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Luxembourg

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Newsletter Q2 2015

Luther S.A.

Adoption by the Government Council of the bill 6831 on the Société d'Impact Sociétal

On 1 July 2015 a new bill on the Société d'Impact Sociétal (the "**SIS**") has been filed with the Chambers of Deputies (the "**Bill 6831**").

The Bill 6831 aims to provide a legal environment favourable to the development of businesses which transcend the classic division between the profit-making commercial sector and the non-profit sector.

1. Conditions to become a SIS

Every S.A., S.C.A., S.à r.l., Cooperative company or S.E. may apply for an agreement from the Minister in charge of Social and Solidarity Economy to the extent that it meets the 3 following conditions:

- carries-out on a continuous basis an activity of production, distribution or exchange of goods or services;
- pursues a social or societal objective which itself fulfils at least 1 out of the 3 below criteria:

  a. aiming to bring support to persons in a fragile situation (i.e. disabled persons, elders, persons into precarious situations…) and who may either be employees, clients, members or beneficiaries of the SIS;

  b. aiming to contribute to the preservation and development of social ties, fight against the exclusion and the health, social, cultural, economic or gender gaps, maintain or reinforce the territorial cohesion or develop educational activities;

  c. participating to the sustainable development and protection of the environment if such activity is related to one of the objectives mentioned above at items a) or b).

- be independently managed and undertakes to reinvest at least half of its profits to the maintaining or development of its activities.

The articles of association of the SIS will have to indicate the means by which its objectives will be reached and provide for performance indicators allowing to verify the achievement of such objectives.

2. Specific rules applying to SIS

- the share capital of the SIS shall be represented (i) for at least at 50 % by impact shares (*parts d'impact*) which do not allow their holders to benefit from the profits generated by the SIS and (ii) for the remaining part by performance shares (*parts de rendement*) entitling to the profits of the SIS to the extent that the SIS indeed fulfilled its social and societal objectives;
- the profits generated by the impact shares of the SIS shall be automatically allocated to an impact reserve which is to be used exclusively for the achievement of the social and societal objectives provided for in the articles of association of the SIS;
- the SIS is not authorised to issue debt instruments to its shareholders (except with the consent of the Minister which shall nonetheless remain exceptional);
- the SIS will have to adopt a remuneration policy and the salaries to be paid to the SIS' management will have to be capped;
- the annual accounts of the SIS will have to be audited by an independent auditor (*réviseur d'entreprises agréé*) and the management of the SIS will have to establish an extra-financial impact report intended at the SIS' shareholders;
- in case of liquidation (voluntary or judiciary) the liquidation proceeds remaining will be assigned to (i) another SIS with similar activities (the liquidation proceeds of the liquidated SIS will be allocated to the impact reserve of the receiving SIS) as a donation, or (ii) a Luxembourg foundation or an ASBL of public interest, or (iii) a private legal person established outside from Luxembourg and having a purpose similar or comparable to the SIS in liquidation;
- the SIS is submitted to the tax rules applicable to commercial companies and, hence, to VAT, municipal tax and business tax. This is to avoid any unfair competition by the use of SIS;
- will only be tax deductible the donations made to SIS having their capital represented at 100 % by impact shares.

Latest amendments made to the bill 5730 on the Modernisation of the Luxembourg law dated 10 August 1915 on commercial companies, as amended (“**Bill 5730**”)

After almost 5 years of apparent standstill and the appointment, in-between of new rapporteurs, the Legal Commission of the Chamber of Deputies has adopted, on 2 April 2015, new amendments (the “**Amendments**”) to the Bill 5730, which was itself adopted on 8 June 2007 and subject, since then, to numerous comments and amendments.

As a reminder, the initial version of the Bill 5730 aimed at modernising the Luxembourg law on commercial and civil companies by, among others, introducing the following provisions in the Luxembourg law:

- for the S.A.: restrictions to the free transferability of shares, squeeze out of shareholders, governance by management committees, extension of minority shareholders’ rights.
- for the S.à r.l.: issuance of beneficiary shares without voting rights, redemption of own shares, squeeze-out.
- introduction of a new type of commercial company: the *société par actions simplifiée.*

1. Main changes brought by the Amendments

The main changes brought by the Amendments to the initial Bill 5730 as amended on 7 May 2009 are the following:

1.1. Changes affecting all the commercial companies regardless of their legal form

- issuance of tracking shares by either commercial and civil companies;
- conversion of a commercial company into a civil company;
- prohibition for Luxembourg companies to adopt a denomination similar (and not identical) to an existing company and which would be misleading for the public.

1.2. Changes affecting the Sociétés Anonymes

- possibility for the management of the S.A. to issue shares without nominal value below the accounting par value of the existing shares.
- possibility for the S.A. to allocate its own shares or issue new shares to its employees for free;
- the conversion of shareholders loans and convertible instruments shall no longer require the issuance of a report from an independent auditor;
- non-voting shares may represent more than 50 % of the share capital of the S.A. and the articles of association of the S.A. will have to set out the financial rights to be attached to such shares and which rights have no longer the obligation to consist in a preferred and privileged dividend;
- possible delegation of the management of the S.A. by the board of directors to a general director;
- minority shareholders and holders of beneficiary shares representing 10 % of the voting rights in the S.A. will have the opportunity to challenge the discharge granted to the management and supervision bodies of the S.A.;
- introduction of the possibility for the articles of association of the S.A. to allow the board of directors to suspend the voting rights of defaulting shareholders;
- the change of nationality is no more subject to unanimity. The management of the S.A. will be entitled to transfer the registered office of the S.A. from a municipality to another;
- simplification of the convening procedures for the ordinary and extraordinary shareholders’ meetings.

1.3. Changes affecting the Sociétés à responsabilité limitée

- possibility for an S.à r.l. to issue redeemable shares.

- introduction of the issuance of beneficiary shares (i.e. shares not comprised in the share capital) for S.à r.l.;

- introduction of the possibility for the articles of association of the S.à r.l. to allow the board of managers to suspend the voting rights of defaulting shareholders;

- the change of nationality is no more subject to unanimity. The management of the S.à r.l. will also be entitled to transfer the registered office of the S.à r.l. from a municipality to another.

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European Long-term Investment Funds

1. Review Process

On 19 May 2015, the regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 on European long-term investment funds (the "**Regulation**") was published in the Official Journal of the European Union. For reminder, the legislative process which started in June 2013 with the submission by the EU Commission (the "**Commission**") of the initial proposal comes thus to an end.

The Regulation provides the regulatory framework for the European long-term investment funds (the "**ELTIFs**") aiming at increasing the available long-term capital in the real economy of the EU by providing long-term commitments to various infrastructure projects, unlisted companies, or listed small and medium-sized enterprises. Pursuant to the Regulation, such infrastructure projects include among others public building infrastructure (i.e. schools, hospitals, prisons), transport infrastructure (i.e. roads, airports), energy infrastructure (i.e. energy grids, power plants, pipelines) and water management infrastructure. The Regulation, creating a new investment fund vehicle, is also intended to contribute to facilitating the Capital Markets Union initiated by the Commission.

2. Background

As funding for infrastructure projects, which requires long-term investments in illiquid non-transferable assets and as bank financing during the financial crisis were not sufficient, there was a need to further consider other financing sources in order to bridge the financing gaps.

3. Key provisions

An ELTIF is an alternative investment fund ("**AIF**") domiciled in the EU and managed by an authorised alternative investment fund manager ("**AIFM**") within the meaning of the Directive 2011/61/EU relating to AIFM. Once authorised in accordance with the Regulation, an ELTIF can be marketed throughout the EU pursuant to the passport mechanism. Thus any non-EU AIFs are excluded from the scope of the Regulation.

3.1. Marketing to retail investors

Contrary to the AIFs, ELTIFs may be marketed not only to professional investors, but also to retail investors, albeit with certain restrictions. First of all, the manager of an ELTIF has an obligation to ensure (i) that any retail investor with a financial instrument portfolio not exceeding EUR 500,000 does not invest an aggregate amount exceeding 10 % of that investor's portfolio in ELTIFs and (ii) that the minimum initial investment is EUR 10,000.

The Regulation also foresees specific provisions when a manager of an ELTIF intends to market an ELTIF to retail investors. As such, the manager of an ELTIF shall, based on a specific internal process, take into account at least the duration of the ELTIF and its intended investment strategy. In addition, the manager of an ELTIF will consider whether the ELTIF is suitable for that particular retail investor after having obtained information such as (i) its knowledge and experience in the investment field relevant to the ELTIF, (ii) its financial situation, including its ability to bear losses and (iii) its investment objectives, including its time horizon.

An ELTIF marketed to retail investors shall (i) publish a key information document ("**KID**"), in accordance with regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on KID for packaged retail and insurance-based investment products and (ii) have a depositary which complies with the requirements of Directive 2009/65/EC relating to undertakings for collective investment in transferable securities ("**UCITS**"), such as the eligible entities, the prohibition of the discharge of liability and the reuse of assets.

In order to facilitate the access of ELTIFs to retail investors, a UCITS may invest into an ELTIF provided that the ELTIF shares are eligible under UCITS Directive.

3.2. Investment policy

Respecting the rationales and the very objectives of the Regulation, ELTIFs may invest in (i) eligible investment assets which are considered illiquid, and (ii) the eligible assets referred to in Article 50(1) of the UCITS Directive which are deemed liquid. It should be noted that eligible investment assets consist of instruments issued by qualifying portfolio undertakings or loans to such undertakings, but also investments units of certain other ELTIFs, EuVECAs or EuSEFs, and direct or indirect holdings in certain real assets. In short, qualifying portfolio undertakings may not be financial undertakings or undertakings for collective investment, nor be admitted to trading, and have to be established in a Member State or certain third countries.

The Regulation states that an ELTIF should invest at least 70 % of its assets in eligible investment assets. For the purpose of ensuring the diversification of any ELTIF, it should invest among others no more than (i) 10 % of its capital in instruments issued by a single qualifying portfolio undertaking, (ii) 10 % directly or indirectly, in a single real asset and (iii) 10 % of its capital in units or shares of any single ELTIF, EuVECA or EuSEF.

ELTIFs may borrow cash provided such intention to borrow is disclosed in the investment strategy in the fund documents. In the marketing material of an ELTIF, it must describe its hedging policy, noting that the financial derivative instruments may not be used other than for the purpose of hedging the risks inherent to its own investments.

4. Entry into force

The Regulation entered into force on 8 June 2015 and shall apply from 9 December 2015. European Securities and Markets Authority shall establish draft regulatory technical standards specifying certain modalities and to be submitted to the Commission by 9 September 2015.

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Capital Markets Union – Green Paper of the European Commission

The European Commission has recently published its green paper on “Building a Capital Markets Union”.

While the priority of the European Commission is to focus on jobs and growth in the EU, the free flow of capital is one of the fundamental principles of the EU. Those two aspects shall be linked and combined by building a Capital Markets Union. In order to strengthen investment in the EU for the long term, a true single market for capital needs to be created and developed throughout the 28 Member States.

As of today, the EU financial system is heavily reliant on banks. By complementing banks as a source of funding, stronger capital markets would create a more stable financial system. Investment for Europe’s companies and in particular small and medium-sized enterprises (the “**SMEs**”) and for infrastructure projects could be unlocked and more investment into the EU could be attracted.

The green paper and the building of a capital markets union will be presented below through setting out the key principles and objectives (1.), the challenges to be overcome (2.), the first steps of implementation (3.) and an outlook on the next steps to be taken (4.).

1. Key principles and Objectives

1.1. Key principles

- Maximizing benefits of capital markets for the economy, jobs and growth;
- Removing barriers to cross-border investment within the EU and fostering capital markets with the rest of the world;
- Ensuring an effective level of consumer and investor protection;
- Increasing EU-competitiveness by attracting investment from all over the world; and
- Establishing a single rulebook.

1.2. Objectives

The main objectives of a capital markets union according to the green paper are the improvement of access to financing (especially for SMEs) (1.2.1), increasing and diversifying the sources of funding (1.2.2) and the improvements of the markets and the rules by which they are governed to make them more efficient and effective.

1.2.1. Improving access to financing for all business and investment projects

In order to facilitate access to financing for companies the cost of capital raising should be reduced, particularly for SMEs. An ideal situation would be where SMEs are able to raise funds as easily as large companies.

Access to capital and the costs of investing should be harmonised all over the EU and a real convergence should be reached. Therefore, a certain degree of standardisation would be required. Where common standards cannot be achieved, policy efforts should allow establishing best practices. As an example for a common standard, a common accounting standard for SMEs could facilitate their access to capital markets due to better comparability. Another important point is that transparency and availability of information should be increased in order to allow for investors to assess and compare investment offers and facilitate their investments. In addition, alternative means of financing, such as peer to peer lending or crowd financing shall be developed in order to enhance capital markets funding. Alternative investments could also be investments in social and corporate governance or environmental projects, such as green bonds.

1.2.2. Increasing and diversifying the sources of funding

In order to allow diversification of the sources of funding, institutional, retail as well as international investors should be attracted to invest in capital markets in the EU.

In order to attract institutional investors, one of the requirements is to reduce the costs for setting up funds and cross border marketing, which would lower the barriers to the entry into the market, and more competition could be created.

To attract retail investors, a key issue is to restore trust of retail investors. Savings held on bank accounts by individuals could be used more efficiently. As deposit rates are declining, investors could be incented to move their savings to capital markets. Besides restoring trust of investors, it should also be focused on proposing standardised products along with improving financial literacy and education of consumers so that retail investors feel more comfortable on the market.

While the high standards of the EU market for market integrity, financial stability and investor protection should be maintained, direct marketing of EU investment funds and other investment instruments in third countries should be facilitated by reducing barriers for EU financial institutions and services to access third country markets.

1.2.3. Making markets more efficient and effective

The creation of a single rulebook, which will need to be effectively implemented and consistently enforced, will set the legal and regulatory framework of the capital markets union to make markets more efficient and effective.

Competition plays an important role for the market, as it helps ensuring to channel investment flows towards the most productive uses. Therefore, entry barriers for new entrants to the markets shall be removed and access to financial market infrastructure shall be assured. Hence, competition law has to be applied rigorously for consumer protection.

As regards the free flow of capital, barriers, such as unjustified restrictions imposed by host Member States on market operators with a European marketing passport need to be removed, as a more stable, transparent and predictable framework could contribute to building investor confidence.

As market infrastructure and securities law are key determinants for the efficiency of investments, the European Commission intends to establish - in addition to the regulatory framework - a legislative proposal to create a European framework for the recovery and resolution of systemically relevant financial institutions, such as central counterparties. Moreover, as the demand for collateral has significantly increased since the financial crisis, the risk that such collateral is reused for multiple transactions also needs to be addressed.

Furthermore, the European Commission is reviewing how company law, corporate governance rules, insolvency and taxation legislation can be harmonised and adapted in order to improve market infrastructure and the securities regime.

New technologies and especially the combination of new technologies with innovative financial services the so-called “FinTech” constitutes an important and growing potential for investments. However, in order to keep pace with this development, European and national company law needs to be updated, amongst other, to integrate the benefits of digitalisation.

2. Challenges

By building a single market for capital, there are considerable challenges to overcome. As of today, capital markets in the EU are fragmented and organised on national lines and access to capital markets differs across firms and across EU Member States. The economy in the EU is quite vulnerable, as it is very reliant on banks for funding, and in the context of the financial crisis, investor confidence has dropped significantly. Furthermore, there are large data gaps and features in the national tax systems that need to be overcome.

These challenges will be tackled by taking the following measures for the creation of a single market for capital.

3. Measures of implementation

In order to achieve the objectives set by the European Commission and to overcome the abovementioned obstacles, the European Commission considers the following implementation measures as a priority:

3.1. Lowering barriers to accessing capital markets – Review of the prospectus regime

As the main document setting out the terms and conditions as well as the risks of an investment, the prospectus is an important document in a capital markets funding, which is subject to a stringent regime. In order to avoid barriers for funding through the requirements for prospectuses, the European Commission will review the current prospectus regime and has launched a specific consultation in order to simplify the requirements.

3.2. Widening the investor base for SMEs – Improving credit information through workshops

As information on SMEs is mostly held by banks, access to such information is limited to non-bank investors and SMEs often have difficulties to reach a broader investor base of non-bank investors. The European Commission intends to organise workshops on SME credit information as a first step to improving availability of information on SMEs.

3.3. Building sustainable securitisation – Solvency II and Liquidity Coverage Ration delegated acts

Securitisation can provide a powerful mechanism for transferring risks by pooling assets together for investors. However, the activity of securitisation has decreased since the financials crisis. Consultations have been launched in order to boost the securitisation market and the publication of the delegated acts on Solvency II and Liquidity Coverage Ratio contribute to a comprehensive and consistent prudential approach for securitisation.

3.4. Boosting Long Term Investment

In order to foster long terms investments, the European Commission has established a new Fund for Strategic Investment Funds (EFSI) and has published a communication on long term financing. Furthermore, the Long-Term Investment Funds (ELTIFs), a regulatory framework, has been created for investors to invest in companies and infrastructure projects for the long term.

3.5. Developing European private placement markets

Investments via private placements may be more cost effective than on public markets and can facilitate the availability of financing for medium to large companies and potentially infrastructure projects. In order to develop private placement markets in Europe, a market guide on common practices, principles and standardised documentation has been established by a consortium of industry bodies.

4. Next steps

Following the three months consultation, which has recently been closed, a conference on the ”Next steps to build a Capital Markets Union” has been held in Brussels on 8 June 2015. Based on the outcome of the consultation, the European Commission develops an action plan for the further implementation of the Capital Markets Union.

We would also like to point out that the European Securities and Markets Authority (ESMA) has confirmed in its response to the green paper that it supports the aims of the Capital Markets Union and has stressed that not only access to capital shall be improved, but also more equity funding shall be the result of the Capital Markets Union.

In terms of timing, the European Commission’s objective is to create a fully functioning Capital Markets Union by 2019.

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Notification of the incapacity of work

A recent case law (C.A. 12/03/2015, No 40824) clarifies the deadline within which the employee has to inform the employer about his/her inability to work, as mentioned in the article L. 121-6 of the Labour Code. In such case, the judges of the Court of Appeal have specified that any clause which imposed the employee to inform the employer before 9 a.m. of her/his sickness is null. In fact, such clause is considered as being less favourable for the employee than the employment law. As the employer has dismissed the employee with immediate effect on the first day of the extended sick leave, the judges of the Court of Appeal have therefore considered this dismissal as abusive.

This case law is a good opportunity to remind some essential rules about the notification of the incapacity of work and the possible protection against dismissal in such case.

1. When must the employee inform the employer and submit his/her medical certificate?

(i) If the employee is unable to work because of sickness or accident, she/he must notify (orally or in written) the employer or an appropriate representative of the employer of her/his incapacity either personally or through someone else the very first day of her/his absence or extended sick leave. The recent case law mentioned above, introduces a new element as the employee has **until midnight** to notify his/her absence.

(ii) On the third day of her/his absence or extended sick leave at the latest, the employee shall be obliged to submit to the employer a medical certificate attesting her/his inability to work and the foreseeable length of time.

2. What are the consequences for the employer and the employee in case of respect of the process?

The employer who has been duly notified of the employee's incapacity of work in due form and within the legal length of time (i) or who has received the medical certificate from the employee in due form and within the legal length of time (ii) is not allowed to notify to the employee, even for serious reasons, the termination of the employment agreement or, where relevant, to convoke the concerned employee for a pre-dismissal interview. Any notification of the dismissal by the employer to the employee who has fulfilled the two cumulative conditions (i and ii) is unfair.

In fact, the employee is, during her/his sick leave, protected against dismissal for a period of twenty-six weeks following the date of the incapacity of work.

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