The voice of corporate governance
in Luxembourg

GETTING OFF BOARD

A Guide to Ending a Company Director's Mandate

CONTENTS

6.2. Do these rights apply in all circumstances or are there circumstances where a Director may not resign?

6.3. Does the legal right to resign at any time, without notice and without stating a reason overrule a contractual agreement to give notice, as often contained in Directors' Service Agreements?

6.4. What happens if all the Directors want to resign at the same time because of a corporate event or an action of which they all disapprove? Are there any restrictions or protocols to be observed?

6.5. In what circumstances should a Director consider resigning?

6.6. Are there circumstances in which a Directors should not resign?

6.7. Having resigned, what are the steps Directors should take to protect themselves from future risks?

6.8. What should a Director seek to include in a Director's service agreement, which can protect his/her position in the event of resignation?

FOREWORD

The objective of "A Guide to Ending a Company Director's Mandate" (the "Guide") is to complement "Getting on Board", ILA's guide for accepting company Directors' mandates, by setting out some of the legal and practical issues related to the ending of mandates.

This Guide makes reference to the main applicable laws and regulations relating to the termination of Directors' mandates and briefly outlines the main principles that a Director should bear in mind when considering to disengage from a mandate and the consequences of it.

Carine Feipel

Former Chair of ILA

Linda Funck

Chair of the ILA Legal & Regulatory Committee

INTRODUCTION

Directors and the Board of Directors play a key role in the prosperity and balance of the company. It is, therefore, necessary and important that non-Executive Directors choose their mandates with great care and are fully aware of the implications of accepting a mandate. The principles of due diligence and the various considerations to be taken into account on accepting a mandate are set out in "Getting on Board" and will not be repeated here.

But once a mandate has been accepted with all due care and diligence, how can a Director disengage from it? What are the various ways in which their mandate can be terminated? What are the procedures and implications of such a step?

Resigning seems an obvious and simple step. But Directors need to be aware of the implications such a step may have for the company. Indeed, it may be met with resistance from the company, its shareholders and other directors, who have concerns about how such an action may be perceived by shareholders, staff, regulators and other stakeholders.

Events that make one Director wish to resign may give rise to similar concerns for other Directors. Indeed, the resignation of a Director may destabilise the balance of the company or even provoke other Directors to resign, potentially leaving the company without any directors, and this poses other problems with the parallel need to act in the corporate interest of the company within the course of a Director's mandate. Any Director intending to resign must take into consideration the difficult balance between the corporate interest of the company and their own interest, paying specific attention that one will not be detrimental to the other.

The Guide was made to provide assistance and advice to members of the Board of Directors , by inter alia:

(i) Providing guidance on how to approach the exit from Directorships;

(ii) Outlining laws and regulations relating to Directors' mandates in Luxembourg;

(iii) Highlighting consequences for the Director and the company.

It is important to pay special attention to the end of a Director's term of office, both for the company and for the Director. As there are many ways to terminate a Director's mandate, proper management of the termination of a Director's mandate is also important. Indeed, each termination scenario has its own issues requiring particular consideration.

Part 1 summarises the legal framework in which Directors' mandates in Luxembourg are set. Part 2 is a Q&A that addresses the kind of practical questions that ILA members typically ask on this subject and attempts to answer them in layman's terms. There is some repetition, but no contradiction, between the two parts.

PART 1

1. Glossary of Terms

When used in this brochure and unless otherwise defined herein, the following defined terms shall have the meaning set out hereafter.

Articles: A company's articles of incorporation or statutes (Statuts)

Board or Board of Directors: The terms „Board" or „Board of Directors", as used in this Guide, refer to that organ of the „Management Body" (see below) of a company which has strategic and supervisory attributions, as distinct from the executive management.

Although this Guide refers mainly to public limited companies (société anonyme), it is intended to embrace all types of companies.

Civil Code: The Code of Luxembourg laws applicable in civil matters

Company Law: The Luxembourg law on commercial companies of 10th August 1915, as amended.

Director: A member of a Board of Directors

General Meeting: The general meeting of the shareholders of a company

Non-Executive Director: A Director who does not represent the interests of any stakeholder of the company, whether shareholder interests, management, staff or customer and thus has no conflict of interest which might impair his/her judgment because he/she is bound by a business, family, or other relationship with the company, its controlling shareholder or the management of either.

Management Body: The term "Management Body" ("organe de direction"), as introduced by European financial legislation applies to the Board as well as to the executive management (administration, gestion et surveillance) of a company. The present guide deals with the Board and its members, as distinct from the executive management.

RBO: The Luxembourg Register of beneficial owners.

RCSL: The Luxembourg Register of commerce and companies.

RESA: Electronic platform for official publication of Companies and Association (Recueil Electronique des Sociétés et Associations).

Société Anonyme ("SA"): Public limited liability company. The SA is managed by a of Directors (Conseil d'Administration, comprised of directors).

Société à responsabilité limitée ("SARL"): Private limited liability company. The SARL is managed by one or more managers (gérants) which may form a board of managers (if provided in the Articles).

2. General Legal Principles and Guidelines for a Director's mandate

2.1. Company Law

Company Law is the primary legislation applicable to corporate law aspects for most entities having their registered office in Luxembourg. Whilst Company Law is the legislation of reference to the corporate law aspects covering inter alia the incorporation, contributions, capital increases, debt, issuances, liquidation, liabilities, governance, shareholder rights, equity investments, mergers, divisions, etc., specific laws (for example relating to Credit Institutions or Investment Funds) will apply in conjunction with Company Law as an additional layer of rules.

Company Law has been thoroughly modernised in 2016, along the principle of "more flexibility by increasing contractual freedom for shareholders and increased security for third parties". The provisions set out in this Guide mainly refer to the rules applicable to a Société Anonyme. Different principles may apply depending on the type of company involved.

2.2. Division of powers between the Board of Directors and the General Meeting

Under Article 441-5 of the Company Law, the Board of Directors of a SA has the power to take any action necessary or useful to realize the corporate object of the company, except for the powers reserved by law or by the Articles to the General Meeting.

Article 450-1 of the Company Law grants significant powers to the General Meeting and provides that it has the widest powers to adopt or ratify any action relating to the company.

The apparent contradiction existing between the powers conferred by Articles 441-5 and 450-1 of the Company Law has been resolved in Luxembourg and Belgian doctrine: because Article 441-5 of the Company Law was inserted therein later than Article 450-1, it must be considered as overriding Article 450-1.

Therefore, the currently recognized division of competencies between the General Meeting and the Board of Directors based on Article 441-5 of the Company Law implies that, in Luxembourg, the General Meeting only has the powers reserved to it by law or the Articles.

Directors of companies with shareholder agreements that reserve additional powers to the General Meeting should take particular note of this. A specific attention must be made in cases where Directors are elected in compliance with shareholders agreements concluded between shareholders. For the avoidance of doubt, even though these rules should ideally be reflected (or at least partially) in the Articles, this might not always be the case.

In all circumstances, upon termination of a Director's mandate, no matter the triggering events, it is important to check if specific provisions of a shareholder agreement govern such a situation and comply with these accordingly.

3. Different scenarii for the termination of a Director's mandate

The mandate of a Director can end in different ways, such as the expiration of the term of their mandate, (cfr point 3.1) their resignation as well as their dismissal by the company.

3.1. Expiry of the term

Pursuant to Company Law, the term of a Director's mandate for a SA is a maximum of six (6) years. However, for a SARL, the appointment is for a definite or indefinite period. Therefore, the termination is automatic upon the expiration of term.

It's important to underline that a re-election is possible (but not automatic) in any case.

3.2. Resignation

Every Director has the right to resign at any time, without notice. As such, no justification is needed for his/her resignation. However, his/her resignation must not cause damage to the company and should, therefore, be done with due care. The removal or resignation of a Director must be filed with the RCSL for publication purposes at the RESA. The Director's resignation will be effective with regard to third parties from its publication in the RCSL.

From a practical point of view, a Director's resignation is valid if the Director notifies the company accordingly, which could be done by email. However, depending on the circumstances and given the potential need to evidence such notification, it remains recommended to send such notification by registered letter with acknowledgment of receipt. This being sent, no approval or any acknowledgment by the company is required.

3.3. Revocation

In a SA, a Director may be dismissed ad nutum. This means that at any time and without any justification, a Director may be dismissed by resolution of a General Meeting duly convened to such effect by simple majority of the votes cast. The effective date of the revocation will also be determined by the General Meeting.

In a SARL, unless otherwise provided for in the Articles, a manager may only be dismissed for legitimate reasons (causes légitimes).

3.4. Other scenarii of termination of a Director's mandate

Other scenarii are possible for the termination of a Director's mandate, including the Director's death, but also the bankruptcy or liquidation of a company.

The Board's (and thus each Director's) mandate automatically terminates upon the appointment of a liquidator. In case of a bankruptcy, the Directors' powers divest upon the appointment of a bankruptcy receiver (le curateur).

4. Consequences for the Director upon termination of his/her mandate

The end of a Director's mandate involves various consequences that are detailed in this section.

A Director needs to weigh the above consideration against his pressing reason to resign. The most careful due diligence will not highlight every fact about a company and decisions taken by the company after a Director has accepted a mandate can change a Director's willingness to continue. A Director's mandate is, however, seen as a serious, long-term commitment to the company and not lightly to be accepted or resigned.

4.1. Administrative measures

Various administrative and regulatory procedures must be carried out, in particular with the RCSL, the RBO and other public and/or regulatory authorities such as the CSSF, the CAA or VAT authority in the context of the termination of a Director's mandate.

4.2. Liability of the Director

Luxembourg Company Law deals with issues related to the responsibility of the Directors in carrying out the mandate granted to them and states that "Directors shall be liable to the company in accordance with general law for the execution of the mandate given to them and for any misconduct in the management of the company's affairs".

Although the Law does not expressly address issues on who should be appointed as a Director, competencies, skills required or time to be committed, Directors' duties and responsibilities shall be based on the general rules set out in the Civil Code regulating execution of an agency mandate (mandat). To this end, Article 1137 of the Civil Code makes reference to the concept of the "bon père de famille" who should be attentive and take reasonable care in carrying out his/her duties. The concept of reasonable care is to be considered in the light of the Director's professional qualification and experience.

In general, the Board of Directors is responsible for the execution of its mandate, but it may delegate various activities to dedicated Board Committees or to the executive management. Case law has established that where such delegation is made, the Board of Directors fulfills its responsibilities by issuing clear formal

instructions to the executive management, ensuring adequate resources are available and monitoring the activity delegated. In that context. It is worth mentioning that where the Board has established or appointed a management committee or a chief executive officer or managing Director, the liability of these persons is substantially the same as those of the Board.

Directors or members of the management committee or a chief executive officer are ultimately responsible for both their actions and their omissions. Liability could arise from breaches of any type of law or regulation.

4.3. Duty of Confidentiality

Company Law imposes an obligation of confidentiality on Directors, even after they have ceased to hold office. They have a duty not to disclose information, the disclosure of which might be prejudicial to the company's interests, except where such disclosure is required or permitted by law, a regulatory provision or is in the public interest.

4.4. Non-competition clause

The law does not place any specific non-competition obligation on a Director. Any such obligation is based on the general rules of contract law. In other words, it may be an obligation incorporated into a Director's service agreement.

In principle, a Director may not prejudice the interests of the company and compete with the company during his/her mandate. Thus, his/her non-competition obligation will cease as soon as the Director's term of office will end[1].

To protect and preserve the interests of the company, a Director's service agreement may contain a non-competition clause for the Director, which may continue to have effect after the end of the Director's term of office. Non-competition clauses set boundaries and conditions on a former Director's ability to work for a competitor upon resignation or termination. The non-competition clause cannot be too general and must specify and limit the geographic location, the period of time it covers and/or specific competitors.

If a non-competition clause is included in a Director's mandate, a Director, whether non-Executive or employed by the company, must comply with his or her obligations under this clause. The period of time specified in the non-competition clause shall start from the mandate's end.

During and after the directorship term, a Director shall not interfere with the company's relationship with, or endeavour to entice away from the company, any person who is an employee or customer of the company or otherwise has a material business relationship with the company.

1. Cass. Belgique, 25 juin 2020, C.18.0144.N.

4.5 Non-sollicitation clause

A non-sollicitation clause ensures the loyalty of customers, employees and former Directors.

If a non-sollicitation clause is included in a Director's mandate, any Director shall comply with his or her obligations under this clause.

4.6. Costs

Company Law provides that extracts of any instrument relating to the appointment or termination of the appointment of Directors of sociétés anonymes, sociétés en commandite par actions, sociétés à responsabilité limitée, sociétés en commandite simple, sociétés en commandite spéciale and civil companies shall be filed and published.

The registration, lodging and publication procedure with the Luxembourg Business Registers requires the payment of a fee. The costs depend on the legal forms of the business and on the type of deed. The costs are laid down in the RCSL table of tariffs.

4.7. Director's reputation and professional integrity

The termination of a Director's mandate could, in some circumstances, jeopardize the reputation or the professional integrity of the resigning Director.

In most circumstances, it would be inappropriate for a Director to resign after carrying out a mandate for a very limited time in a company's Board. Therefore, any Director, in case of resignation, must bear in mind that his/her resignation could be perceived as a sign of a lack of due diligence and professionalism.

5. Consequences for the company upon termination of a Director's mandate

The termination of a Director's mandate has various consequences for the company. Indeed, as detailed above, some administrative and regulatory steps must be taken, such as filing and publishing the termination with public and/or regulatory authorities, namely, RCSL, RBO, RESA, etc.

It is important to emphasise that other consequence may impact the company. For example, there are possible impacts on business licenses (if the Director is the licence holder) and other authorizations (in the case of a regulated entity where the regulator approves Director appointments) as well as the organisation of the new Board members' appointment and ensuring their integration into the Board.

PART 2

6. Q&A

This Q&A attempts to answer the practical questions Directors may have in relation to their situation with particular reference to resigning. The Q&A complements the legal analysis above and tries to put the issues in terms of the questions Directors ask and the type of issues they typically face when they wish to disengage from a mandate.

6.1. What are Directors' rights / duties in relation to resigning?

Company Directors have a legal right to resign at any time without notice and without providing a reason for doing so. This right is mirrored by the Company's equivalent right (in the case of a SA) to remove Directors, through a General Meeting, without notice or justification.

A Director wishing to resign has simply to give notice to the company to its registered office (siège social). For sake of evidence, even if the notification can be made by electronic mail, it is however recommended to notify the decision by registered postal letter. The resignation is effective from the date the letter is recorded as having been sent. There is no need for any approval or acknowledgement on the company's part.

It should also be borne in mind that the maximum duration of a single renewable Board mandate is 6 years. But whether the mandate is for 1 or 6 years, a Director's mandate theoretically ends at the end of the term of the mandate unless renewed, normally at the annual general meeting.

All the Directors cease to hold office on the appointment of a receiver or liquidator.

6.2. Do these rights apply in all circumstances or are there circumstances where a Director may not resign?

The resignation should not harm the company; it should not be abusive or untimely.

Care in this respect is needed to ensure that there is no reputational damage to the company or the Director. This may be especially important in the case of a regulated company.

A Director who has resigned may need to continue to perform some duties until a new Director is appointed, particularly when the company has only a minimum number of Directors (as determined by law or by the company's Articles).

In addition, contractual arrangements between the company and the Director (typically in the form of a Director's Service Agreement) may modify the right to resign by stipulating notice requirements.

It is important to note that the rights of the shareholders of a SA to remove a Director cannot be limited by such contractual arrangements.

6.3. Does the legal right to resign at any time, without notice and without stating a reason overrule a contractual agreement to give notice, as often contained in Directors' Service Agreements?

Typically, Director's Service Agreements seek to protect companies from the impact of sudden resignations of Directors in a manner that could damage the company's reputation or impede its operations, for example by bringing the number of Directors below the statutory minimum.

Such agreements are usually designed with a "normal" situation in mind, to provide for a situation where a Director decides to retire from their position or has capacity issues. These notice requirements seldom consider a different situation where a Director feels an urgent need to dissociate themselves from the company, perhaps because they disagree with a Board decision or have a problem with the company's governance or where the company is in breach of the contract. In such circumstances, a typical 3-month notice period is inappropriate. So, care should be taken to draft the service agreement in a way that avoids resignations with immediate effect where giving notice is appropriate, but allows the Director to quit without notice in "abnormal" circumstances.

6.4. What happens if all the Directors want to resign at the same time because of a corporate event or action of which they all disapprove? Are there any restrictions or protocols to be observed?

The resignation of a majority or all Directors is a real possibility, as non-Executive Directors will tend to be like-minded when it comes to critical matters of governance. For example, if the Directors have unanimously recommended to shareholders that the company is insolvent and should be placed in liquidation, but the shareholder(s) insist on maintaining it as a going concern, that could be a valid reason for all the Directors to resign.

Technically the legal right to resign applies to any or all Directors. The resignation of one Director does not limit the right of another Director to do so.

In practice, the resignation of all or a majority of Directors at the same time creates the risk that the company is harmed by having its decision-making machinery paralysed. This might mean that the Directors have to continue to perform vital functions for the company after they resign and until new Directors are appointed.

6.5. In what circumstances should a Director consider resigning?

6.5.1. Unresponsive shareholder (e.g. Unable to hold a general meeting or obtain a decision about capital erosion/insolvency).

The behaviour of shareholders, particularly if they fail to enact key decisions or statutory duties incumbent on shareholders, may be a prime reason for a Director to resign. Examples might include the failure to approve accounts, appoint auditors or to attend or appoint proxies to general meetings.

6.5.2. Company fails to honour Directors' Service Agreements (e.g. Payment of fees, provision of D&O insurance).

Breach of contract should be covered in the Director's Service Agreement as an event giving the aggrieved party the right to resign with immediate effect.

6.5.3. Company management acts against Board decisions.

In a normal corporate hierarchy, the Board would fire the managers. But in many Luxembourg structures, whilst this remains the theoretical position, the practical reality is that an over-arching international group would not allow the Board of a subsidiary or sponsored fund to fire its management. So, resigning from the Board may be the only reasonable step to take.

6.5.4. Board takes decisions to comply with law or regulations, but company fails to implement.

Similar to 6.5.3., if the Board decides on certain actions and the company does not implement them, or, if the Board makes recommendations to shareholders that are not implemented, these are situations where directors should consider resigning.

6.6. Are there circumstances in which Directors should not resign?

Following is a list of circumstances under which Directors should not resign:

a. Statutory duties incomplete (e.g. annual accounts not approved).

b. Board would be reduced below minimum number (including the possibility that no Directors remain): case law indicates that resigning Directors may have to continue in office until replacements are appointed. However, this leaves unresolved questions about Directors' liability and is therefore a matter on which ILA cannot provide guidance.

c. A major transaction is at a critical point (e.g. Merger or acquisition).

d. Company's reputation could be damaged (e.g. With investors or regulator).

6.7. Once having resigned, what are the steps Directors should take to safeguard themselves from future risks?

a. Check that they are removed from the RCSL.

b. In certain circumstances, it may also be necessary to notify the RBO, if the Directors have been named in the absence of beneficial owners (likely to be the case with an Asbl).

c. It may also be necessary to notify the Administration de l'Enregistrement et Domaines (AED) (VAT

department) and/or the CCSS (Centre Commun de la Sécurité Sociale) if the termination of the mandate implies the termination of the Director's activity.

d. Arrange that the company continues to provide access to Board documents that pertain to the Director's period in office and any Director duties required to be undertaken after the resignation has taken effect. This would include minutes of any meetings held in which the Director has participated or had the right to participate. This may include minutes of shareholder meetings held to consider Board recommendations to which the Director has been party. Directors should bear in mind that such minutes are often produced after a considerable delay.

Particular care needs to be taken where access to Board documents is via an on-line portal and the Director has no locally saved copies, as this may leave them with no evidence of the corporate governance to which they were party.

e. Make sure the company (through a shareholder meeting) provides a discharge (but be aware that the discharge is only valid vis-a-vis the company but is not opposable to third parties).

6.8. What should Directors seek to include in a Director's Service Agreement, which can protect their position in the event of resignation?

a. Clarity on fees (precisely what annual fees cover and do not cover, when they should be billed etc.).

b. Clarity on termination notice requirements.

c. What should be grounds for immediate resignation (regardless of a notice requirement):

i. Breach of contract.

ii. When the Director believes the company is in breach of the law or its own Articles.

iii. When the Director believes the company is not in compliance with its regulatory obligations.

iv. When the Director has voted against a Board resolution and believes his/her position is untenable.

v. When the Director is in fundamental disagreement with the company's governance.

d. D&O insurance obligations of the company

e. Company's undertaking to maintain the Board at a certain size or with a certain number of non-executive or non-Executive Directors (where such undertaking has been expressed in discussion with the Director).

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www.ila.lu | info@ila.lu | +352 26 49 58 5963