Institut Luxembourgeois
des Administrateurs

FAQ Best Practice corporate governance non-regulated financial holdings companies and SPVs

Contents

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General principles

- This document is intended as a brief overview of common questions for directors of non-regulated companies in Luxembourg. It gives an indication of the general framework of relevant company laws and regulations, as well as market practice as at the date of drafting. Different types of vehicles have varying legal and regulatory requirements, not all of which can be covered here. The information provided is not intended as a substitute for legal or tax advice. The term "Company" in this FAQ refers to company, entity or partnership where relevant.
- Whilst reasonable care has been taken in compiling these answers to the Frequently Asked Questions (FAQ), ILA does not accept any responsibility and does not guarantee in any way that they will be appropriate for a particular structure, circumstance or vehicle. **Readers should take their own professional advice in order to clarify which rules and practices apply to their individual circumstances**.
- We agreed that in principle the definition of a company under Luxembourg law is the basis of our subject. This already excludes associations, foundations etc. even though these may in fact be involved in financial activities and their management may benefit from following some procedures for companies.
- The limited or unlimited liability of the shareholders in itself should have no impact on the management of the company.
- Although many answers are generic to all non-regulated entities and legal types of vehicle, **we have mainly focused on S.A. and S.à r.l. with a board of directors** as this is the most common configuration. Although this document reflects general consensus of discussions with various specialists in the non-regulated sphere, there exists a wide range of market practice due to different types of assets held by these entities as well as different type of business.

1915 Companies Law	The Law of 10 August 1915 concerning commercial companies (as amended). This is the primary legislation governing commercial companies.
Articles	The "*statuts*" or articles of incorporation of a company.
Board **or board of directors / managers**	The management body of a Luxembourg company. In this document we use the term board to refer generally to a grouping of directors, however please note that an SCA does not have a board in the legal sense of a collegial body whereas boards in an S.à r.l. may operate as such a board only if the articles of the S.à r.l. are structured accordingly. Whereas in this text reference is made to Directors this may include Managers for a S.à r.l. as the case maybe.
RCSL or **Registrar of Companies**	"*Registre de Commerce et des Sociétés Luxembourg"* is the Registrar of Companies who keeps the register of commerce and companies.
CSSF	The *"Commission de Surveillance du Secteur Financier"* is the supervisory body of the Luxembourg financial sector.

S.A.	*Société Anonyme* (public limited liability company). The "*Conseil d'administration"* is the board of directors of an S.A.
S.à r.l.	*Société à responsabilité limitée* (private limited liability company). An S.à r.l. is managed by one or more managers (*gérants*).
SCA	*Société en commandite par actions* (partnership limited by shares). An SCA is managed by one or more unlimited members or general partners *(associés commandités*).
SCS	*Société en commandite simple* (limited partnership - tax transparent). An SCS is managed by one or more unlimited members or general partners *(associés commandités*).
SOPARFI	*Société de participations financières* (Financial holding company).
Société de gestion de patrimoine familial ("SPF")	The SPF was launched by the Law of 11 May 2007 in order to replace the abolished Holding 1929 regime and is aimed at the private wealth holding and management activities. The object of this vehicle is limited to holding passive investments (acquisition, holding, management and disposal of financial assets excluding any type of commercial activity). Furthermore, the circle of investors is restricted to private individuals (individuals managing their private wealth or private wealth entities acting for one or several individuals, or intermediaries acting on behalf of either of the above).
The Luxembourg law of 22 March 2004 on securitizations (the "Luxembourg Securitization Law")	A securitization is a type of structured financing in which a pool of financial assets (such as loans, mortgages, etc.) is transferred to a special purpose vehicle ("SPV") that then issues equity or debt backed solely by the assets (collateral) transferred and payments derived from those assets. While the benefits of securitization may vary for different issuers and investors, the common advantages of securitization are that it provides a lower cost of capital, enables a company to convert illiquid assets into cash and transfers the risks related to defined assets to third parties.
2011 Law on Business Licence for trading companies	The members of the board or management body of a Luxembourg company.

Directors / Managers	The members of the board or management body of a Luxembourg company. • S.A. - *administrateur* • S.à r.l. - *gérant* • SCA or SCS - *associé commandité*
Transfer Pricing Circulars (« TP Circulars ») TP Circular 164/2 from January 28, 2011 TP Circular 164/2 bis	A group finance company in the sense of Circular L.I.R. 164/2 will be considered to have real substance in Luxembourg if it satisfies all of the requirements as detailed in the circular.
EVCA	The European Private Equity and Venture Capital Association (EVCA) is a member-based, non-profit industry association that was established in 1983 in Brussels. The EVCA represents and promotes the European private equity and venture capital industry.
INREV	European Association for Investors in Non-listed Real Estate Vehicles (INREV) is a platform for the sharing and dissemination of knowledge concerning the European non-listed real estate fund market.

1 Board composition and organisation

1.1	What are the different types of Luxembourg entities?	Luxembourg has 7 main structure types: • Société Anonyme - S.A. • Société à responsabilité limitée - S.à r.l. • Société coopérative organisée comme une S.A. - COOPSA • Société en commandite par actions - SCA • Société en nom collectif - SNC • Société en commandite simple - SCS • Société coopérative - SC The two first ones are the most commonly used company structures in Luxembourg. SOPARFI and SPF may take any of the four first structure types. • A Luxembourg Société Européenne (SE) has to use the company structure of a Société Anonyme - S.A. The Bill of law nº 6471 regarding the transposition of the AIFMD introduces a new special limited partnership (*Société en commandite spéciale*): at the date of issue of this FAQ, the law has not yet been formally adopted.

1.2	Are there specific qualifications required to be a director?	There are no specific qualifications or continuing education requirements for directors of Luxembourg companies. Certain persons may be excluded e.g. if banned following a previous bankruptcy. For some types of business, a business license ("*autorisation d'établissement*") is required as some professions or activities are regulated or are subject to the operations being run by persons who have appropriate professional qualifications and repute. A degree in line with the core business of the company is needed and the relevant qualifications acceptable to the government organisation in charge of issuing the license. Despite the absence of general expertise requirements, directors should have relevant experience and understanding of the business and investments made by the company on whose board they are appointed to allow them to contribute positively as well as to understand their duties, responsibilities and risks and how they should be mitigated. Thus knowledge of the relevant or similar business areas **should** be a **pre-requisite** for the directors/managers. **In line with suitability requirements for regulated entities, best practice should aim at directors meeting acceptable reputation, experience and governance criteria (cf. EBA Guidelines on assessment of the suitability of members of the management body and key function holders, 22 November 2012).** The appointment of independent directors can add diversity to a board via the introduction of desirable skillsets and competencies not represented or insufficiently represented on a board, it can lend additional credibility to a company vis-à-vis its investors, expand the scope of the company's business networks and give experienced outside perspective and guidance. This is particularly important where the company may become listed or change status to a regulated company (see recommendation 3.4. of Ten principles of corporate governance of the Luxembourg Stock Exchange). There should be a commitment from directors/managers to remain up-to-date with changes in e.g. legislation and other factors affecting the business and to remain aware of the challenges faced by the business going forward and how these are changing.

	The key elements are integrity and professional experience The company will assess the appropriateness of a candidate director and existing directors for performing the required duties. The company should ensure that directors also have some knowledge/expertise, as appropriate, in the types of assets and liabilities as well as the operations of the company and for the sector in which it operates. ***Sufficient time for each mandate*** On both the international, EU and national political agendas there is increasing scrutiny of the number of mandates each individual director holds. Although a maximum number of mandates has not been set due to the enormous variances in complexity and time required by different entities, directors should ensure they have sufficient time to fulfil each of their mandates, including, but not limited to meeting attendance, preparation time and other tasks. ***Residence of directors*** There is no general legal requirement for directors to be resident in Luxembourg. However, Luxembourg residence may be desirable for a number of practical reasons (e.g. local representation, expertise etc). This will also allow direct knowledge of local regulations and the local market. The Transfer Pricing Circulars however do require in principle a majority of Luxembourg resident or professionally domiciled directors.

1.3	How many directors are required?	Pursuant to the 1915 Companies Law, unless a higher number is set out in the articles**, a minimum of three directors (*administrateurs*) is usually required** for an S.A. (although a single-member S.A. can be administered by a single director), at least one manager (*gérant*) for a S.à r.l. and at least one general partner being an unlimited member (*associé commandité*) for an SCA. The total number of directors on entities boards varies widely. **A company typically has between three and seven directors.** Three directors/managers would seem to be the minimum for a board to be effective and to ensure an acceptable decision making process. The addition of a greater number of directors/managers should reflect the size and complexity of the company and its activities with both independent and executive directors/managers to ensure an appropriate balance of skills and experience at board level. The board needs to be large enough to provide a mixture of skills, experience and to ensure an adequate level of individual contribution to discussion and debate and communication in general. Research indicates that too large boards are unmanageable and lose effectiveness. Ideally, a **board should be balanced in terms of experience, diversity (including gender) and expertise**.
1.4	Do we need a chairperson, a company secretary or any other official appointee of the board?	**Chairperson: S.As must mandatorily appoint a permanent chairperson. Other company forms may or may not have a chairperson in accordance with the terms of the articles of company.** **Company secretary**: a company secretary may be appointed, although not legally required. A company secretary can add value by acting as the main point of contact for the board, taking minutes of meetings and ensuring in support of the chair (if any) that the board is well run and coordinated. If no official company secretary to the board is nominated by the board, then an employee of the company or an outside service provider generally takes this role. In practice it is important to have **a support person who assists with the administration of the board, including taking minutes.** **Scrutineer: the board may also enlist a scrutineer whose role is to assist in the voting process. A scrutineer collects, verify and counts votes cast at a shareholder meeting. Scrutineers are formally appointed by the shareholder meeting, in particular for physical meetings of SAs.**

1.5	Do we need a compliance officer?	The term officer is *per se* not a standing term under Luxembourg corporate law and practice. It is the responsibility of the board to define if a compliance officer is required and to define the areas to be complied with, such as local regulation, tax regulation, accounting regulation, VAT, fraud, corruption and moreover, the requirements can be defined according to the business relevance and the size of the company, i.e. small, medium and large.
1.6	Do we need a risk officer?	The term officer is *per se* not a standing term under Luxembourg corporate law and practice. It is the responsibility of the board to define if a risk officer is required and to define the areas to be complied with, such as operational risks. The risks and the coverage of risks are sector and business specific and need to be addressed accordingly. The requirements may vary according to the size of the company, i.e. small, medium and large.
1.7	Do we need independent directors?	There is no legal requirement to appoint an independent director, however an increasing number of companies are appointing independent directors. Unlike certain jurisdictions, there is **no legal or regulatory definition of an independent director**. Employees of company service providers do not fulfil the criteria for being an independent director as such employees may have conflicts of interest. Recommendation 3.5. of the Ten Principles of Corporate Governance of the Luxembourg Stock Exchange gives some guidance with regard to a definition of independence. The Ten Principles of Corporate Governance apply to Luxembourg companies listed on a Luxembourg regulated market but they can also be referred to as a useful source for determining best practice of other Luxembourg companies. Note: In relation to Luxembourg companies listed on a Luxembourg regulated market, the Ten Principles of Corporate Governance of the Luxembourg Stock Exchange recommends the appointment of independent directors in listed companies and gives some guidance (see Luxembourg Stock Exchange's definition of independence in Recommendation 3.4.). ALFI Code of Conduct gives also recommendation regarding independence of Directors in its recommendation II.2 :*"Consideration should be given to the inclusion in the Board of one or more members that are, in the opinion of the Board, independent."*

1.8	Are there diversity requirements (e.g. age, sex)?	There are no diversity requirements in Luxembourg law. However boards should consider **a balanced composition in terms of diversity**. In relation to listed companies, the Ten Principles of Corporate Governance of the Luxembourg Stock Exchange recommend, for example, an appropriate representation of both genders and account to be taken of the specific features of the company and its activities, and particularly the various business lines of the company and their geographic diversity (see Luxembourg Stock Exchange's definition of independence in Recommendation 3.1.). The European Commission has proposed legislation with the objective of a 40% presence by gender among non-executive directors of listed companies. It does not apply to unlisted companies nor to small and medium-sized listed entities defined as companies with less than 250 employees and a global turnover not exceeding EUR 5 million.
1.9	Must one be a shareholder to become a director?	There is no legal obligation for a director to hold shares in the company of which they are a director. There is also no prohibition.
1.10	How are directors appointed and removed?	*Appointment:* • By the shareholders. The director is appointed by shareholder resolution in accordance with the articles of association. In an S.A. the appointment would be made in general meeting; • A replacement director may be co-opted by the remaining directors if there is a vacancy on the board of an SA between general meetings, unless restricted by the articles. The shareholders must ratify this appointment at the next general meeting; *Removal:* • Resignation of the director • Non re-election of the director upon expiration of the term of the mandate • Removal of the director by vote of the shareholders in general meeting • Dissolution or insolvency of the company on whose board the directors serves • Death or incapacity of the director • Personal bankruptcy of the director

		Publication: • Any changes to the board must be notified to the Registrar of Companies or RCSL “Registre de Commerce et des Sociétés Luxembourg” within one month, which will publish these in the Mémorial C (i.e. the Official Gazette).
1.11	Accepting a mandate - due diligence	***Due diligence by the candidate director*** The appointment as a director is not only about companies selecting and carrying out due diligence on candidates; it applies equally to candidates selecting their mandates. Directors are encouraged to conduct and record their due diligence to ensure they are familiar and comfortable with the structures and affiliates with which they will be associated.
1.12	Is it usual to receive an appointment letter or contract?	**Appointment letters and contracts are increasingly seen in practice** and are strongly recommended as they can be useful for clarifying certain issues relating to duties, remuneration, insurance, term of appointment and certain rights after termination of the appointment. Sometimes such a letter/contract will also give the right to the director to inspect documents at the registered office after termination of the appointment.

1.13	Who pays the directors fees and decides on their level?	There is a wide range in remuneration levels and structures, depending on the type of mandate and the responsibilities of the directors. In practice the company typically negotiates the level of remuneration, and the shareholders vote to approve it at the next general meeting, usually at the meeting which appoints the director or extends the term of the mandate. Directors should also be entitled to claim payment of reasonable expenses, which should be agreed with the company. Fees are normally paid by the company.
1.14	Will director's fees be published?	There are no general legal or regulatory requirements to list or publish detailed remuneration amounts although there is a general disclosure in annual accounts.
1.15	What taxes are payable in Luxembourg on director's fees?	If paid by the company and received by the directors as an individual, director's fees (known as *tantièmes*) will be subject to a **special withholding tax of 20%**. Depending on the director's personal circumstances it may be possible to set this off against other Luxembourg or foreign income tax liabilities. In any event, a tax adviser should be consulted. If the Luxembourg company puts a director at the disposal of another Luxembourg company, the fees paid for the supply/put at disposal a director to the latter may be subject to VAT. If invoiced via a private company, they will also be subject to corporate income tax.

2 The role of a director

2.1 What is the role of a director?	**The board is generally entitled to do all things deemed necessary to achieve the corporate objects ***except for*** those actions that have been expressly reserved by the 1915 Companies Law or the articles for decision by the shareholders** (*1915 Companies Law, Art.53, al.1*), or the shareholders agreements. Accordingly, **the board is in charge of all administration and management matters** of the business of the company **and collectively represents the company towards third parties.** Examples of items the board would be involved in include: • Approving the strategy and business plan of the company; • Approving material transactions including, for example, the acquisition or the disposal of assets; • Deciding on important matters of policy, for example, accounting and valuation principles to be applied by the company; • Holding regular meetings plus ad hoc meetings where required; • Approving the annual report for submission to the approval of the shareholders of the company and meeting accounting deadlines; • Convening the general meeting of shareholders; • Proposing and declaring interim dividends (the declaration of dividends being a reserved matter for the shareholders); • Signing audit letters e.g. engagement letters and representation letters; • Appointing service providers and signing other material agreements; • Ensuring compliance with regards to accounting and tax deadlines.

	Directors must **ensure the company applies the standard of care and diligence of a reasonable person in that (or a similar) position and circumstances**. Directors should ensure they **regularly receive detailed reports (e.g. management accounts)** from agents and advisers of the company to enable proper consideration of all decisions. They should monitor and supervise and should, if they cannot see to this themselves, put adequate processes in place which allow the directors to monitor and supervise the relevant business matters. They should also **request further information** when required. The directors always consider the Company's corporate object, (ii) act in the Company's best corporate interest and (iii) within the Company's powers

2.2	Can a director delegate his/her functions?	• **What can be delegated?** The 1915 Companies Law allows the board to delegate day-to-day management of a company to one or more directors or managers or to delegate specific tasks. Material business decisions may not be delegated and it is important to note that ultimate responsibility remains with the board. • **To whom can it be delegated**? The 1915 Companies Law does not specifically provide for the board of managers of a private limited liability company to delegate the day-to-day management and the representation of the company in relation to such day-to-day management, unlike in the case of an SA. Special powers may be granted to any member of the board of managers of a company. The scope of such special powers should however be restricted to certain operations or special types of operations in which the company is involved, in order to avoid that such a delegation be interpreted as a complete and general delegation of the management of the company. The board of managers will remain liable for the management of the company towards the shareholder(s) of the Company, even though it has delegated certain of its powers. Accordingly, it is strongly recommended the board of managers control the assignments of the manager(s) to whom special powers have been granted on a regular basis and ratify acts passed on behalf of the company by such manager(s). Delegation may be implemented inside the organisation or, more problematically (and requiring most often a greater degree of vigilance), outsourced to a third party provider. Boards must act as a prudent person would in similar circumstances. This includes performing due diligence on service providers before their appointment as well as on-going monitoring during the relationship, such as thorough questions, visits, periodic due diligence, etc. • **Take care when delegating** Internal delegation - distinct responsibilities may be attributed to different persons, however restrictions on delegation are not enforceable towards third parties even if they have been published. The board should ideally have delegation of authority guidelines, including: • Date and duration of the delegation; • Circumstances of the delegation (e.g. why? Approved at board meeting dated xx, etc.);

- What has been delegated to whom? It is best practice to set out in detail the powers, roles and responsibilities of each delegate - what areas, what limits, must they act as a committee, jointly or can each act alone?
- Reporting obligations - set out what reporting is expected in return, including what reporting is expected from delegates at board meetings, in between meetings and following any significant event;
- Any other relevant details regarding the delegation.

Third party arrangements - outsourcing - In addition to the above, it is recommended that all outsourcing arrangements are set out in a legal agreement. Such agreement should clearly set out:

- Roles and responsibilities of the delegates, including their reporting obligations (including obligations to disclose and seek approval of all sub-delegations);
- Duties are either to achieve certain results or, depending on the services, to act in accordance with the due skills and care of a normal businessman in the pursuit of the objectives.
- Access protocols to enable due diligence exercises;
- The board has unrestricted access to information;
- The delegate should not retain documents and has the obligation to return them to the board at the end of the outsourcing job, unless agreed otherwise.
- Confidentiality;
- Non-compete;
- Detailed operating procedures and/or service level agreements;
- A break-up clause;
- AIFM Directive In relation to certain structures which are part of alternative investments, certain items will be required to be outsourced, such as valuation to an external valuer.

	• **On-going monitoring** The board must retain control over delegated duties e.g. via regular upward reporting to the board and ensuring that delegated tasks are managed in accordance with applicable law and regulations, the articles, the contracts and are in the best interests of the company. Periodic due diligence regarding outsourced responsibilities and performance reviews should also be undertaken. This requirement may extend beyond the company's direct service providers to sub-service providers (e.g. prime brokers or sub-custodians who may hold assets). Although there may be issues in gaining access to sub-providers both initially and on an on-going basis for monitoring, a certain amount of effort should be expended for assurance that indirect service providers can be relied on. Where possible, agreements should contain provisions allowing access to sub-providers.

2.3	What sort of internal controls should the board have?	**Internal board policies and guidelines are recommended**. Even though not required by law and regulation, implementation of internal policies and guidelines is recommended, as, no or at best, minimum guidelines are set out in the articles and/or the 1915 Companies Law (e.g. quorum, participating by telephone etc.). The board should maintain a **sound system of internal control and compliance** designed to safeguard shareholders' investment and the company's assets. **The board should develop over time its own set of internal functioning procedures and guidelines.** The board should ensure the establishment of effective systems and controls for compliance with applicable requirements and standards under relevant laws and regulations. Best practice is to compile all of these in a «**Procedures manual**». • A procedures manual would be considered best practice for all entities. It should be reviewed at least annually and as often as necessary and updated as required to cover all controls, including financial, operational and compliance controls and risk management. More detail on the functioning of the board is given in section 3. More detail on board policies is given in section 2.4. below.
2.4	Our group already has board policy and corporate governance guidelines for entities outside of Luxembourg. Can the board simply apply these?	As long as they do not conflict with Luxembourg laws and regulations a director/board may, *with the necessary changes,* make use of other guidelines. The board should still develop specific board guidelines for Luxembourg entities to help avoid breaches of Luxembourg laws or regulations. To complement and fill-in the legally required policies, guidance is often sought (and may even be adopted into board policy and procedures) from other relevant, recognised sources, such as professional guidelines in other countries. Good places to start include: • Local directors' institutes e.g. the Luxembourg Institute of Directors (ILA); • Overseas trade associations Specialist industry bodies, such as the European Venture Capital Association (EVCA), the European Association for Investors in Non-listed Real Estate Vehicles (INREV) or Alternative Investment Management Association (AIMA); • Standards boards such as the Accounting Standards Board, and the UK Financial Reporting Council. A more detailed list of useful links is given in Section 6. below. As a result of the «8th Audit Directive» (EU Directive 2006/46/EC), **listed entities must adopt a corporate governance code.** Adoption of such a code by unlisted entities depends on the individual circumstances of each company.

3 Functioning of the board

3.1	Are there rules on how the board should function?	The 1915 Companies Law sets out how the management bodies should operate. **The articles and the shareholders agreements usually set out the basic rules regarding meetings of the board** (convening, voting majorities etc.). More detailed internal rules regarding the board's functioning and deliberations are recommended - see Section 2 above.
3.2	When or how often does a board meeting need to be held?	The board should **meet at the registered offices of the company as often as is necessary for the company to be properly managed** and to enable the board to exercise its powers. As a result, the frequency of board meetings will differ in accordance with the specific needs of the company, its current business needs and conditions. A minimum of four board meetings annually is generally held to constitute best practice. The annual accounts must be discussed and approved at board level. Specific board committees may be created to deliberate on specific ad hoc issues. They generally function as advisory committees of the board doing preparatory work and where the board takes the formal decisions.
3.3	How is a board meeting called?	This is usually set out in the articles. The board should ensure the convening notice always contains a **formal and specific agenda** of all matters the board will review, discuss and approve with **sufficient supporting documentation** made available in advance so that the board members can assess the agenda items with the underlying documents and facts in their overall context ahead of the actual board meeting. Board members should be treated equally and have access to the same information and documentation. A sample agenda can be found in the appendix.

3.4	What information can a director expect to receive?	**The board should be supplied in a timely manner (If possible, at least five working days in advance. However, subject to urgent matters, which require immediate attention, this period can be shortened as there is no legal requirement as to the minimum number of days) with information in a form and of a quality appropriate to enable it to discharge its duties.** Each director is entitled to receive copies of all information and documents transmitted to the board. Directors should normally review all company documents. However, the board may have delegated certain functions, and only request a list of related agreements with one or more sample full agreements attached for review. **Luxembourg has strict confidentiality laws**, particularly in the financial sector, but also set out as a general principle of Luxembourg company law. Directors must take care to ensure that no information received is divulged to third parties or used for any other purposes. The disclosure of information to shareholders by a director is a sensitive issue and merits, depending on the circumstances, caution. Under specific circumstances sensitive information should not be disclosed to shareholders. **Examples of documents likely to be supplied to the board**, and which the board should have the opportunity to comment on, include: • Review of corporate documents (extract from the Registrar of Companies); • Review and approval of the last minutes; • Review and approval of budgets and business plans; • Review and approval of the management accounts; • Review and approval of financial statements (once per year); • Status of Luxembourg tax & VAT compliance; • Review of company activities / investment portfolio; • Review of delegated activities; • Review of bank mandates and signature lists; • Review of large payments; • Review of large liabilities (in particular if they are outside the ordinary course of business) • Cash flow forecast (12 months); • Legal compliance; • New agreements (if applicable);

		• Related party transactions (if applicable); • Accounting treatment changes (if applicable); • On-going supervision - between scheduled board meetings; – Options include ad hoc telephone meetings, circular resolutions (i.e. resolutions in writing) or delegation to (sub-)committees and/or service providers/directors; • It is important to remember, however, that whilst a board may delegate certain activities and decisions, it cannot avoid responsibility for those decisions. Any significant decisions taken should be reported to the board in writing at the next scheduled meeting so that they can be ratified.
3.5	If a director wants more information – can they demand it?	If a director does not feel that information provided by the relevant parties is enough, they should make further enquiries and requests from appropriate parties (typically the chairperson the CEO and other executives). It is acceptable for the board and even, under specific circumstances, certain board members, in the execution of its duties, to take independent legal advice at the company's expense.
3.6	Can a director still access information after termination of their appointment?	It is recommended that this is dealt with in an appointment letter - see above section.
3.7	Do meetings need to be held in Luxembourg?	Not pursuant to Luxembourg law. Often there are reasons making it desirable to hold the majority of board meetings in Luxembourg. Luxembourg companies should have their domicile, i.e. central administration, in Luxembourg.
3.8	Can a director attend by proxy, telephone or videoconference?	Usually the articles expressly allow this, however, they should be checked. The right of representation (by proxy) is possible provided that the articles do not prohibit it (the right to be represented is implicit). If the articles do not expressly allow board attendance by telephone or videoconference is questionable. *Proxies* - the articles usually also set out that a director may represent one or more of their fellow directors at a board meeting. A proxy (or power of attorney) cannot be granted to a non-director for board attendance. There are no substitute or delegate directors under Luxembourg law. *Telephone attendance* - such meetings tend not to be as effective as physical meetings given that there is typically less interactivity between board members. Conference calls are generally initiated from the board meeting in Luxembourg. They are deemed to be held at the registered office of the company (see article 64 bis (3) of the 1915 Companies Law in respect of an SA).

3.9	Can a director bring an adviser to meetings?	A board meeting is a private meeting - a director may only invite a third party (such as service providers or advisers) to attend a board meeting (i) for information and advisory purposes, and (ii) if all the directors present at that meeting agree to this. The third party cannot vote and may only comment if invited to do so.
3.10	What is the quorum for meetings and voting?	In the absence of a special rule or a higher number set out in the articles the usual rules in respect of an S.A. are: • *Quorum* - at least half of the directors must be present or represented. • *Votes* - a decision is passed if a majority of those directors present or represented vote in favour. • *Chair's casting vote* - unless there is a provision to the contrary in the articles, where there are equal votes the chair gets a casting vote (see Article 64 bis (2) of the 1915 Companies Law). • *Circular resolutions* (i.e. resolutions in writing) –need to be taken unanimously (all directors must sign). Circular resolutions cannot systematically replace face-to-face meetings.

3.11	Must there be a chairperson?	The 1915 Companies Law requires the board of an S.A. (see Article 64 bis of the 1915 Companies Law) to elect a chairperson from among the directors, who (in the absence of anything to the contrary in the articles) has a casting vote. The 1915 Companies Law does not, however, otherwise detail the chairperson's functions or powers. There are no legal provisions in respect of chairs that apply to a S.à r.l.
3.12	Can a director still vote if they have a conflict of interest?	The 1915 Companies Law (Article 57) states that directors cannot vote on decisions where they have a conflict of interest to that of the company unless these are in the ordinary course of business. Generally, a director will still be able to vote on decisions taken in the ordinary course of business and under normal conditions. The articles of the company should be checked in relation to the type of decision to be made. In cases where there is a *real/potential conflict of interest*, the director of an S.A. must (1) inform the board, (2) abstain from participating at the deliberation, (3) abstain from voting, (4) ensure the conflict is mentioned in the minutes and the board must (4) inform the next general meeting of shareholders of the conflict and the resolution passed in respect of the matter where the director was conflicted before any other business is voted by the shareholders at the meeting. Although the 1915 Companies Law does not mention specific provisions for Sàrl, ILA considers that the same principles should be applicable. cf: ILA Code of Conduct.
3.13	Are there limitations on what the board can decide?	The board is generally entitled to do all things deemed necessary to achieve the corporate objects except for those actions that have been expressly reserved by law or the articles for decision by the shareholders. The articles and the shareholders agreements may contain restrictions.

3.14	Should the board keep minutes?	Yes - **board meetings should always be evidenced by minutes.** • *Significant legal status* - minutes can and are often used in litigation and disclosed in court, to regulators and to auditors. They are to serve as evidence of genuine discussion and decision-making, and as *prima facie* evidence that directors are doing their job (properly). They are a record of the decisions taken. • *Reviewed & commented on before signing* - After a meeting the minutes should once drafted be circulated to all directors for review and comments, and then for the final minutes to be signed by such persons as mentioned in the articles. It is best practice for the minutes to be drafted shortly (within a couple of days) after a board meeting so that there are good recollections of the directors in respect of the facts and the resolutions passed at the meeting. In quite a number of companies minutes of the previous board meeting are approved and signed only at the subsequent board meeting • *Detail* - It is good practice for each separate item/decision to be dealt with in a separate point. It is also good practice to set out a table of action points to be followed up at the beginning of the next meeting (e.g. action, when arisen, due by, who is responsible - see Appendix A). • *Board secretary* - a board may appoint a corporate secretary or equivalent to take minutes (see section 1.4. above)
3.15	Must there be performance evaluations of the board?	There is no legal requirement for performance evaluations of the board. As a result performance evaluations are not yet widely carried out for Luxembourg company boards, although this correspond to best international corporate governance practice. Sample questionnaires may be requested from the ILA Secretariat.
3.16	What are the signatory powers of the board and of directors generally?	**The board of a S.A. or S.à r.l. is a collegial body**, the general principle being that individual members have no powers to bind the company. The **articles usually set out the signature and representation powers** of directors as well as whether such powers are sole or joint. The board should pay attention to its own **delegation guidelines** and keep track of persons to whom it has delegated representation powers.

3.17	What reporting or communication obligations exist for directors?	In addition to the company-level reporting required, directors also have individual responsibilities. It is impossible to list all possibilities, however some examples of reporting or communication obligations may include: • Directors must report to the shareholders at least annually plus ad hoc reporting following a significant event. • There are various reporting obligations in the 1915 Companies Law regarding items, which must be published at the Registrar of Companies, and/or in the Mémorial C. Directors should also check their board's guidelines or policies and ideally incorporate any reporting obligations into those guidelines.
3.18	What are Board committees? If the committee makes a recommendation, does this mean the rest of the board does not need to consider the matter further?	**Board committees are simply sub-sets of the board** - certain tasks may be delegated for efficiency reasons. Their purpose and functioning are usually contained in formal terms of reference defined by board decision, although these could also be in the Articles. Board committees may include an appointment & remuneration committee, audit committee, valuation committee and/or investment committee. There may also be *ad hoc* committees to deal with a specific circumstance or issue. Note, however, that even if a board committee has made a recommendation to the board regarding a particular matter, **each director must properly consider each proposal before voting on the matter**.

4 Liabilities

4.1	What is the practical exposure stemming from a director's management duties and responsibilities?	Until recently, few directors had been brought to court in Luxembourg as most cases were dealt with in out of court settlements. As a result, there is little case law in this matter. It may be important to consult a lawyer to receive tailored legal advice. In the past, focus has been more on mismanagement issues. More recently, regulatory fines have become common for late and incomplete reporting.
4.2	As a director, what types of liability are there?	Directors are ultimately responsible both for their actions and their omissions. Liability could arise from breaches of any type of law or regulation - e.g. the 1915 Companies Law, accounting rules, tax laws, insolvency regulations, employment law, environmental regulations, health and safety, planning regulations etc…and trigger in particular civil liability, criminal liability, tax liability and liability towards the relevant authorities. **The 1915 Companies Law governs the general duties and responsibilities of directors and it is this law, which also sets out the main liabilities of directors.** Directors face two main types of liability - **contractual liability towards the company** and **liability in tort towards the company and third parties**. Because of divergent legal entities and structures of entities, plus self-managed structures as well as those using management companies, there may be differing liabilities applicable. Directors should always seek independent legal advice. Some of the main liabilities include: • *Individual (or collective) contractual liability to the company for **mismanagement** (art.59, al.1)*. The directors must act as a normally prudent and diligent person in the same position would. Any director found liable would have to indemnify the company for foreseeable loss (except in cases of fraud). **Appropriate risk management should be set up to ensure regular review of risks**. Examples could include errors in the annual reports or incorrect valuations. • *Joint liability to the company or third parties for **breaches of the 1915 Companies Law or the articles**(art.59, al.2).* Liability is only incurred as a result of wrongdoing, whether through action or negligence. An example would be acting in breach of the company's objects.

- *Quasi tortious liability (individual liability of that director)* - this principle of "*responsibilité aquilienne*" applies generally if a person commits a fault (whether by act or omission) that causes a loss to the company or a third party who has dealt with the company. The party bringing the action must prove the wrongdoing of the director(s) has caused them specific and personal loss, distinct from that suffered by the company.
- *Tax liability:* the manager of a Sàrl or the executive director of a S.A. (the other directors are not jointly liable) must meet the tax obligations of the company and notably carry out the payment of taxes due by the company. However, the liability is committed only in case of fault of the manager/executive director (the non payment of taxes must not be considered ipso facto as a fault).
- *Certain breaches of the 1915 Companies Law may also incur criminal liability for directors* (Art. 162 to 173). Most often these are limited to fraudulent acts on the part of the directors, but not always. Examples include:
  - Not filing accounts within the statutory deadline;
  - Not convening a shareholders meeting after a request made by 10% of shareholders;
  - For fraudulent reasons, not publishing the accounts or making misrepresentations in accounts;
  - Issuing shares without receiving payment for them;
  - Improper use of corporate assets.
- *Money laundering compliance.*
- *Insolvency liabilities.*
- *Agency liability for delegates of the management body:*
  - Delegates are liable vis-à-vis the management body;
  - Delegates are liable vis-à-vis third parties for quasi-tortious liability;
- The management body has an obligation to monitor its delegates and may also be liable vis-à-vis the company for acts/omissions by delegates if not authorised to delegate or if the person appointed was incompetent. If so, it may also take action against the delegate.

4.3	Practical steps to limit liability	• Consider meeting regularly throughout the year and attend all board meetings when possible; • Document all decisions (ensure there is evidence that issues have been properly considered). Consider also whether the discussions and the basis for the decision require documenting or not - although minutes are usually records of decisions taken there can be situations where it will be important to also summarize the discussion or note a dissenting vote; • Think about how each document may look if viewed critically, in particular when read out later in a court. Where appropriate, documents should be reviewed by legal counsel and professional advice should be sought pro-actively and at an early stage, whenever required; • Understand and document what the service providers think their roles and responsibilities are, ensure there are no gaps and know who is doing what and who is responsible for what. Overlaps may also be the cause of confusion and should be avoided. You may wish to consider appointing a company secretary to assist with the management and coordination of the tasks.
4.4	What if a director voted against a decision - could he still be held responsible?	In principle, yes. Ultimately this is for the court to decide. Directors should ensure the minutes of the meeting expressly set out their objections to certain matters or even to consider resigning or «*whistle blowing*». As a general rule, directors should actively disassociate themselves from decisions and board actions, which they do not support. Independent legal advice should be obtained. Where, for example, there has been a breach of the 1915 Companies Law or of the articles, a director can avoid liability only if there is no fault on their part and they denounce the actions to the first meeting of shareholders that follows their becoming aware of the infraction(s) (art. 59).
4.5	Does the designated person of a company that is a corporate director have a different liability?	A representative of a corporate company has the same rights, duties and liabilities as if appointed a director directly in his/her own name. The company represented will, however, be jointly liable with the director. Representing a company may lead to certain conflicts of interest.

4.6	What happens if the company gets into significant difficulties?	Significant issues could include, for example, the fact that the board can no longer function, if the company has become insolvent. The directors will need to take actions as to call a shareholders meeting or to file for insolvency (Art. 437 of the *Code de Commerce*). The filing for insolvency needs to occur within 30 days of the company having become insolvent i.e. where the company was no longer able to pay its liabilities when they fell due and where the company ceased to be creditworthy. Although the general liability rules apply, continuing to trade where the company has ceased to meet its financial obligations will likely be judged as faulty behaviour by those directors. In addition, article 495-1 of the *Code de Commerce* provides that where a director's gross negligence has caused or contributed to the company's insolvency, the court may decide that the director(s) must bear part of the debts of the insolvency from their personal estate. Eventually the company may be declared insolvent or be placed in mandatory liquidation. Depending on the circumstances, there will be a insolvency receiver or, as the case may be, court appointed liquidator and the courts seeking to apportion blame and claiming damages from those involved.

5 Indemnities and insurance

5.1	In my home country, directors get an "indemnity/*hold harmless*" agreement? Can they ask the Luxembourg company for the same?	An indemnity can be asked for, however, it is not automatic. Indemnities cannot cover gross negligence, criminal liabilities or fraud. In case where the company may be insolvent an indemnity may be of limited value. Therefore, it may be important that there is adequate D&O insurance cover in place.
5.2	What is the "annual discharge"?	Each year the shareholders in general meeting may, by special vote, grant "***discharge***" to the directors. This discharge has the effect of liberating the directors from contractual liability towards the company (but not towards third parties) for the financial period for which the accounts are being approved (i.e. the previous year). However, this is conditional on the accounts containing no omission or false information regarding the real situation of the company. In certain cases (e.g. breaches of law or the articles), these facts also need to have been expressly set out in the notice convening the shareholders meeting. If there is no accusation of fault, it is customary for a director to request a "discharge" when resigning or being removed as a director.
5.3	Auditors' letters of representation and engagement letters with other service providers	*Auditors' letter of representation* Before signing the audit report, **the auditors will seek a letter of representation from the company's directors**. The exact contents will vary depending on the nature of the company, however it will typically cover items such as (i) an acknowledgement of responsibilities, including in respect of internal controls and for assessing fraud risk, (ii) that all appropriate books and records have been made available, (iii) that all material transactions have been properly recorded, (iv) that investments and other financial instruments have been valued in accordance with law, (v) that all related party transactions and all contingent liabilities have been disclosed to the auditors. It is important for the directors to review carefully not only the accounts, but also the contents and context of each auditors' letter. The directors increasingly request **«*representation comfort letters*» from the company and other service providers** (where applicable) as to the delegated areas covered. The service providers should review the accounts and be asked to provide directors with details of any significant matter arising from that

	financial period and respond to any queries the directors may have. This needs to be built into the timetable for the approval of the accounts to ensure that the directors receive the necessary comfort and have sufficient time to carry out their reviews effectively. In the context of a holding company, the directors should request an internal representation letter from the subsidiaries to ensure that no elements should be taken into account in the accounts of the holding, nor should be included in the holding's representation letter. *Letters of engagement with auditors and other service providers* Always read proposed letters of engagement carefully. Question the provisions (what is said to be standard often is not). For example, certain specific limitations of liabilities may not be in the best interests of the company and its shareholders for the directors to accept.

5.4	What professional directors and officers indemnity insurance (**D&O cover**) is available against all these liabilities?	It's strongly recommended that directors should **never accept mandate unless insured** by the company. A Luxembourg-based policy is preferable. It must cover Luxembourg and all countries where the company is located/operates. It is also in the company's best interests to have adequate D&O cover for directors, as where the insurance cover does not apply, directors may call on the company's assets for indemnification having an indemnity from the company itself. Recommendations include: • Each director should receive a copy of the policy and check each year that it is up-to-date and renewed. It is also standard to receive an additional one-page summary of the policy from the insurer. • The directors should negotiate the policy - policies are highly technical and are also extremely varied in terms of amount, terms and exclusions. • In complicated cases, the company may consider employing an insurance broker specialised in D&O insurance, who understands the risk profile of the company, and who will undertake a process of due diligence regarding the company. Following this, the broker should highlight the differences between the various D&O products on offer. • The directors should review the policy in detail for coverage retentions, significant exclusions etc. Entities should also consider employing a specialist insurance lawyer to review the D&O products on their behalf. Directors need to review and consider the impact of each exclusion. For example: – When considering the amount, remember this is an aggregate amount for all the company directors each year, so in the case of disagreement between them and each appointing its own lawyers, this amount may erode quickly. – The policy may need to cover not only the cost of protracted and complicated litigation and/or investigations brought by investors and/or regulators, but also cover potential damages awards. – Often excluded are: • US claims and litigation made in the US or the enforcement of US decisions in other territories, US ERISA claims and/or claims under the US securities Act of 1933 or US Securities Exchange Act of 1974; • Fraud;

- Claims related to money laundering (actual or alleged), claims relating to market fluctuations and investment performance, claims by major shareholders, market abuse, punitive damages exclusions, regulator claims exclusions;
- Bankruptcy/insolvency are often excluded, yet you are most likely to need the cover following an insolvency event;

- Sometimes the Luxembourg directors are included in the company's group insurance cover. Important issues to consider include in relation to group cover:
  - Although there may be higher overall coverage levels, often these are for all actions worldwide and per annum. If for example, there has been a significant claim elsewhere in the group, that year's director coverage may already have been used up - meaning there is no insurance left for that year (it is applied on a first come, first served basis). Some insurance policies provide for a ring-fenced part for independent directors.
  - If group entities prejudice the cover (e.g. not pay the premium, commit a breach or a fraud), there will be no cover and local directors will not necessarily be aware of this.
  - In the case of a dispute, claims through an insurer in a foreign jurisdiction rather than in the company's home jurisdiction may not be convenient.
  - Company level cover will be easier to monitor & control, although it may be more costly than simply adding the company to the group's existing D&O policy. Additionally, if a director leaves a company on bad terms he may have difficulty getting access to the policies.
  - Price varies enormously, depending on parties involved, experience, etc. Often larger groups have better negotiating power and are perceived by the insurers as being a lower risk.
  - Consider tail insurance on termination of a company.
  - The director should make sure that they have cover after resignation or termination as a director for any loss caused by action or omission, which occurred during the time they were a director.

- Best practice is to also have additional second ranking insurance in case the group/ company insurance is not sufficient. Directors normally need to arrange this themselves, although it may be billable to the company.

	• Beware of insurance deductibles (*franchises*) • Be aware of the difference between the company's indemnity insurance and the director's individual D&O insurance (which are usually mutually exclusive). It is advisable to obtain policies combining both professional indemnity and D&O policies to ensure there is no gap in the coverage. The level of any cover, which will be limited, will depend on the size and complexity of the company. The insurance will often only cover the defence costs, not any fines or penalties which may ultimately be levied. One should be aware of whether damages, which may be awarded, are covered by the policy or not.

6 Bibliography

Website links

Luxembourg regulators and governmental bodies

- Commission de Surveillance du Secteur Financier (CSSF) - www.cssf.lu
- The Ten Principles of Corporate Governance of the Luxembourg Stock Exchange - www.bourse.lu/corporate-governance
- Register of Commerce & Companies Luxembourg - www.rcsl.lu
- Chamber of Commerce - www.cc.lu

Industry associations

- AIMA - Alternative Investment Management Association (Hedge Funds) - www.aima.org
- ALFI - The Luxembourg Association of Investment Funds (ALFI) - www.alfi.lu
- EFAMA - The European Fund and Asset Management Association - www.efama.org
- EFAMA - Code for External Governance Principles for the Exercise of Ownership Rights in Investee Companies (or so-called “Stewardship” rights and obligations)
- EVCA - European Private Equity and Venture Capital Association - www.evca.eu
- IIFA - International Investment Funds Association - www.iifa.ca
- Luxembourg For Finance - http://www.luxembourgforfinance.lu/
- INREV - European Association for Investors in Non-listed Real Estate Vehicles - www.inrev.org
- LPEA - Luxembourg Private Equity Association - www.lpea.lu
- Overseas trade associations, e.g. Bundesverband Investment and Asset Management (BVI)

Directors and other corporate governance institutes

- The Luxembourg Institute of Directors (ILA) – www.ila.lu
- European Corporate Governance Institute - www.ecgi.org
- Institute of Directors (England) - www.iod.com

Useful publications can be found on the sites of various local law firms, accounting firms, trust companies etc. For example:

- Global accounting firm publications, for example:
  - Deloitte - http://www.deloitte.com/dtt/home/0,1044,sid%253D48224,00.html
  - Ernst & Young - http://www.ey.com/global/content.nsf/Luxembourg_E/Financial_services_overview
  - KPMG - http://www.kpmg.lu/VirtualLibrary/Handouts.htm
  - PwC - http://www.pwc.com/extweb/pwcpublications.nsf/docid/F2E50885001DC41580257559004A168F
- Local law firm publications, for example:
  - Allen&Overy - http://www.allenovery.com/locations/europe/luxembourg/en-gb/publications/Pages/default.aspx
  - Arendt & Medernach - http://www.arendt-medernach.com/knowledge/laws-and-regulations
  - Elvinger, Hoss & Prussen (see under Legal Topics) – http://www.ehp.lu/index.php?id=23
  - Linklaters - http://www.linklaters.com/locations/Luxembourg/english/

Loyens & Loeff - http://www.loyensloeff.com/en-US/AboutUs/Offices/Pages/Luxemburg.aspx

Main sources of Luxembourg laws and regulations

- **CSSF** - http://www.cssf.lu/index.php?id=23&L=1

Certain key CSSF documentation relevant to directors include:

  - CSSF annual reports - http://www.cssf.lu/index.php?id=33
  - CSSF director's declaration of honour (under www.cssf.lu/formulaires/)
  - Anti-Money Laundering Circulars - http://www.cssf.lu/en/laws-and-regulations/circulars/news-cat/43/

- **ALFI** - **Code of Conduct for Investment Funds** - www.alfi.lu/about-alfi/alfi-code-conduct

Major laws relating to entities (as at 31 December 2012):

- **Luxembourg Law - primary sources**

  - **Légilux** - **www.legilux.public.lu/**
    Légilux is the Luxembourg government portal for laws and regulations and also for Mémorial publications. Note that only those versions of the laws that are found on Légilux (in their original French) are official versions.
  - **The CSSF also has a list of relevant laws and regulations – many also translated into English (unofficial translations) - www.cssf.lu/en/laws-and-regulations/legislation/news-cat/31/**

- **1915 Companies Law**

  - **French - (as amended up to 15 August 2011) http://www.ehp.lu/uploads/media/Loi_du_10_aout_1915_concernant_les_societes_commerciales_Aout_2011.pdf**
  - **Unofficial English translation (as amended up to August 2011) www.ehp.lu/uploads/media/Law_of_10th_August_1915_updated_August_2011.pdf**

- **Securitisation Law**

  - **Law 22 March 2004**

7 Appendices

Example board meeting agenda – (depending on structure of company, current issues etc.)

Below are items relevant to regular board meetings. Entities may also have transactional board meetings at short notice and often with pre-prepared agenda/minutes and draft documentation to enable decisions to be taken swiftly.

Although it will not always be possible, try to send board papers electronically to board members at least one week in advance. **Receiving board packs only at the meeting is too late.**

1. **Legal and corporate**
   - Constitution of the meeting (cf notice, chair, quorum, Agenda, waiver of notice/consent to short notice)
   - Review of corporate documents (Company extract from RCSL)
   - Declarations from any directors having opposing interests to those of the company
   - Approval of the previous board minutes
   - Review of circular resolutions signed in the period
   - Review of minutes of committees
   - Review list of agreements signed since the last board meeting or under negotiation
   - Any changes to the articles, minutes of meetings of shareholders
   - Tax, legal and regulatory review - any major legal, regulatory or fiscal changes affecting the company (consider inviting the external counsel and auditors at least once per year)
2. **Investment Management**
   - Investment reports
   - Investment valuations
3. **Compliance**
   - Compliance report (including any compliance breaches)
   - Compliance with own investment policy or restrictions (if applicable) KYC/AML compliance
   - Updates to procedures manual

4. Business and operations update

- Management accounts
- Cash flow forecasts
- Account balances
- Large payments made since last meeting
- Budget
- Human resources

5. Any other business

- Action points (see also table in A.3. below)
- Other

6. Date of the next meeting

Checklist of some other non-exhaustive potential items to consider

- Review of board delegations and delegation guidelines
- Audit and financial statements
  - Auditor engagement letter
  - Year-end report
  - Representation letter to the auditor and from service providers
  - Report from auditors - invite potentially once a year
- Discuss accounting principles
- Question auditors before signing off accounts
- Management letter from auditor
- Insurance coverage review
- Remuneration
- Review of compliance with corporate governance guideline

Sample action points table

Luxembourg Company XYZ

Action points outstanding from the board of directors' meetings

As at XX 20XX (date)

	Action point	Ref. Board papers - date	Responsibility	Due by	Status
1					
2					
3					

Sample template: status of agreements

Luxembourg company

Overview of agreements & contracts*

**The proposed contents are indicative only and will depend on the nature of the company*

Investments related agreements	*Status*	*Date*	*Comments*
xxx	Completed & signed		
xxx	Final, ready for use		
xxx	Final		
Borrowing agreements	*Status*	*Date*	*Comments*
xxx			
xxx			
xxx			
Administrative agreements	*Status*	*Date*	*Comments*
xxx			
xxx			
xxx			
Corporate agreements	*Status*	*Date*	*Comments*
xxx			
xxx			
xxx			

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