INTERNATIONAL CORPORATE LAW AND
FINANCIAL MARKET REGULATION

Perspectives in Company Law and Financial Regulation

EDITED BY MICHEL TISON,
HANS DE WULF,
CHRISTOPH VAN DER ELST AND
REINHARD STEENNOT

8. The Nordic corporate governance model – a European model? 145
Jesper Lau Hansen

SECTION 2 **Corporate governance, shareholders' rights and auditing**

9. Stakeholders and the legal theory of the corporation 165
Peter Nobel

10. The renaissance of organized shareholder representation in Europe 183
Stefan Grundmann

11. In search of a middle ground between the perceived excesses of US-style class actions and the generally ineffective collective action procedures in Europe 200
Douglas W. Hawes

12. Some modest proposals to provide viable damages remedies for French investors 223
Marie-Claude Robert Hawes

13. Pre-clearance in European accounting law – the right step? 231
Wolfgang Schön

14. International standards on auditing and their adoption in the EU: legal aspects and unsettled questions 244
Hanno Merkt

15. Corporate governance: directors' duties, financial reporting and liability – remarks from a German perspective 264
Peter Hommelhoff

16. Some aspects of capital maintenance law in the UK 276
John Vella and Dan Prentice

17. Luxembourg company law – a total overhaul 302
André Prüm

18. Role of corporate governance reform and enforcement in the Netherlands 322
Joseph A. McCahery and Erik P. M. Vermeulen

SECTION 3 **Takeover law**

19. Adoption of the European Directive on takeover bids: an on-again, off-again story 345
Joëlle Simon

20. Application of the Dutch investigation procedure on two listed companies: the *Gucci* and *ABN AMRO* cases 363
Levinus Timmerman

21. Obstacles to corporate restructuring: observations from a European and German perspective 373
Klaus J. Hopt

22. Protection of third-party interests under German takeover law 397
Harald Baum

23. Takeover defences and the role of law: a Japanese perspective 413
Hideki Kanda

PART II **Perspectives in financial regulation**

SECTION 1 **European perspectives**

24. Principles-based, risk-based regulation and effective enforcement 427
Eilis Ferran

25. The Committee of European Securities Regulators and level 3 of the Lamfalussy Process 449
Niamh Moloney

26. Market transparency and best execution: bond trading under MiFID 477
Guido Ferrarini

17

Luxembourg company law – a total overhaul

ANDRÉ PRÜM

I. Introduction

After many years of reacting only to new European directives – the best analyses of which are by Professor Eddy Wymeersch, in whose honour the present contribution is made – Luxembourg company law is now undergoing major modernization, as demonstrated by the series of innovative laws that have been adopted over the last two years. The 25 August 2006 Act on the European company (the *Societas europaea* or SE), *sociétés anonymes* (public limited companies or SAs) with management and supervisory boards and single-person private SAs, together with the first Act of 23 March 2007 reforming the mergers and divisions (M&D) regime, and introducing partial asset contributions, transfers of all assets and liabilities, arms of business and professional assets are the key changes in the overhaul. The creation by the 11 May 2007 Act of a separate framework for companies managing family assets is just one further step intended to encourage the formation of companies under Luxembourg law. At the margins of company law, the 19 May 2006 Act on takeover bids transposes Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004. More modestly, the second Act of 23 March 2007 on international mergers stops a loophole in commercial company law while we await transposal into Luxembourg law of the directive of 26 October 2005 on cross-border mergers of companies with share capital. Of varying scope, these laws all deal with specific matters but do not yet address company law as a whole.

The Luxembourg government is now seeking to move beyond these reforms and to modernize company law in its entirety. It has therefore recently produced a bill amending the 10 August 1915 Act on commercial companies along with several provisions in title IX of the Civil Code that deal with companies. The bill (the Bill), which was submitted to the Chamber of Deputies on 8 June 2007 under number 5730 and is

the result of a long-term project by the Ministry of Justice, supported by the *Laboratoire de Droit Economique*,[1] proposes a large number of changes to the Act with the aim of making it clearer and more attractive. The plan for codification à *droit constant*[2] will round off the ambitious reform programme[3]. The Bill consequently adopts the realistic, consensual approach typical of Luxembourg legislative intent in the field of business law.

The small amount of Luxembourg case law, an obvious result of the low number of disputes and limited quantity of doctrine such a small country can produce, denies Luxembourg the luxury of total originality in its approach to the law. Yet while Luxembourg law can of course seek to differentiate itself from other legal systems through its generally liberal philosophy and innovative solutions, natural caution prevents it cutting itself off entirely from Belgian and French law. The Bill recognizes this connection and in the comments on its various sections takes care to point out the inspiration for the new provisions so that their interpretation can benefit from the analyses and decisions that inspiration provides.

The Ministry of Justice has been particularly careful to find out what the legal professions want and to test their reactions to the solutions provided. The dedicated *Commission d'études legislatives* (Legislation Studies Committee) working group within the Ministry, which includes representatives from the government, public authorities and the legal professions that prepared the reform, has been the focal point for all work. The consultation process was further enlarged by canvassing the opinions of a number of eminent lawyers when work began and before the Bill was finalized.

To prevent the huge number of changes involved in a full overhaul of the 10 August 1915 Act producing just a jumbled patchwork of results, the Bill is firmly anchored to the founding principle of the Act, which Professor Nyssens, one of the originators of the initial text, has summarized as, '*contractual freedom for partners and protection for third parties*'. This dual objective, along with the aim of achieving

[1] Created under the auspices of the *Centre de Recherche public Gabriel Lippmann* and now attached to the Faculty of Law, Economics and Finance of the University of Luxembourg.

[2] Codification *à droit constant* subsumes the content of all previous relevant laws that are not obsolete and then abrogates the laws themselves.

[3] In the wake of Belgium and France, article IV of the Bill provides the legal basis for statutory codification.

a delicate balance between the sometimes contradictory solutions it can produce, are the key guidelines of the proposed reform and for its analysis.

II. Greater freedom

The overarching purpose of company law is to provide economic operators with a framework in which to share resources – traditionally production resources – so that they can run a commercial or civil business. The framework itself can be more or less flexible in determining authorized formats, the way in which a collective will can be formed and expressed in those formats and how those formats are financed. A liberal approach allows future members the widest possible choice on how their company will be structured, the organization of the powers on which it is based and the ways in which it can issue debt securities.

In these three areas (choice of structure, internal organization and type of finance) the Bill opens new doors.

A. *Greater choice of structures*

In line with recent reforms, the Bill increases firstly the range of company formats available and secondly the number of ways in which an existing company may be transformed or restructured.

1. Increased range of company formats to include the *société par actions simplifiée*

The Bill proposes to introduce, in addition to the traditional company formats and the SE introduced by the law of 26 August 2006, a *société par actions simplifiée (SAS)*. The idea is clearly of French inspiration and derives from European company law in particular, which enables operators to avoid the constraints of the 2nd Directive on company law by setting up an SAS. Since their introduction in 1994, French *sociétés par actions simplifiées* have been a major success.

With the same objective, the Bill defines the *société par actions simplifiée* as a company 'whose capital is divided into shares and that is formed by one or more persons who accept liability up to a limited sum only'.[4] The main characteristic of an SAS is not so much this definition as the very significant freedom it gives shareholders to negotiate and create both its organization and their own inter-relations.

[4] Bill: art. 101–18 of the 1915 Act.

The Bill thus gives shareholders free rein in the articles of association to decide how their company is to be managed,[5] which decisions must be taken collectively by the shareholders and which by management alone. In the case of shareholder decisions, the manner and terms of adoption can also in principle be set out without restriction in the articles of association.[6]

As regards relations between shareholders, the Bill allows the articles of association to prohibit the disposal of shares for up to ten years and to make disposals subject to prior approval by the company or to preemptive right. The articles of association may also provide that in some circumstances a member may be required to sell his shares.

These rules, which illustrate the significant freedom allowed to shareholders, should ensure the SAS has a rosy future in many different fields.

2. New transformation solutions

The 27 March 2007 Act has revolutionized merger and demerger law by introducing new, additional ways of restructuring companies. Previously applying to *sociétés anonymes* only, mergers and demergers can now be undertaken by any company with a legal personality of its own and by economic interest groups. A long time coming, full and partial contributions or transfers of assets and liabilities, including of business arms, are a new addition to the range of restructuring techniques allowed. Luxembourg company law therefore now permits companies to use demerger law to transfer assets in the form of a single transfer of all assets and liabilities. They no longer have to make separate transfers of debts and receivables, which are often impossible in practice. At the same time, Luxembourg law has sought inspiration in Swiss law to allow companies, groups and also single-person undertakings to transfer professional assets. No time has been wasted in implementing these new laws, particularly those relating to the transfer of business arms, indicating that they are the answer to what was a pressing need.

[5] Bill: art. 101–21 of the 1915 Act, 'the articles of association set out the terms under which the company will be managed'.

[6] Bill: art. 101–25 of the 1915 Act, 'the articles of association set out the decisions that must be taken by the shareholders collectively and the terms and conditions under which this shall be done'.

To complete the picture, the Bill proposes a reform of the company transformation regime which up to now has applied only to the transformation of one commercial company into another and of civil companies into commercial companies but not the reverse, or the transformation of commercial companies into economic interest groups or vice versa.[7] Such restrictions have no justification. The Bill also allows the transformation of any private entity with a legal personality (company or economic interest group) into any other form of company or economic interest group.

The change would be accompanied by a proposed new transformation regime that is largely drawn from Belgian law (which takes quite a liberal approach to the subject).[8] The new measures are specifically intended to protect members against increased liability to which they have not agreed and third-party rights.[9] For example, the Bill would protect capital if the transformation were from a type of company to which the legal definition of 'capital' does not apply to a company based on that very concept.[10] Majority or unanimous voting rules would apply for such decisions, depending on company type. A unanimous vote would always be required to change from a general partnership to another type of company or from a company with limited liability to one with unlimited liability.[11]

B. *Greater freedom to organize power within the company*

Until the recent reforms, Luxembourg law took a traditional, not particularly innovative approach to the organization and sharing of power within the company. This can be seen firstly in its continuing attachment to the principle of *one share, one vote,* where the only

[7] Bill: art. 3 of the 10 August 1915 Act.

[8] At present the only legislation in the area (apart from that allowing an SE to transform into an SA or vice-versa, as allowed under articles 31–2 and 31–3 of the 10 August 1915 Act) is articles 3 ('The rights of third parties are protected'), 46 (holders of shares that do not carry voting rights acquire them for decisions on whether the company should be transformed), 69(5) ('If the capital reduction would bring the capital below the legal minimum, the meeting of shareholders must at the same time decide either to increase the capital by the appropriate amount or to transform the company') and 137–1(4) ('The provisions relating to the formation of *sociétés coopératives* organised as *sociétés anonymes* apply to the transformation of companies with other forms into *sociétés coopératives* organised as *sociétés anonymes*') of the 10 August 1915 Act.

[9] Bill: art. II, 105, introducing arts. 308bis-15 to 308bis-27.

[10] Bill: art. 308bis-16 to 308bis-20 of the 10 August 1915 Act.

[11] Bill: art. 308bis-21(5), of the 10 August 1915 Act.

exception is non-voting shares that were introduced about twenty years ago, and the system of non-equity *parts bénéficiaires* (income certificates) that do not necessarily carry voting rights. However, the total freedom with which the founders and shareholders of a *société anonyme* can decide the extent of any voting rights and the number of votes attaching to *parts bénéficiaires*, a freedom that distinguishes Luxembourg law from Belgian law, can have a significant effect on the *one share, one vote* principle. The reductive approach to management structures within *sociétés anonymes*, which ignores the management committees that exist in all major companies, is another example of the rather outmoded style of the 1915 Act.

By giving greater scope to the methods for organizing shareholders' rights and powers and to modern types of management within *sociétés anonymes*, while at the same time making it easier for decisions to be taken using modern communication techniques, the Bill increases members' freedom in these areas.

1. Freedom to organize shareholders' rights and powers

The main aims of the Bill are to make it easier to raise capital, to allow more sophisticated allocation of power among shareholders and to allow measures that will encourage a stable share register.

Allowing *sociétés anonymes* to issue shares of differing face value clearly connects to the second objective while at the same time increasing the means they can use to attract new investors. However, since the number of voting rights depends on the size of the stake held, the proportional equality of shareholders would remain protected.[12] Funds could also be raised thanks to the new powers to issue separate subscription rights and shares of less than the fractional value of old shares.[13]

Looking to Belgian law, the Bill would also allow *sociétés anonymes* to give priority rights at capital increases for which pre-emptive rights have been cancelled or reduced.[14] Replacing pre-emptive rights with priority rights should enable third parties to subscribe new shares in public issues at the market price or near market price of the issuer's old shares.

The introduction of shares carrying double voting rights, which already exists under French law, would encourage greater loyalty by rewarding shareholders who retain their shares for at least two years.

[12] Bill: art. II, 22) and 43) amendments to arts. 37 and 67 of the 10 August 1915 Act.

[13] Bill: art. II, 17) and 21) amendments to arts. 32 and 32–4 of the 10 August 1915 Act.

[14] New art. 32–3 to the 1915 Act proposed by the Bill.

The Bill would not however adopt the French approach of restricting this option to European shareholders only.[15]

Since the original reason for banning the sale of future shares or bonds has disappeared,[16] the Bill, following in the footsteps of changes in Belgian law in this area, proposes that the restriction should be lifted.[17] Future shares and bonds would therefore be regulated only by ordinary law on the sale of future items as the sale is defined in article 1130 of the Civil Code.

2. Freedom to organize and operate management structures

The Luxembourg legislator has taken advantage of the arrival of the SE to allow all *sociétés anonymes* to opt for a two-tier management system with both a management board and a supervisory board. Few companies appear to have taken up the option so far but a large number have set up management committees with powers far beyond those needed to carry out day-to-day management. In banking the committee is almost unavoidable if there is to be compliance with the 'four eyes criterion' (*Vieraugenprinzip*). At present, under the 1915 Act the board of directors of a *société anonyme* can permanently delegate day-to-day management only.

The Bill proposes that management committees should be officially recognized and be subject to rules close to those adopted in Belgium in 2002, which allow the articles of association to permit boards of directors to delegate their management powers to a management committee without this impinging on the company's general policies or on any of those areas that are by law reserved to the board of directors.[18] Where such delegation occurs, the board of directors is required to supervise the management committee. To prevent objections to a potential conflict of powers, which Belgian law has not prevented, the Bill is careful to point out that powers delegated to a management committee would be exercised by that committee alone. In other words, the board of directors would not be able to reserve any residual authority in those areas. For the protection of third parties, the Bill also states that any restrictions placed on the management powers delegated to a management committee and any distribution of duties among management committee members could not be enforced against third parties. The conflict of interests regime that applies to members of boards of directors and management boards would be transposed to apply also to members of management committees.[19]

Other sections of the Bill aim to facilitate the running of management bodies and their decision-making processes. For example, it is suggested that circular resolutions by boards of directors, which are already common practice, should be formally recognized. Directors, like the members of the supervisory boards of *sociétés anonymes*, but unlike the members of management committees, would as a result be able without fear to take unanimous decisions in writing so long as this is allowed in the articles of association.[20] There would be no need to justify the procedure on the grounds of emergency, as is required under Belgian law.

Preceding the recent EU directive on shareholder rights,[21] the Bill would enable shareholders outside the Grand Duchy to take part in the general meetings of Luxembourg companies by videoconference or any other remote method that ensures effective participation. An original presumption is that general meetings of shareholders held using these techniques would be deemed to be held at the company's registered office. The Bill simply requires that at least one shareholder or his proxy is physically present in Luxembourg.[22]

C. *New freedom to choose finance methods*

The most remarkable innovation of the Bill in this area is without any doubt the right of any company with a legal personality of its own to raise finance by issuing ordinary bonds,[23] i.e. by issuing bonds that are not convertible into shares and carry no warrants. To ensure maximum flexibility, the bonds could be registered or bearer and the issue could be private or public. The ability to issue bonds would give companies that are not *sociétés anonymes* new financing options that they will certainly leap at.

15 Proposed new art. 67 para. 4 bis to the 1915 Act.
16 To prevent agiotage.
17 By the abrogation of article 43, para. 1 and of article 79 of the 1915 Act.
18 Proposed new art. 60–1 of the 1915 Act.

19 Proposed new art. 60–2 of the 1915 Act.
20 Amendment of art. 64 (1) proposed under the Bill.
21 Directive of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies 2007/36/EC [2007] OJ L184.
22 Bill: art. II, 43) and 49) amending arts. 67 and 70 of the 10 August 1915 Act.
23 Bill: art. 11ter of the 10 August 1915 Act.

The important position Luxembourg accords to the *société à responsabilité limitée* (private limited company) has led the government to make an additional suggestion that would allow this type of company, like *sociétés anonymes*, to issue convertible bonds and bonds carrying subscription rights, both of which are particularly appreciated when it comes to financing. The change would not be possible however were it not for the closed nature of *sociétés à responsabilité limitée* that allow new partners only if approved by a reinforced majority of existing partners. The new proposal is that anyone wishing to subscribe or acquire a convertible bond or bond carrying a subscription right should be put up immediately for approval. This would give him prior permission to become a partner in the company, after which he could exercise his right of conversion or subscription without hindrance. At the same time, the issue of these bonds would not short-circuit the agreement process.

Another proposal to help *sociétés à responsabilité limitée* is that in future sweat equity contributions would be allowed. While these of course do not create capital and therefore are not a source of financing, they do provide resources of a different kind that can be particularly valuable if the company is micro or medium sized. Following the French model, the government therefore wants to give *sociétés à responsabilité limitée* the right to accept sweat equity so long as this is allowed under their articles of association, which must also set out the acceptance method.

D. Assessment

We expect economic operators will know exactly how to exploit these new freedoms to the full: the increase in the number of available company formats that will follow the introduction of the *société par actions simplifiée*, the new ways of transforming companies and economic interest groups, the resources provided for the finer tuning of shareholder powers, the tighter organization of management committees and the ability of any company with its own legal personality to obtain finance by issuing bonds which, in the case of *sociétés à responsabilité limité*, can even be convertible bonds.

Yet modern company law cannot focus only on contractual freedom, it must also seek to ensure that companies operate properly and to give balanced protection to the various interests involved. It is in this area that Luxembourg company law appears to hang back, paralysed by the fear that too much regulation could prevent business expansion. Indeed before the recent reforms, the only changes undertaken were the almost verbatim transposal of Community directives, strictly limited to the mandatory provisions only, although every option to increase shareholder freedom was carefully picked up. At the same time, Luxembourg legislation did not follow the consecutive reforms introduced in Belgium and France, firstly to prevent dilution of the original liberal spirit of the 1915 Act and secondly because Luxembourg remained largely immune to the economic incidents that were often the trigger for change in other countries. Despite the applause this attitude has usually drawn from economic operators, it does present problems. The 1915 Act is now a dated law that is no longer entirely in step with modern economic reality. Its remoteness from the changes in Belgian law and to a lesser extent from French law also prevent it from using the case law and doctrine of these two systems that are so valuable to interpretation.

The Bill in some way seeks to reduce these weaknesses by increasing the intrinsic protection afforded by Luxembourg company law as well as that which it must provide to company members and third parties.

III. Greater protection

The Bill deals with protection in two ways: firstly, by making the effect of company law (i.e. legal protection) clear and transparent; and secondly, by ensuring a proper balance among the interests at stake. The first way removes a number of muddy areas and the second produces the most interesting of the innovations.

Apart from steps to protect creditors, particularly during restructurings, Luxembourg company law has until now been little interested in the 'agency' problems of majority rule or in the relationship between shareholders and management. Today, the position of minorities and the relative independence of management bodies from partners/owners create problems to which, particularly for listed *sociétés anonymes*, the 1915 Act offers no answers. Recent disputes have highlighted these shortcomings. By proposing new rights for shareholders and increasing management duties and responsibilities, the Bill is aiming to counter the potentially negative effects of excessive liberalism. In order better to protect third parties it also suggests that *sociétés à responsabilité limitée* should be subject to some of the capital protection rules that already apply to *sociétés anonymes*. In future, decisions on which of these two company formats to choose should no longer be based on the loopholes in the *société à responsabilité limitée* format.

A. *New rights and responsibilities*

The biggest problem with the 1915 Act is probably its treatment of minorities and in particular of *société anonyme* minority shareholders.[24] Under the Bill, they would be far better protected. In addition, the concern of shareholders in general that their ownership interests should be properly protected by management acting in a transparent and responsible manner is no longer overlooked, even though the adjustments to the 1915 Act in this respect would be more modest. The Bill proposes to bring *sociétés à responsabilité limitée* in line with *sociétés anonymes* as regards certain provisions on capital protection; this would be in addition to the recommended increase in the protection company law provides to third parties.

1. Majority–minority relations

Under the law as it stands at present, the complex relationship between controlling and non-controlling shareholders is subject to the double democratic principle that each share carries one single vote and that decisions passed by majority vote are binding on all the shareholders. Of course, *parts bénéficiaires* that carry voting rights and non-voting shares can have a (considerable) impact on these rules. Yet the 1915 Act offers little help to minorities seeking to protect themselves against majority shareholders acting primarily in their own sole interests. The theory of 'essential items' or 'accrued entitlement' has had limited success in Luxembourg law.[25] Only decisions that do not increase members' commitments or that change the company's nationality are exempt from the majority rule. Now, in order to facilitate trans-European mobility for companies, the Bill proposes abandoning even the unanimous rule for nationality changes. Minorities who believe they have been treated unfairly by majority shareholders are thus generally forced to rely on abuse of rights as a defence. But in this area actions come up against not only the difficult task of proving that disputed decisions go against the company's interests and have been taken solely in order to benefit the majority shareholders to the detriment of the minority shareholders, but also against the sensitivity of the Luxembourg courts on the matter.[26]

The Bill offers a real remedy here by expanding the scope of the *expertise de gestion* (the expert report minority shareholders can demand in the event of disputes with majority shareholders) and introducing the *action sociale minoritaire* (derivative action). But in some circumstances, differences between the huge majority and small minority of shareholders will have to be resolved: either in the interest of one of the two parties or by liquidating the minority shareholding. New exclusion, sell-out and squeeze-out procedures meet this need.

a. Action sociale minoritaire and expertise de gestion To date the 1915 Act does not allow shareholders acting individually to sue company officers for negligence. This right is reserved to the company alone and is subject to approval by the board of directors and the general meeting of shareholders.[27] The rule is the result of the view that the relationship between directors and the company is similar to a mandate and binds directors to the company alone, not to each shareholder. While logical, the view creates a problem in that liability actions against negligent officers cannot be brought without the agreement of the majority shareholders, who may be reluctant to proceed against people they have themselves appointed. This is probably the reason for the rarity of such actions.

The problem has been overcome in many countries, notably in Belgium and France, by allowing minority shareholders that individually or collectively hold a minimum shareholding to sue officers on the company's behalf if the company itself fails to take such action.

The Bill proposes adopting the same approach by introducing the *action sociale minoritaire* (derivative action).[28] Based primarily on the provisions added to the Belgian companies code in this area, it would allow shareholders and *part bénéficiaire* holders who own at least 1% of the company's voting rights to bring an *action sociale minoritaire*. The holders of non-voting shares could take the same action so long as the negligence imputed to the officer(s) concerned relates to a decision in which they do hold exceptional voting rights, i.e. a decision that might alter the privileges given to compensate for the normal loss of voting rights or one

[24] See as an example the recent decision by the Luxembourg Supreme Court, on 21 February 2008 in *Audiolux et al.* v. *Groupe Bruxelles Lambert, RTL Group, Bertelsmann et al.* (case no. 2456).

[25] I. Corbisier and A. Prum, 'Le droit luxembougeois des sociétés, une conception contractuelle et une personnalité morale non obligatoire', in J.P. Buyle, W. Derijcke, J. Embrechts and I. Verougstraete (eds.), *Bicentenaire du code de commerce*, (Brussels: Larcier, 2007), 139 and 183.

[26] A. Steichen, *Précis de droit des sociétés*, (Luxembourg: Saint-Paul, 2006), n. 335 and quoted case law.

[27] Corbisier and Prum, 'Le droit luxembougeois', (note 25, above), n. 46.

[28] Bill: art. II, 41 introducing arts. 63bis to 63septies to the 10 August 1915 Act.

affecting the substance or survival of the company. As in French law, an *action sociale minoritaire* could be brought not only against directors but also, if the company has a two-tier board structure, against members of the management and/or supervisory board. The procedure would be to appoint a special agent to take charge of the case. To prevent frivolous proceedings, if their action failed, the applicants could be ordered to pay all costs personally plus, if appropriate, compensation to the defendants. However, if they won, all costs reasonably claimed by the applicants and not included in the defendants' costs, would be refunded by the company. These rules should ensure that the *action sociale minoritaire* is as popular as in the countries that have already adopted the system.

Under the present law, the right of shareholders to have management documents examined is very strictly limited: firstly, to shareholders who individually or collectively represent at least one-fifth of the company's capital; secondly, it covers only inspections of the company's books and accounts by auditors appointed by the court; and finally, applications for investigations will be rejected unless there is proof of exceptional circumstances.

This contrasts with the regime that applies in European countries that have already modernized their company law. Based this time on French law, the Bill proposes a total overhaul of the system. The number of people who could request an *expertise de gestion* would be significantly raised to include any member or group of members representing at least 10% of the share capital or 10% of all voting rights. In addition to dropping the threshold by 50%, the Bill also recommends extending the right to all forms of commercial company. Although the proposed threshold is higher than that set under French law, it is the same as that applying to the rights to convene meetings of shareholders, request an item to be placed on the agenda of a meeting of shareholders or, as a result of the Bill, to request an adjournment.

There would be a two-stage procedure when exercising the right. Entitled shareholders could firstly ask the management body for details of one or more transactions or operations by the company or a consolidated subsidiary. If a satisfactory answer is not forthcoming within one month they could then ask the courts to appoint one or more experts to produce a report on the operations in question. The urgent applications judge ordering the report could also order the company to pay the expense and require publication in the manner he decides.[29]

[29] Art. II(76) of the Bill reforming art. 154 of the 10 August 1915 Act.

By making it easier to obtain *expertises de gestion* and extending their scope, the reports themselves become significantly more useful and should encourage the members of commercial companies to make use of a so far very underused facility.

The Bill gives minority shareholders authority by allowing them to sue negligent officers and to demand *expertises de gestion*, thus strengthening their position vis-à-vis the majority shareholders. But these rights will be meaningless unless the minority shareholders, who feel overpowered, can impact on company decisions at least in the medium term. In some cases the dominant position of the majority shareholders will be so all-encompassing that the only solution will be to find some way of enabling the minority shareholder to leave the company.

b. Exclusion, sell-out and squeeze-out Sell-outs and squeeze-outs first appeared in Luxembourg law at the same time as mandatory general offers (MGOs) – in the 19 May 2006 Act transposing directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids. But under this Act such operations can be undertaken only if the shares in a company listed on a regulated market in one or more Member States of the European Union are, as a result of an MGO, highly concentrated in the hands of one or more persons acting together.

The Bill relies on the introduction into Luxembourg of sell-outs and squeeze-outs but proposes firstly to expand their scope and secondly to introduce a parallel general exclusion and sell-out procedure to be applied when there is just cause.

In its opinion on the Bill and MGOs, the *Conseil d'État* said it hoped that sell-outs and squeeze-outs would not be used only when the concentration of power was the result of an MGO. Their hope will become a reality if the Bill is passed, since minority shareholders will then be able to demand sell-out of their holdings and majority shareholders will be able to force minority shareholders to sell them their shares (squeeze-out) as soon as 95% of the voting capital and 95% of the voting rights are directly or indirectly in the hands of a single shareholder. The result will be that minorities will have the right to sell their shares if any single shareholder acquires such a dominant position within the company that their own shares almost cease to be liquid. The only condition for sell-outs of this kind is a threshold that is higher than that for sell-outs following an MGO, when the offeror need have obtained only 90% of the company's capital. At the same time, any shareholder who, without any takeover bid, has obtained a hyper majority may buy out the hyper

minority shareholders. In both sell-outs and squeeze-outs the right to buy or sell applies not only to voting shares but also to non-voting shares and *parts bénéficiaires*. The Bill refers precise procedures and price-setting methods to a future Grand Ducal regulation.

These proposals apply not only to *sociétés anonymes* all or some of whose securities are traded on regulated markets, but also to those whose securities have been delisted. They do not apply however to securities that have never been listed.

For the latter, the Bill suggests an alternative path by introducing a general exclusion and sell-out with just cause system for all SAs.[30] The idea comes directly from Belgium, where the system appears to have been highly successful ever since its introduction. The aim is to ensure that in the event of disputes between shareholders that have a serious impact on their *affectio societatis* there is an alternative to the extreme solution of winding up with just cause that is allowed under article 1871 of the Civil Code. By bringing an exclusion action, the shareholders who hold a substantial part of the powers within the *société anonyme* (in principle at least 30% of the voting rights) can remove a shareholder with whom disagreements are so great that they compromise the proper running of the company. If the court can be convinced that the just cause they allege in support of their application is relevant, it will order the respondent to transfer his securities to the applicant at a price set by the court. The pendant to this solution is the shareholder's right to demand in law that another shareholder be ordered to buy his securities. There would be no threshold on the number of shares or voting rights held but the applicant would have to prove not only that there is just cause for the action (e.g. by demonstrating serious disagreement) but also that this is imputable to the respondent. As in exclusion, the court would set the transfer price and order the respondent to sell his securities.

It is hard to predict how the Luxembourg courts would react to exclusion and sell-out proceedings since the position of the judge in such actions is the complete opposite of the extremely cautious attitude judges normally adopt in disputes between shareholders, particularly where majority interests are concerned. The duty of setting share or other risk security price that would now be imposed on the judge is likely, particularly where unlisted securities are concerned, to cause quite a few palpitations. To make the bringing of such actions easier, articles of association could provide price-setting methods that the court would have to use. They would not be able to rule out either system.

[30] Unlike Belgian law, this would also apply to companies with listed securities. See art. II(58) of the Bill which introduces arts. 98bis to 98quinquies to the 10 August 1915 Act. The system would also apply to *sociétés à responsabilité limitée* under art. II(101) of the Bill which introduces arts. 201bis and 201ter to the 10 August 1915 Act.

2. Shareholder/management relations

a. Increased liability of directors and members of the management board The new right given in the Bill to minority shareholders under certain circumstances to bring liability actions against negligent company officers on behalf of the company does expose officers to greater risk of such action.

The Bill not only increases the scope of the right of action, but it also increases the liability of directors and members of management boards if as a result of major loss the company's net assets fall below half its share capital. Officers would then have to convene a general meeting of shareholders to be held within two months to decide whether the company is still a going concern or whether it should be wound up. If it is decided to remain in business, the report presented by management would have to set out the steps recommended for putting the company back on a firm financial footing.

Under the law as it stands at present, failure to convene a shareholder meeting in due time means directors and members of management boards can be sued for serious negligence. In theory, company officers could be ordered to pay all or part of the loss incurred as a result of the failure to call the shareholder meeting but in practice it is hard to prove sufficient causal link between the loss and the alleged negligence of the company officers.

Referring to the Belgian solution, the Bill would remove the problem by creating a simple presumption of sufficient causation between the loss suffered by the company and the failure to call a shareholder meeting.[31]

Serious liability actions could also be brought against directors and members of management committees for violation of the new accounting standards.

b. Better regulation of conflicts of interest The 1915 Act uses standard prevention methods to regulate situations in which a company officer might put personal interest before that of the company: directors must disclose conflicts of interest to colleagues, they are excluded

[31] Bill: Art. II, 60) reforming art. 100 of the 10 August 1915 Act.

from deliberations on operations and transactions in which the conflict occurs, and they must report the conflict to the meeting of shareholders with a view to *ex-post* approval.

The key change by the Bill in this field is the expansion of the scope of the rule to cover day-to-day management, members of management and supervisory boards and also liquidators.

But the Bill also seeks to make the rules on conflicts of interest more effective.[32] This is achieved by making the rules apply specifically to the direct and indirect interests of the company officer but not to non-pecuniary interests. Other exclusions are current operations entered into under ordinary conditions. The person or body before whom the matter is put will now have to prepare a report on the cause of the conflict, the decision taken and the reason for that decision, along with its impact on company assets. The consequences will also have to be assessed in a report to the shareholders prepared either by the statutory or the internal auditor, depending on circumstances.

If the shareholders do not approve the decision taken by the board of directors on a conflict of interests, they can dismiss the board or bring a liability action against it. This will however not affect the action actually authorized by the board. Under current law, in the event of violation of a required procedure the ability of the company to cancel decisions taken and actions undertaken by the board of directors is unclear.[33] The Bill removes all uncertainty by giving the company the specific right to demand cancellation by the courts if the third party involved in the operation, transaction or decision knew, or ought to have known, that the rules governing conflicts of interests had been violated.

In addition to making conflicts of interest more transparent and introducing more direct procedural sanctions to protect the company, the amendments introduced by the Bill would clarify the scope and operation of this area of law, generally tightening up the 1915 Act.

3. Protection of third parties

The current focus is on the third parties – particularly the creditors – of *sociétés à responsabilité limitée* since although this company format was originally devised as an alternative to the *société anonyme*, it is not covered by the capital protection rules that company law applies to *sociétés anonymes* by virtue of the 2nd Directive.

[32] Bill: New art. 57 of the 1915 Act.
[33] A. Steichen, *Précis de droit des sociétés*, (note 26, above), n. 816.

The limitations of the *société à responsabilité limitée* include no duty to have independent appraisals of contributions in kind, no regulation of its subscription of its own shares or of any third-party financing of own share buy-ins.

The Bill would stop these loopholes.

Contributions in kind to *sociétés à responsabilité limitée* would have to be independently appraised along with the valuation method used, to certify that their value is at least equal to the shares issued as consideration. The exceptions currently applying to *sociétés anonymes* would apply to *sociétés à responsabilité limitée* too.

The rules on *sociétés anonymes* are also the model for the terms under which a *société à responsabilité limitée* could buy in its own shares or finance their purchase through third parties.[34] The aim in both cases would be to prevent buy-ins being used by companies materially to reduce unavailable equity without creditors' knowledge. Not all the same rules would apply to *sociétés à responsabilité limitée* however – e.g. the 10% ceiling, the maximum holding period and the duty to obtain the approval of the general meeting of shareholders.

The legal profession is unlikely to be happy about the extension to *sociétés à responsabilité limitée* of the third-party protection until now afforded only by *sociétés anonymes*. But is it reasonable to allow a choice to be made between two company formats on the basis of the weaknesses in the *société à responsabilité limitée* system? In our view, the need to provide reasonable protection to creditors, who must be able to place at least some trust in the declared capital of a company, justifies the restrictions the Bill would place on shareholder freedom.

B. *New certainties*

The absence of regulation is not necessarily conducive to private initiatives or to contract innovation since the lack of any framework can give rise to considerable uncertainty, particularly in an area as technical as company law, where the ordinary law of obligations does not always provide the reassurances economic operators need as to the legality of the mechanisms they have developed. The lack of a reliable framework can therefore limit contractual freedom.[35]

[34] Bill: new articles 190bis to 190octies of the 10 August 1915 Act.
[35] Bill: grounds, 37.

The legislative intent here is clear: ordinary law and contractual freedom in particular are not always able to provide economic operators with the legal security they require.

Doubts remain about the validity of voting agreements, the legality of contract restrictions on the sale of shares or *parts bénéficiaires* in *sociétés anonymes*, the scope of the ban on the use of leonine clauses and the rights of remaindermen and usufructuaries where stripped rights are concerned, to take only the most significant examples.

The Bill would remove these uncertainties.

Voting agreements between shareholders in a *société anonyme* and partners in a *société à responsabilité limitée* would be valid in principle and invalid only if in breach of the company's interests or of the 1915 Act, or if they rendered the person concerned subject to the decisions of the company's officers and bodies. As a precaution, squeeze-out for just cause is also introduced.

The free negotiation of shares and other securities carrying an entitlement to shares could be limited through the articles of association or by agreement, so long as the limitation is restricted in time and is in the company's interests. Any transfer made in violation of such a clause would be invalid.

The ban on leonine clauses imposed under article 1855 of the Civil Code is now too radical because it undermines schemes set up to enable banks and other contributors of funds temporarily to acquire shares or units so that they can support the restructuring of the issuer. Indeed, both the French and the Belgian courts of cassation have relaxed their positions here and have recognized the legality of these carry methods. The Bill would codify the changes in case law by recognizing the legality of the sale or acquisition of company rights '*that do not aim to harm participation in the profits, or contribution to the losses, of the company*'.[36]

The stripping of ownership rights from company rights with attribution to a remainderman and a usufructuary raises many questions about, in particular: who is the partner and who has the right to vote? who owns the right to dividends and to attributed reserves? who has the right to information? What are the rights of the remainderman and the usufructuary in the event of capital increase or sell-out by the company of its shares, capital depreciation etc? The Bill presents a bold, original general solution for the allocation of the rights of the remainderman and the usufructuary of the company rights, based on the assumption that

[36] New paragraph 3 of article 1855 of the Civil Code as proposed by the Bill.

in principle the remainderman is the partner. Yet it does not ignore the rights of the usufructuary, particularly where quasi usufruct is involved, or the spirit of fair collaboration with which both must exercise their rights.

To illustrate the government's intention of ensuring company law provides more legal protection, we must add to the above some reference to: the abolition of the invalidity of meetings of partners or bond holders; the amendment of the bans on companies subscribing or buying in their own shares or financing the subscription or buy-in of their own shares through third parties; and the differentiation between *sociétés coopératives à responsabilité limitée* (limited cooperative companies) and *sociétés coopératives à responsabilité illimitée* (unlimited cooperative companies). This article does not unfortunately allow us to go beyond a brief description of the general orientations of the Bill.

The additions with which the Bill fills some of the loopholes in the 1915 Act are not the only corrections it would make to clarify the Act and increase the legal protection it affords. The thirty-eight amendments the Act has undergone since it was brought into law have allowed some inconsistencies in wording to slip in and its architecture in general is not particularly harmonious. By looking at the Act as a whole, the Bill deals with these two weaknesses. If only at a marginal level, it does suggest some adjustment to the terminology used.

More ambitiously, the Bill paves the way for the merger of the 1915 Act with the relevant sections of the Civil Code to produce a new Companies Code to remove '*pointless repetitions, inconsistencies and contradictions*' that would delete '*words, expressions and concepts that are no longer used or are old-fashioned*'.[37] It would also reorganize the whole into a more comprehensive and logical body of work, simplifying the process of access and understanding of its rules.

The modernized substance would thus be reflected also in the form.

[37] Bill: grounds, 42.