not exceed (i) total profits made since the end of the last financial year for which the annual accounts have been approved, *plus* (ii) any profits carried forward and sums drawn from reserves available for this purpose, *less* (iii) losses carried forward and any sums to be placed in reserve pursuant to the requirements of the law or of the articles;

3. The decision of the managers to distribute an interim dividend may not be taken more than two months after the date at which the interim accounts referred to under 1. above have been drawn up; and

4. The statutory or independent auditor, if any, shall verify whether the above conditions have been satisfied.

If the articles of association of your SARL contain detailed provisions regarding the distribution of interim dividends, a review should be carried out to ensure that such provisions comply with the new rules in the 2016 Law (e.g., with respect to the date of the interim accounts).

Conflicts of interests in SARLs

Managers of SARLs have always been subject to fiduciary duties towards the company that appointed them but, prior to the 2016 Law, the Companies Law did not contain any explicit provisions setting forth how managers should act in case of conflicts of interest. It was therefore widely accepted that SARLs could contractually determine the obligations of managers in this context. For instance, it was not unusual to allow managers to deliberate and vote even where there was a conflict of interest.

The 2016 Law has extended to managers of SARLs the conflicts of interest provisions applicable to directors of public limited liability companies (**SAs**). As a result, managers of SARLs are now prevented from deliberating and voting on any item on which they have a conflict of interest, and conflicts must be disclosed to the general meeting at its next meeting prior to the approval of any resolutions.

If the articles of association of your SARL contain conflict of interest provisions, a review should be carried out to ensure that these provisions comply with the new rules in the 2016 Law.

Exit right for shareholders in SARLs

A defining feature of SARLs is the requirement that any transfer of shares to a non-shareholder requires the prior consent of the general meeting. In the past, the refusal of the general meeting to give its consent meant that no transfer of shares could take place.

Following the 2016 Law, article 710-12 (previously article 189) of the Companies Law now provides that if the general meeting refuses to give its consent but the selling shareholder does not want to retain its shares, the company or the remaining shareholders (or a third party designated by the remaining shareholders) must acquire the shares (at a price determined in accordance with the articles of association) within three months from the refusal. Failing the exercise of such acquisition right, the selling shareholder may freely proceed with the intended transfer.

If the articles of association do not contain a price determination mechanism, there is a risk that a shareholder wishing to sell its shares may sell to third parties at any time (without complying with the procedure of the new article 710-12), as the remaining shareholders and the company would not be in a position to acquire them at a determined sale price.

If your SARL has several shareholders, the articles of association should be amended to determine the price at which the shares could be acquired by the company or the remaining shareholders (or a third party designated by the remaining shareholders) in case a transfer to a non-shareholder is refused by the general meeting.

Limitations on pre-emption and approval rights in SAs and SCAs

Notwithstanding the fact that shares of SAs and of partnerships limited by shares (**SCAs**) are by nature freely transferable, practitioners had accepted they could be subject to preemption rights or to approval processes (to the extent that such shares could be disposed of within a reasonable period of time).

The 2016 Law has codified this possibility while providing that such preemption or approval processes must be completed within 12 months from the date of the transfer request. Should these clauses provide for a longer time period, such time period shall automatically be reduced to 12 months.

However, as preemption and approval processes are generally broken down into several steps, each having its own duration, it would unadvisable in practice to rely on this automatic reduction of the whole duration.

If the articles of association of your SA or SCA contain preemption or approval provisions, a review should be carried out to determine the duration of the relevant process and, if it exceeds 12 months, the various periods of time should be reduced to comply with the new rules.

Management committees (comités de direction)

Market practice has developed to allow the boards of directors of SAs to create committees – particularly for operational entities that require specialist or expert knowledge. Until the 2016 Law, boards of directors were free to delegate powers to committees (to the extent that they were not delegating all their powers) under the general rules applicable to delegation of powers.

The 2016 Law has introduced the possibility for the boards of directors of SAs to delegate their management powers to management committees (*comités de direction*), provided that this process:

- is authorized in the articles of association; and
- does not cover the setting of the general policy of the company, or the whole of the powers reserved for the board of directors.

N.B., although boards of directors may restrict the powers delegated to management committees, such restrictions are not enforceable against third parties.

If your SA operates with a management committee, such committee should be renamed (if you do not wish it to have the features of the management committee created by the 2016 Law) or the articles of association should be amended to confirm that the board of directors may delegate management powers to such committee.

Authorized share capital in SARLs

Prior to the 2016 Law, the Companies Law did not contain any explicit provisions allowing authorized share capital in SARLs. Certain practitioners had nevertheless accepted that managers of SARLS could be authorized to issue new shares to existing shareholders under the terms set forth in the articles of association.

The 2016 Law has codified this practice. Article 710-26 (previously article 199) of the Companies Law makes the authorized capital provisions applicable to the SAs also applicable to SARLS, it being understood the any non-shareholder to which shares are issued must have been approved by the general meeting in compliance with article 710-12 (previously article 189) of the Companies Law.

If the articles of your SARL authorize the managers to issue shares, a review should be carried out to ensure that the provisions comply with the new provisions of the Companies Law. This could also be an opportunity to remove any restrictions that are no longer required (e.g., limiting the issue of new shares to existing shareholders).

Limitations on the number of shares to be redeemed by SARLs

Prior to the 2016 Law, the Companies Law did not explicitly allow SARLs to redeem their own shares. Practitioners had accepted that shares could be redeemed under the assumption that the rules applicable to SAs would have to be complied with.

The Companies Law now explicitly allows SARLs to redeem their shares without having to comply with the stricter rules applicable to SAs (e.g., there is no need to obtain the prior consent of the general meeting and the managers may cancel the shares and reduce the capital accordingly themselves).

However, contrary to SAs, there is a minimum number of shares of SARLs (i.e. representing the minimum share capital) that must always be held by persons other than the company.

If the articles of association of your SARL allow it to redeem its own shares, they should ideally be amended to ensure that a number of shares (representing the minimum share capital) cannot be redeemed. It could also be an opportunity to remove any formalities that are not applicable to SARLs.

White & Case LLP
Wetstraat 62 rue de la Loi
1040 Brussels
Belgium

T +32 2 239 26 20