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Luxembourg: Law & Practice and Trends & Developments

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LUXEMBOURG

Law and Practice

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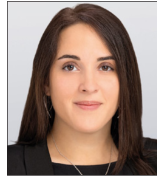

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1. Market Trends

1.1 Recent Changes

While it would be inaccurate to claim that inflation, interest rate fluctuations, geopolitical tensions like the war in Ukraine and ongoing Middle Eastern conflicts, or shifting market demands have not impacted Luxembourg-based joint ventures, the jurisdiction remains appealing for JV structuring. This is largely due to its political and economic stability, as well as its reliable, business-friendly, and flexible legal framework.

In recent years, family offices have increasingly invested alongside commercial partners or institutional investors, such as private equity firms, through joint ventures. These JVs are frequently used to acquire assets located outside Luxembourg, with the involved parties often situated internationally. Luxembourg serves as a compromise, a “safe haven”, for incorporating the holding structure that will ultimately own assets across the European Union or even globally.

The trend in these segments clearly leans towards controlling and sharing both financial and corporate risks while ensuring the distribution of profits to co-investors. In uncertain times, JVs have proven to be a strategic option for parties to pool resources and expertise, leveraging their combined strengths, funds, and shared risks to pursue specific projects or opportunities.

1.2 Key Industries

In Luxembourg, several industries and sectors have seen heightened JV activity, notably in the financial services, renewable energy, real estate, healthcare and life sciences, logistics and supply chain the technology and fintech sectors. Luxembourg is a leading financial and tech hub for innovation in financial technology. The country’s strategic support for the space technology sector has also attracted numerous private space companies and tech firms.

This increase in JV activity can be attributed to the factors described in **1.1. Recent Changes**, particularly the stable but very flexible legal environment of the Grand-Duchy of Luxembourg.

2. Types of Joint Venture (JV)

2.1 JV Vehicles

JVs are not legally defined under Luxembourg laws. A JV is an arrangement between at least two parties reflecting their willingness to share a venture, for either joint commercial or joint investment purposes, by gathering their resources and sharing the risks implied by the project.

While JVs are not required to take any prescribed legal form, the two types of JVs typically used in Luxembourg are the corporate JVs – which implies in most cases the incorporation of a separate JV vehicle by the participants (should an operational company not already have been incorporated by one participant to the JV) and the contractual JVs, based on a single contractual arrangement whereby participants define the scope of their collaboration and related rights and obligations in an agreement.

Contractual JVs are recommended for short-term collaboration focused on a specific project. In a contractual JV, the participants remain liable for the JV liabilities, but do not have to bear the costs incurred by the incorporation and day-to-day administrative management of a common JV vehicle. Although not all aspects of Luxembourg law applicable to agreements can be mentioned here, it is worth mentioning that there are no compulsory formalities required in relation to contractual JVs. The joint venture agreement

is structured as an agreement and executed by the parties thereto. There is no requirement to have it enacted by a notary, to adopt any specific form, and there is no stamp or registration duty. The agreement may be written in English without requiring translation into any of Luxembourg's national languages.

As to the content of the agreement, the principle of freedom of contract largely applies, subject to non-conflict with public policy rules. In relation to any Luxembourg law-governed agreement, an overriding duty of good faith always applies between the parties in their performance of the provisions of the agreement itself, but also in pre-contractual discussions and in any enforcement of the agreement that may be required.

While a corporate JV involves some costs and complexity, for instance in compliance and governance, it offers limited liability to participants, an established governance structure, and capital-raising capabilities for future business growth.

A successful JV requires a high level of collaboration and co-operation, which may explain the dominance of corporate JVs in Luxembourg.

The forms of JV vehicles most commonly adopted for corporate JVs in Luxembourg are the following:

- private limited liability company (*société à responsabilité limitée* – S.à r.l.);
- public limited liability company (*société anonyme* – SA);
- simplified joint stock company (*société par actions simplifiée* – SAS);
- partnership limited by shares (*société en commandite par actions* – SCA); and
- limited or special limited partnership (*société en commandite simple* – SCS, or *société en commandite spéciale* – SCSp).

It is specified that for the SCA, SCS and SCSp, the JV participants are limited partners with limited liability and the general partner has unlimited liability.

2.2 Choice of JV Vehicle

In Luxembourg, the choice of the most appropriate legal form for the JV vehicle depends on several factors, notably the possibility offered by the selected structure to provide for tailor-made solutions regarding the decision-making structure of the JV, management preferences, capital needs, pooling of profit and losses, transfers of shares, and its accounting and tax treatment.

If the JV is not established to conduct a regulated activity or to issue securities to the public, then the S.à r.l. is typically the preferred vehicle for a JV as it offers greater flexibility and is not subject to extensive statutory requirements. As per the law on commercial companies dated 10 August 1915, as amended (LCC), the S.à r.l has a share capital of at least EUR12,000, is managed by a single manager or a board of managers, cannot make public offers (either of shares or debt securities) and the transfer of shares in an S.à r.l. to non-shareholders requires the approval of the existing shareholders holding at least 75% of the issued share capital by a formal shareholder resolution – it being specified that the articles of associations can provide for a lower threshold which, however, cannot be less than 50%. Given the importance attributed to the individual identity of the shareholders, it is not permissible to adopt such resolutions of approval at the inception of the joint venture without knowing the identity of the proposed future transferees. The JV agreement could, however, include a pro-

vision whereby all shareholders at the time of execution of the JV agreement commit to vote in favour of such a resolution. Voting arrangements are, subject to certain conditions, valid under Luxembourg laws. Finally, it is worth mentioning that the identities of the shareholders of an S.à r.l. are mandatorily disclosed publicly at the Trade and Companies Register (*Registre de Commerce et des Sociétés* – RCS).

While often overlooked in practice, the SAS, introduced in Luxembourg in 2016, presents a compelling alternative to the S.à r.l. It provides a high level of confidentiality to shareholders, with their identities and shareholdings remaining undisclosed at the RCS. Moreover, except for mandatory or public order provisions, it permits extensive customisation, particularly concerning management structures, voting features (such as shares with multiple voting rights), and profit and loss sharing through the issuance of preference or ratchet shares.

The SCA, SCS and SCSp legal structures are typically favoured for investment-focused JVs (involving silent investment partners) where some participants prefer not to be as deeply involved in the management decisions as they would be in a different legal structure and as such, prefer to have a limited partner position.

From a regulatory perspective, when established for investment purposes, it has to be confirmed that the JV vehicle does not qualify as an alternative investment fund subject to the EU alternative investment fund managers directive (AIFMD). If the JV vehicle has characteristics that place it within the scope of alternative investment funds as defined in the AIFMD, the regulatory requirements applicable to the investment vehicle and its manager will be significantly different from those applicable to an unregulated JV vehicle.

3. Regulation

3.1 Regulators

In Luxembourg, the main set of rules applicable to the JV vehicle are the provisions of the Luxembourg civil law rules and the LCC. However, depending on the nature of the JV set-up and the sectors in which it operates, and especially if the JV vehicle qualifies as an investment fund, public authorities will need to be involved, such as the Luxembourg Financial Supervisory Authority (*Commission de Surveillance du Secteur Financier* – CSSF) or the Luxembourg Insurance Commission (*Commissariat aux Assurances*).

If a JV is structured as an alternative investment fund (AIF) in Luxembourg, it falls into the regulatory framework established by the AIFM Law and the AIFMD. This requires, inter alia, seeking authorisation from and registration with the CSSF, and adhering to, inter alia, investment restrictions and transparency requirements.

According to the Law of 2 September 2011, which regulates access to various professions, any economic activity carried out on a regular basis, with few exceptions, necessitates obtaining a prior business permit from the Ministry of Economy. This permit must be held by a natural person on behalf of the relevant company. The said person must satisfy the following conditions:

- professional integrity;
- the necessary professional qualification relevant to the planned activity:
- establishment in Luxembourg; the business permit is only granted if there is a physical presence in Luxembourg that includes infrastructure suitable for the nature and scale of the concerned activity;

- effective and permanent management of the business by the business permit holder, who must:
  - (a) be physically present in the establishment at all times to ensure effective day-to-day management of the business; and
  - (b) be effectively connected to the business (as an owner or legal representative of the business); and
- compliance with tax and business obligations; the permit holder must not have evaded business and tax obligations (including withholding tax) in their previous or current business activities, whether these activities were carried out in their own name or through a company run by said permit holder.

3.2 AML

The key AML legislation applicable in Luxembourg is the law of 12 November 2004 on the fight against money laundering and terrorist financing (the "AML Law"), as last amended on 29 July 2022.

The AML Law implements the Fourth European AML Directive (EU 2015/849) as amended by the Fifth European AML Directive (EU 2018/843), and establishes the obligation for entities and individuals listed in Article 2 of the AML Law to (i) implement customer due diligence measures (Know Your Customer); (ii) ensure an adequate internal organisation with respect to AML-FT; and (iii) maintain transactional records as well as report any suspicious transactions or activities to the Luxembourg Financial Intelligence Unit (FIU) (*Cellule de Renseignement Financier*).

A further European AML package, to be partly applicable from early 2025, was adopted on 19 June 2024 by the European Parliament. This package includes the introduction of the Sixth European AML Directive, a proposed AML regulation introducing stricter due diligence requirements, beneficial ownership transparency and monitoring of transactions, and provides for the establishment of a new European AML authority (the Authority for Anti-Money Laundering and Countering the Financing of Terrorism – AMLA).

3.3 Restrictions and National Security Considerations

In Luxembourg, restrictions on co-operation with JV partners arise from both EU regulations and national legislation. At the European level, as a member state of the EU, Luxembourg is subject to the EU sanctions regulations. At the national level, the Law of 14 July 2023 on Foreign Direct Investment (the "FDI Law"), implementing Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019, establishes a national screening mechanism with respect to foreign direct investments that could impact national security or public order. With some exceptions, the FDI Law requires that direct investments made by foreign investors – ie, natural persons or legal entities residing outside the European Economic Area, seeking to gain control over a Luxembourg entity, be reviewed by the Ministry of the Economy if they involve critical sectors within Luxembourg, such as energy, transport, water, health, communications, data processing and storage, aerospace, defence, finance, media and business, as well as the trade of dual-use goods or which could affect national security. The FDI Law entered into force on 1 September 2023.

Beyond sanctions and national security considerations, there are additional regulatory and legal frameworks that may impose restrictions on JVs, including sector-specific regulations, competition law and other compliance requirements.

3.4 Competition Considerations

JVs in Luxembourg are currently not subject to a national ex ante merger control regime. Hence, to date, the antitrust regulation applicable to the setting up of JVs, if the latter qualify as a concentration, is the EU Merger Regulation on the control of concentrations between undertakings (Regulation (EC) No 139/2004) (the "EU Merger Regulation"). The EU Merger Regulation provides for an obligation to notify the European Commission should the thresholds set therein be met by the JV.

At the national level, should the JVs fall outside the scope of the EU Merger Regulation, no mandatory obligation to notify the Luxembourg national competition authority (NCA) currently exists. As per applicable Luxembourg laws, the NCA can only perform an ex post intervention with the aim of ensuring the proper functioning of the EU internal market.

Luxembourg is in the process of reshaping its competition framework, with the proposed enactment of the draft bill of law No 8296, which establishes a national ex ante merger control regime. This would require JVs to be notified to the NCA before being created in case they could affect competition in Luxembourg. The thresholds contemplated to trigger the NCA review will concern parties involved in the concentration if they have a combined total turnover generated in Luxembourg of more than EUR60 million and at least two of the parties involved in the concentration have an individual turnover generated in Luxembourg that exceeds EUR15 million. The NCA will have the authority to examine a concentration that falls below the abovementioned thresholds if it deems that such concentration could affect competition in the Luxembourg market. This new regime will undoubtedly impact the timeline for implementing a JV in Luxembourg, adding another layer of regulatory scrutiny alongside any notification that may be required under the FDI Law.

3.5 Listed Party Participants

The mere fact that a listed company (ie, whose securities are admitted to trading on a European regulated market), MTF or OTF, participates in a JV in Luxembourg, will not lead to the applicability of specific rules in Luxembourg in addition to or different from the EU capital market directives and regulations applying to listed companies in general.

3.6 Control/Ownership Disclosure Requirements

Since the entry into force of the Law of 13 January 2019 establishing the Beneficial Owner Register, as amended, (the "RBE Law"), all legal entities registered with the RCS are required to disclose and submit information about their ultimate beneficial owner(s) (UBO(s)) to the Register of Beneficial Owners (*Registre des bénéficiaires effectifs* – RBE). Such information must be updated within one month of any change. To date, the RBE is only accessible by "professionals" as defined in Article 2 of the AML Law for the purposes of their AML/KYC obligations and by entities registered with the RCS with respect to their own information.

Under Luxembourg laws, a UBO is any natural person who, ultimately, directly, or indirectly, owns or controls a legal entity (including by means of bearer shares), by a percentage of more than 25% of the shares, voting rights or an interest in the capital, or by other means. If, after all possible means, no UBO can be identified (and there are no grounds for suspicion), the natural person holding the position of principal executive officer of a legal entity is considered the UBO.

4. Legal Developments

4.1 Significant Recent Decisions or Regulatory Developments

Apart from the entry into force of the FDI Law, and the ex ante merger control regime provided by the bill of law No 8692, there have been no significant court decisions or legal developments in the past three years relating to JVs or business collaboration.

5. Negotiating the Terms

5.1 Negotiation Documentation

Setting up a JV entails a multi-phase process for the participants. The negotiating phase of a JV will effectively involve (i) the completion of a due diligence questionnaire focusing not only on the JV itself, its rationale or commercial goals, but also on the JV participants; (ii) the execution of a mutual non-disclosure agreement (NDA); (iii) the execution of a head of terms document which is crucial as it sets forth the main commercial and legal terms the participants have agreed upon during the negotiation; and (iv) in most cases, the execution of an exclusivity agreement prohibiting the parties from entering into negotiation with others for a restricted period of time.

At a pre-JV agreement stage, the following provisions would be expected to be contemplated and settled in the terms sheet:

- the purpose and scope of the JV;
- the financial contributions of each participant and further funding opportunities;
- the decision-making structure;
- the management structure;
- the transferability of shares and any restriction rights in relation thereto;
- profit sharing arrangements;
- contemplated dispute resolution mechanisms;
- exit mechanism; and
- termination of the JV.

5.2 Disclosure Requirements and Timing

Information about the JV will have been disclosed between the participants to the JV when the heads of terms is signed. For regulatory requirements around disclosing the JV, please refer to **3.3 Restrictions and National Security Considerations** and **3.4 Competition Considerations**.

5.3 Set-Up

Setting up a JV under Luxembourg law requires careful planning, and several steps must be complied with:

- Drafting the JV agreement: This crucial document will comprehensively outline the rights and obligations of the parties to the JV.
- Drafting the articles of association (or limited partnership agreement) of the JV vehicle: As publicly available (except for the limited partnership agreements which are only published partially), some parties prefer not to mirror the provisions of the JV agreement in the articles of association. This will be negotiated on a case-by-case basis.
- Incorporation of the JV vehicle under the chosen form: Generally, the incorporation of a company must be enacted before a Luxembourg notary, except for SCS and SCSp which can also be incorporated under private seal.
- Registration of the newly incorporated JV vehicle: The RCS articles, or extract of the limited partnership agreement in the case of SCS and SCSp, will be publicly accessible.
- Complying with any regulatory requirements: Depending on the nature of the JV's activities,

it may be necessary to comply with specific regulatory requirements. These could include merger control regulations, FDI rules, or obtaining relevant business permits, as applicable.

6. The JV Agreement

6.1 Agreement Documentation

Regardless of the form of the JV vehicle, the terms the parties agreed upon for the JV will be set out in detail in the JV agreement. In Luxembourg, JV participants can agree that the JV agreement will not be subject to Luxembourg law if the provisions of the chosen foreign law do not contravene public order provisions under Luxembourg law. As is often the case, parties to a JV may be based in different jurisdictions and will prefer to apply a law that is more familiar to them.

The main terms that a JV agreement would be expected to address include the following:

- scope of the JV, roles and responsibilities of each party;
- share capital modification and related anti-dilution aspects;
- funding obligations of the participants;
- management structure;
- reserved matters;
- deadlocks and dispute resolution mechanism(s);
- restrictions on share transfers, restriction to ensure the maintenance of the share capital and the withdrawal of certain of its shareholders under certain circumstances (drag-along/tag-along clauses);
- term of the JV;
- termination possibilities;
- plan for future change;
- exit provisions;
- put and/or call options;
- allocation of profits;
- distribution of assets;
- intellectual property rights; and
- confidentiality and non-disclosure obligations.

6.2 Decision-Making

Structuring the decision-making process within a JV is undeniably one of the most critical aspects to be discussed and carefully considered during its establishment. While the LCC provides a default framework, certain contractual mechanisms can play a vital role in shaping and refining the decision-making process within the JV, ensuring it aligns with the specific needs and objectives of the parties involved.

The following clauses can be inserted in the JV agreement or in its articles (where necessary):

- clauses relating to the allocation of the directors' mandates; such clauses will enable the JV partners to have a certain degree of representation at the management level by ensuring that the former have one or more of their representatives on the board of directors or managers (the "Board") of the JV vehicle;
- clauses allowing different categories of board members to be created – eg, class A and B, with different powers to act on behalf of the JV vehicle;
- a clause allowing the adjustment of the quorum and majority rules in decision-making bodies, enabling stricter rules in this respect than the ones provided for by the LCC (except for public order provisions);
- observer appointment clauses; in some cases, the JV partners will prefer to have an observer appointed instead of a director with voting prerogatives (an observer may receive all the documentation related to a particu-

lar meeting of the board and will be able to attend any board meetings); and
- specific consent clauses; in a classic JV vehicle, decisions by the board on strategic matters can require the approval of all, a majority, or a supermajority of the partners of the JV (the so-called reserved matters).

6.3 Funding

The funding of JV vehicles generally involves a blend of equity and debt – depending on the financial resources of the JV participants; the latter will make contributions in cash or in kind directly to the JV share capital or grant shareholders loans to the JV vehicle.

The JV agreement can provide for a future funding obligation to support the JV vehicle, notably with respect to capital requirements, working capital, ongoing operations, or financing of a project. Adjustment clauses in terms of default by one partner can help resolve situations where such a funding obligation cannot be satisfied by a partner.

Equity funding can lead to a change in the ownership of the JV vehicle and could effectively trigger a dilutive effect on the shareholding of existing participants. Several mechanisms, such as preferential subscription rights, anti-dilution clauses, issuance of instruments such as warrants and options do exist under Luxembourg law to ensure that a JV partner's shareholding is not diluted. Another equity funding option is the contribution to the capital account 115 of the JV vehicle without issuance of new shares, which is widely used.

6.4 Deadlocks

As mentioned in **6.1 Agreement Documentation**, one of the most essential issues to be addressed in a JV agreement is the resolution of a deadlock situation.

Provisions relating to confiscation or compulsory purchase of shares are generally valid, as long as they do not deprive shareholders of their shares without payment or deprive them of the right to request the dissolution by court of the JV for cause.

Furthermore, several contractual mechanisms can be contemplated to prevent a deadlock, which can be set forth either in the JV agreement or its articles or in both:

- escalation clauses to senior representatives of the involved parties;
- mediation and negotiation clauses;
- dispute resolution mechanisms (international arbitration or expert determination); and
- exit strategies – put and call options in favour of the dissenting partner, exclusions mechanics provided for in the articles of the JV vehicle.

6.5 Other Documentation

The set-up of a JV usually further requires the execution of additional documents, each having a specific role to play with respect to the success of the JV, notably:

- NDAs;
- IP licenses covering the use of the IP rights held by one of the partners to the JV by the latter;
- agreements to transfer assets to the JV vehicle as the case may be;
- asset management and service agreements;
- business Plan; and
- policies (eg, KYC, conflicts of interests).

7. The JV Board

7.1 Board Structure

Please refer to **6.2 Decision-Making** for an overview of governance organisation proposition and notably, the possibility of the shareholders of the JV vehicle being represented at the board by proposing candidate(s) to be appointed as board member(s) of the JV vehicle.

With respect to weighted voting rights, even though the current Luxembourg legal landscape tends to recognise them as a means to ensure board control, they are not commonly used in Luxembourg. The Luxembourg doctrine strongly advocates for the principle "one vote per person".

7.2 Directors' and Board' Duties and Functions

The management body of a JV vehicle is often either the board of managers in case of an S.à r.l, the board of directors in case of a one-tier SA or the management board in case of a two-tier SA, the president in case of an SAS (and any director as the case may be). This management body has the broadest powers to take any actions necessary or useful to realise the corporate object of the JV vehicle, except those expressly reserved by the LCC or the articles of association for the shareholders of the JV vehicles.

The members of the management body of the JV vehicle, which can also be legal entities, must:

- act with loyalty and in good faith for the benefit and in the corporate interests of the JV vehicle, exercising their duties with as much diligence and care as a reasonable person acting in the same circumstances;
- represent the JV vehicle in dealings with third parties;
- avoid any conflicts of interests; and
- exercise their mandate in compliance with, inter alia, the LCC and the articles of association of the JV vehicle.

It is possible to provide for an explicit non-compete obligation of any member of the management body. Should this member be a natural person employed by the JV vehicle, this obligation will need to be compensated financially and be limited in time and space in order not to be considered void by applicable laws.

In terms of delegation of functions, the management body of the JV is authorised to delegate certain of its functions to committees or subcommittees, depending on the legal form chosen for the JV vehicle. When committees or subcommittees are created, it is recommended that each of them has adopted a policy, rules of procedure or common charter relating to their functioning and scope of intervention.

The management body can also delegate the day-to-day management of the JV vehicle and the power to represent it in dealings with third parties to one or more persons who are not necessarily members of the management body. These individuals are referred to as "*délégué à la gestion journalière*" or day-to-day managers. Nonetheless, the liability for these delegated functions remains with the management body of the JV vehicle, which shall supervise the actions of those in charge of such delegated functions.

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7.3 Conflicts of Interest

Pursuant to the LCC, a member of the management body of the JV vehicle having, directly or indirectly, an interest of a financial nature conflicting with the those of the JV vehicle, in relation

to an operation within the competence of such management body, must disclose such conflict of interest to the other members of the management body and must not participate in the deliberation of or vote on the conflicted matter. Any conflict of interest must be recorded in the minutes or resolutions of the management body's meeting and a special report in this respect will need to be made to the shareholders of the JV vehicle at the next general meeting of shareholders before any resolution is put to the vote.

As contemplated under **6.2 Decision-Making**, it is common that a director/manager of a JV participant is appointed as a director/manager of the JV vehicle, as long as he/she performs his/her duties in the best interests of the JV vehicle and not in the best interests of the JV participant. According to case law, the mere fact that an individual holds an executive role at a JV participant does not, in itself, establish a conflicting financial interest with the JV vehicle.

8. Intellectual Property and the JV

8.1 Key IP Issues

From an IP perspective, when setting up a JV corporate entity, three main IP issues needs to be considered.

Corporate Entity

Firstly, ownership of pre-existing IP that each party brings into the JV is to be defined, as well as the terms on which the JV will be allowed to use this IP. Secondly, it is to be determined who will own the IP developed during the course of the JV and who will have the rights to use, license, and commercialise the new IP both during the life of the JV and after its termination. Thirdly, clear terms for the protection of confidential information and trade secrets exchanged between the JV partners are to be established. Finally, the conditions under which the JV can license its IP to third parties, including revenue-sharing arrangements and control over licensing decisions, are to be defined, as well as IP valuation methods, especially in order to assess how IP valuation impacts equity shares in the JV.

Contractual Collaboration

When engaging in contractual collaborations, several key IP issues should be carefully considered to ensure that the rights, obligations, and expectations of all parties are clear and protected. In particular, ownership of pre-existing and newly created IP during the collaboration is to be clearly defined, just as questions of revenue sharing and royalties are to be answered. Liability issues, if the collaboration results in the infringement of third-party IP rights, are to be addressed, along with what happens to the IP after the collaboration ends, including rights to continued use, licensing, and the return or destruction of confidential materials.

JV Agreement

IP issues are usually comprehensively addressed in JV agreements. They cover questions regarding the ownership of pre-existing IP and which usage rights are licensed to the JV and to the other party, the ownership of newly created IP and how to commercialise and exploit it, and what happens to the IP if the collaboration ends.

Moreover, in complex JVs, dispute mechanisms should be included to handle any conflicts over IP ownership, usage, or infringement. Strict NDAs ensure that all IP and proprietary information exchanged remains confidential, helping to build and foster trust within the JV.

8.2 Licensing and Assignment

When deciding whether to license or assign IP rights, it is important to conduct a thorough evaluation of the IP owner's long-term objectives, financial requirements, and strategic interests.

Licensing IP rights is ideal when the IP owner wants to retain control over the IP, continue benefiting from the IP, and is interested in long-term revenue streams. Assigning IP rights should be considered when the IP owner seeks immediate capital or wants to transfer the responsibility of managing and exploiting the IP to another party. The assignor, however, loses all control and future revenue potential from the IP.

9. ESG and the JV

9.1 ESG Regulations and Developments Affecting JVs

Even if a JV does not fall under the classification of a fund, ESG factors still warrant careful attention. Indeed, depending on the business activity of the JV and its shareholders, the structure itself will be subject to greater or lesser ESG obligations and commitments, and the JV contract will at least stipulate certain obligations in this respect (most of the time to comply with the internal policies of certain shareholders).

ESG issues may also have a greater or lesser impact on customer/supplier relations, on internal governance procedures and risk management (including sustainability risks), depending on the JV's field of activity and where this business is operated. In fact, ESG-focused evaluation criteria are increasingly being used in management incentive packages, further emphasising their growing importance. In summary, JV partners are strongly advised to adopt a comprehensive risk-based approach when establishing and operating a new JV. This entails ensuring appropriate ESG compliance and implementing a robust compliance management system that encompasses the JV, its employees, and shareholders.

If the JV vehicle qualifies as a fund, ESG topics are a must. Indeed, since the entry into force of Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial sector (SFDR), the number of ESG and impact funds has been rising. Luxembourg currently stands as the number one green financial centre in the EU. As a result of pressure from both investors and legislators, it appears certain that sustainable finance products will become a major trend in the investment funds industry in general.

Revision of the EU Disclosure Regulation

Last September, the EU Commission launched a consultation on the review of the SFDR, which ended on 22 December 2023. Some extensive changes could be made to the previous version, which has been in force since March 2021. For example, the disclosure obligations at company level in the SFDR could be removed and replaced by the obligations of Directive (EU) 2022/2464 on sustainability reporting by companies (CSRD). Additionally, the current categorisation of financial products into Article 6, 8, or 9 products may be abandoned. Shortcomings in this classification have become apparent in the past, for example from the Article 8-Plus classification created by the market for MiFID marketing. Instead, the European Commission is now considering introducing sustainability disclosure standards for all financial products. On the other hand, it is considering switching to a more differentiated classification system for sustainable products.

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ESMA Guidelines on ESG Terms in Fund Names

On 14 May 2024, the European Securities and Markets Authority (ESMA) published its final report on the use of ESG or sustainability-related terms in fund names. Accordingly, the use of ESG or sustainability-related terms in fund names is subject to certain conditions. Fund names incorporating ESG or sustainability-related terms are permissible only if at least 80% of the fund's investments consider ESG criteria or pursue sustainability objectives. In addition, it is assumed that the exclusion criteria of the Paris-aligned Benchmarks (PAB) are taken into account and that a significant proportion is invested in sustainable investments within the meaning of Article 2(17) of the SFDR in order to reflect the expectations of investors based on the fund name. The guidelines also address, for the first time, the use of transition-related terms and the combination of different terms.

Funds that are subject to supervision by the CSSF, regardless of whether they qualify as an Article 6, 8 or 9 product, must use fund denominations that are consistent with the respective investment objective and investment policy of the fund and with the ESMA Guidelines. The CSSF also expects that future developments on this topic will also be implemented at the European level.

EU Taxonomy Regulation

Since 1 January 2023, non-financial companies have had to provide evidence of the rate of conformity of their business activities with the environmental objectives of the Taxonomy Regulation as part of their reporting. However, this only applies to the environmental objectives of climate protection and adaptation to climate change. From 1 January 2024, the reporting obligation also applies to financial companies when it comes to these two environmental objectives. With regard to the other environmental objectives, however, non-financial companies fall under the reporting requirement as of 1 January 2025 and financial companies as of 1 January 2026. The implementation of the EU Taxonomy is to be facilitated by a communication on the legal interpretation and implementation of the technical screening criteria.

The Main ESG Regulations in Our Jurisdiction

The ESG regulatory framework in Luxembourg is dominated by directly applicable as well as transposed European legislation. Our main references are the SFDR, the SFDR Regulatory Technical Standards (SFDR RTS) and Regulation (EU) 2020/852 (the "Taxonomy Regulation"). This is in addition to specific guidelines provided by the CSSF.

The CSSF's current priorities with regard to ESG are essentially focused on (i) the integration of sustainability risks by investment fund managers (alternative investment fund managers (AIFMs), management companies and external portfolio managers); (ii) compliance with existing ESG-related requirements; and (iii) consistency of pre-contractual information in offering documents and on websites or as marketing material.

With regard to the consideration of sustainability risks, the CSSF emphasises that the delegation of portfolio management functions in particular has no influence on the investment fund manager obligations to disclose the consideration of sustainability risks. Accordingly, this also includes the obligation to implement an adequate risk management framework.

The CSSF will increasingly focus on verifying compliance, in particular with the ongoing disclosure obligations under Article 11 of the

SFDR in connection with Articles 50 and 58 of the SFDR RTS.

Particular attention is also paid to the increased control of the consistency of ESG-related disclosures made in pre-contractual documents (in particular offering documents with SFDR RTS annexes), websites and marketing materials.

10. Completion of the JV's Purpose, Winding Up and Redistribution of JV Assets

10.1 Termination of a JV

JV arrangements can come to an end in several ways that should be outlined in the JV agreement, the most common being:

- a deadlock situation that has not been resolved;
- at the expiry of a determined period, unless agreed otherwise between the participants to the JV;
- upon termination of the object of the JV – indeed, some JVs are only set up for the completion of a specific purpose and once completed, the JV may be terminated;
- by mutual decision of the participants to the JV;
- by any participant to the JV on contractual grounds thoroughly defined in the JV agreement – eg, breaches of certain provisions of the JV agreement, insolvency of a participant, change of control, violation of IP license agreement, failure to meet a funding obligation following an unsuccessful cure period; or
- poor performance of the JV.

A JV vehicle can also be dissolved by the Luxembourg courts in accordance with the LCC.

Contemplating the consequences of the termination of the JV is crucial. The main general matters that should be dealt with in this respect notably concern:

- settlement of liabilities;
- assets allocations;
- employment issues;
- IP issues;
- survival clauses from the JV agreements; and
- de-registration from the RCS if the JV is a registered entity.

The JV agreement can provide that the termination of the JV does not trigger the termination of the JV vehicle. As a separate legal entity, transfer of shares or liquidation of the JV vehicle should also be contemplated.

10.2 Transferring Assets Between Participants

When contemplating the transfer of the assets owned by the JV to the JV participants, whether they have been originally contributed to the JV vehicle by the JV participants or whether they directly originate from the JV, the following main issues should be addressed:

- Assets valuation: The valuation of the assets to be transferred is generally determined in accordance with the calculation method provided for directly in the JV agreement.
- Contractual restrictions over the assets: Depending on the nature of the assets, it must be ensured that the asset to be transferred is free from any encumbrances or third-party rights that would prevent the transfer (eg, mortgages, pledges over shares, limitation to the transferability of IP rights).
- Nature of the assets: Fulfillment of legal registration requirements may be triggered by the

transfer of certain assets (eg, IP rights, real estate).
- Corporate interest: The management body of the JV vehicle must ensure that the transfer of assets contemplated is in the best interests of the JV, either from a corporate perspective or from a business perspective, when assessing the impact of such transfer on the modus operandi of the JV. The decision to transfer assets of the JV to its participants can require the further approval of an ad hoc committee beforehand or the shareholders of the JV vehicle.

The transfer of assets from the JV to its participants is a scenario that is worth contemplating in advance directly in the JV agreement.

Trends and Developments

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GSK Stockmann SA is a leading independent European corporate law firm with more than 250 professionals across offices in Germany, Luxembourg and the UK. It is the law firm of choice for real estate and financial services, and also has deep-rooted expertise in key sectors such as funds, capital markets, public, mobility, energy and healthcare. For international transactions and projects, GSK Stockmann works together with selected reputable law firms abroad. In Luxembourg, it is the trusted adviser of leading financial institutions, asset managers, private equity houses, insurance companies, corporates and fintech companies, with both a local and international reach. The firm's lawyers advise domestic and international clients in relation to banking and finance, capital markets, corporate/M&A and private equity, investment funds, real estate, regulatory and insurance matters, as well as tax.

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Joint Venture Agreements in the Grand Duchy of Luxembourg

A successful and efficient joint venture (JV) requires careful planning. One of the first steps for the parties is selecting the jurisdiction where they intend to set up the JV vehicle. The choice of such jurisdiction may vary on the basis of the features of the envisaged project, for example, fiscal reasons, the legal framework and the asset location as well as specific preferences of the parties, such as official language, effectiveness of the judicial system, economic stability, access to financial institutions and the regulatory environment.

The Grand Duchy of Luxembourg is considered by many as one of the most attractive jurisdictions to establish a JV vehicle. It offers not only a flexible legal framework but also a stable political and economic environment, consistently recognised by its enduring AAA credit ratings. Moreover, its deeply international character confers numerous advantages upon the parties involved. In particular, it is standard practice in Luxembourg for the transaction and corporate documents of a joint venture to be drafted in English.

When parties choose to incorporate a joint venture in the Grand Duchy of Luxembourg, it is both customary and advisable to first establish a term sheet outlining the key aspects of their economic relationship. This precedes the drafting of a more comprehensive joint venture agreement. Additionally, a crucial consideration in forming a JV is to address not only the initial establishment and business plan but also the various phases of the Luxembourg-incorporated entity's life cycle, including a tax-efficient exit strategy.

While there is no one-size-fits-all answer, market practice highlights several key considerations that parties should be particularly mindful of during negotiations:

- the JV shareholding;
- the management of the JV;
- the governing law of the JV agreement;
- the relationship between the JV agreement and the articles of association of the JV vehicle;
- the potential qualification of the JV vehicle as alternative investment fund; and
- the foreign investment control mechanism applicable in the Grand Duchy of Luxembourg.

However, any consideration of these aspects differs depending on the type of company or partnership selected. This article will focus on Luxembourg private limited liability companies (*sociétés à responsabilité limitée* – SARL), which is one of the most commonly used type of entity for JV vehicles due to the flexibility of its rules. However, there are several other suitable types of company forms that could be used for a JV vehicle, such as public limited liability companies (*sociétés anonymes*), simplified stock companies (*sociétés par actions simplifies*) or common/special limited partnerhips (*sociétés en commandite simple/spéciale*).

The Shareholding of the JV Vehicle

Once the purpose, target(s), and objective of the JV are clear, one of the initial points for discussion among the parties is the investment structure and governance within the JV vehicle. The parties must consider questions such as the proportion of debt and equity to be invested, the number of shares each shareholder will hold that confer voting rights and influence in the JV, and what each party will contribute to the venture. These negotiations are crucial, as they define the balance of power between the shareholders.

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Luxembourg law offers various possibilities for structuring shareholding arrangements effectively. While a comprehensive analysis of all options is beyond the scope of this article, the focus of this section will be on key potential scenarios concerning (i) the type of financial instruments used; (ii) the nature of contributions made by the parties; and (iii) how these contributions are allocated.

Type of instruments

The share capital of a SARL is generally divided into shares (*parts sociales*), which may or may not have a nominal value. The subscription of such shares by the shareholders entitles them to economic rights, such as preferred distributions, dividends, liquidation proceeds and non-economic rights, such as voting rights, and observer and board member appointment rights, which are, as a general rule, proportionate to the number of shares held.

While this is the general structure, JV parties often require a more complex structuring to achieve their purposes. For example, minority shareholders may insist on having specific protection rights in order to better safeguard their interests. Luxembourg law offers several possibilities in this respect. One possibility is the use of shares with different share classes – eg, class A and class B shares. In such case, each shareholder may subscribe for a different class of share and different rights may be granted to each class.

In terms of distribution rights, the structure with different classes of shares also offers the possibility of granting a right of preference in case of distributions. Such right of preference may be structured on a waterfall or case-by-case basis, for example with view to specific IRRs achieved.

In terms of voting rights, the structure with different classes of shares may be particularly useful for minority shareholders. It is in fact common to include a list of important matters for the management of the joint venture vehicle, the so-called reserved matters, and to submit the approval of such matters to specific majorities or the approval of one class of share independently of the amount of shares held. For example, the JV agreement may provide that the majority necessary to approve a merger of the JV vehicle needs to include the favourable vote of shareholders representing the majority, or the totality, of the class of shares held by the minority shareholder(s).

Beyond shares, Luxembourg law offers also the possibility of issuing beneficiary or profit units (*parts bénéficiaires*). Beneficiary units are instruments that can be issued by the company but do not form part of its share capital. The features of this instrument are therefore highly flexible, and can be freely defined in the articles of association of the JV company.

The contributions

Once the structure of the share capital of the joint venture vehicle is outlined, the parties need to consider the means of the initial contributions to be made into the JV vehicle. Generally, contributions into an SARL are made in cash or in kind by contributing receivables or shares in other companies. The contribution in cash is the easiest way to contribute value, but some practical implications need to be considered. When incorporating an SARL in the Grand Duchy of Luxembourg in cash, the minimum corporate share capital of EUR12,000 needs to be transferred to a bank account of the company before it is incorporated and legally existing. This requires opening a bank account for the future company with a Luxembourg or foreign bank. In some jurisdic-

tions, financial institutions are unable to open bank accounts for future companies and assist with the formation process. The bank onboarding process for opening an account needs to be taken into account, in particular in terms of timing and documents to be provided, as this may delay the envisaged timeline to set up the joint venture vehicle.

The allocation: share capital, share premium, account 115

Once the JV partners have decided how to contribute the value to the JV vehicle, they will need to decide how to allocate such value. If the shares are subscribed at their nominal value, the contributed value will be fully booked to the share capital of the JV vehicle. However, if one or more shareholders subscribe for shares at a price higher than the nominal value, the share premium needs to be allocated to one of the accounts of the JV vehicle. If new shares are issued, such additional value will be booked to the share premium account of the company. In Luxembourg, shareholders have, however, the flexibility to contribute such additional value to the capital reserve of the company, the so-called account number 115 of the Luxembourg standard chart of accounts (*apport en capitaux propres non rémunérés par des titres*). A contribution to the account 115 can be swiftly done, because it does not require the involvement of a notary.

The Management of the Joint Venture Vehicle

Once the debt/equity contributions are structured, the JV parties often then negotiate and agree upon the management structure of the JV company. Under Luxembourg law, the management of a SARL is generally entrusted to a board of managers, since a sole manager is unusual for JVs. The board of managers considers and approves the actions of the company in accordance with, inter alia, its corporate object and its corporate interest.

The appointment of the managers

The members of the board of managers are appointed by the shareholders of the company, either in connection with the incorporation of the JV before a Luxembourg notary, at a subsequent general meeting of shareholders or by means of written shareholder resolutions. Under Luxembourg law, the individual shareholders only have a nomination right, but not an appointment right. This means that JV parties cannot agree in the JV agreement that one shareholder alone can directly appoint, without a shareholders' resolution, one or more manager(s). In practice, the JV parties therefore provide in the JV agreement for the right of a shareholder to nominate a specified number of future managers. This is coupled with an undertaking from all other shareholders to appoint the managers so nominated by way of a shareholder resolution. If certain shareholders do not have the right to nominate a manager, under Luxembourg law it is also possible and common to appoint an "observer" to the meetings of the board of managers. An observer is not a manager and is therefore not entitled to vote in favour or against any resolution. However, an observer usually has the right to receive the relevant documentation presented in the board meetings and is entitled to attend.

The majorities

Once the principles of the composition of the board of managers are agreed, the JV parties normally then negotiate the board of managers' quorum and majorities for approvals. As a general rule, the board of managers can validly meet if at least half of the members are present or represented, while board resolutions can be approved with the favourable vote of at least half of the managers attending the meeting.

Luxembourg law offers certain flexibility in this respect. A very common structure used in the context of a JV agreement is the organisation of the managers by different classes – eg, class A and class B managers. The JV agreement may provide that a meeting of the board of managers is validly constituted only if at least one manager from a certain class is attending. Similarly, it is possible that a resolution can be approved only with the favourable vote of at least one manager of each class or that only one class A and one class B manager may represent jointly the company vis-à-vis third parties.

This structure can be particularly useful from a minority shareholder perspective, as minority shareholders usually have the right to nominate only one manager. A board of managers divided into different classes may thus permit the manager nominated by the minority shareholder to have a "veto" right on certain matters or prevent one manager from entering into agreements with third parties without the knowledge of the managers appointed by the other JV parties.

The Governing Law of the JV Agreement

A JV agreement regulating a Luxembourg SARL does not necessarily need to be governed by Luxembourg law. The parties may choose a different governing law based on their preferences, for example, because they have a preference for the provisions of their home jurisdiction or because the main assets of the JV are located in a different country.

Despite the fact that the choice of the governing law is in principle free, submitting the JV agreement to a law other than Luxembourg law has several implications. First and foremost, such choice will not change the fact that the JV vehicle is a Luxembourg-established entity and therefore subject to the applicable rules and regulations of the Grand Duchy of Luxembourg.

As a result, it is essential that the JV agreement, if submitted to another law, is carefully reviewed from a Luxembourg perspective too, in order to ensure that its provisions are fully compliant with Luxembourg law.

By way of example, Luxembourg corporate law provides that the shares of a SARL may be transferred inter vivos to non-shareholders only with the favourable vote of shareholders representing at least 75% of the share capital. It may happen that the JV agreement, submitted to another law, provides that the shares in the JV company are transferrable in line with the permitted transfer provision and usual tag-along, drag-along and RoFR provisions, omitting this formal aspect.

The Relationship Between the Joint Venture Agreement and the Articles of Incorporation

When assisting with Luxembourg JV transactions, a common point of discussion is to what extent the provisions of the JV agreement shall be implemented into the articles of association of the JV vehicle.

The JV agreement is a contract and, in general, is confidential and binding only on the parties that signed it. However, the notarial deed incorporating the SARL is published in the Luxembourg Trade and Companies Register (*Registre de Commerce et des Sociétés*) and is therefore publicly accessible by anyone. Unlike the JV agreement, the articles of association of the company are enforceable on all (the so-called erga omnes effect).

The JV parties thus need to find a balance between confidentiality and erga omnes efficacy, by deciding to what extent the provisions of the

JV agreement should be transposed into the articles of association of the JV vehicle. Usually, the articles of association do not replicate in length JV provisions, but are limited to the most important ones regarding restricted transferability of the shares, the management of the company and distribution rules.

The Qualification as Alternative Investment Funds

A JV vehicle, if certain requirements are met, may be qualified as an alternative investment fund. As a consequence, such JV vehicle will need to be compliant with the provisions of Luxembourg law on alternative investments funds. In order to clarify the status of the joint venture vehicle, the parties should carefully analyse with their advisers if the joint venture vehicle is really a pure corporate structure or meets the requirements for being considered as an alternative investment fund, which can be the case, inter alia, if it raises capital from a certain number of investors, with the aim of investing the capital for their benefit and pursuant to an investment policy.

The Luxembourg Foreign Investment Control Mechanism

In September 2023, a screening mechanism for foreign direct investments was introduced in the Grand Duchy of Luxembourg. If the investment in a company established in the Grand Duchy of Luxembourg meets the relevant requirement, the investor will be required to notify the transaction to the Ministry of Economy (*Ministère de l'Économie*) in Luxembourg, which will evaluate it and provide its approval or denial on a case-by-case basis.

An investment is subject to the mandatory notification if it is made:

- by a foreign investor – ie, a physical person which is not a national of, or an entity that is not incorporated/established under the laws of a EU member state or a country which is part of the European Economic Area:
  - (a) into a company established under Luxembourg law which operates in certain critical areas – eg, energy, transportation, health, communication, etc; and
  - (b) which enables such investor to control the Luxembourg company 0 eg, to have more than 25% of the voting rights of such company, to have the majority of the voting rights (also by means of an agreement between shareholders) of such company, to have the right to appoint or remove the majority of the board of managers (and at the same time be a shareholder of such company), etc.

The parties to a JV agreement should thus carefully analyse the features of their JV in order to clarify if there is a need to proceed with the notification to the Luxembourg Ministry of Economy.

Conclusion

This article outlined some of the main aspects that are usually considered and negotiated by the parties when planning a JV involving a JV vehicle established in the Grand Duchy of Luxembourg. The list and content of topics are not exhaustive and the JV parties need to observe a number of economic, legal and tax aspects on the basis of the envisaged project.

While negotiations may seem lengthy and challenging, well-structured and thoroughly negotiated JV agreements are crucial in ensuring that the JV operates efficiently. Luxembourg's legal framework is frequently selected as it provides a favourable environment that can contribute to the smooth functioning of the JV.

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