contrast

NEW CODE OF COMPANIES AND ASSOCIATIONS

IN A NUTSHELL

#6

Cap on director liability: *much ado about nothing*?

Directors are responsible for the proper fulfilment of their tasks and can be held personally liable, by the company and (in some cases) by third parties, for shortcomings in their management.

Under our current company laws, a director's liability is, in principle, a personal and individual matter. In some circumstances, however, directors can be held jointly and severally liable, for instance in the event of a violation of the current Companies Code or the company's articles of association. In such situations, each member of the governing body can be sued for the full amount of the damage.

Furthermore, the liability of directors today is essentially unlimited, both *vis-à-vis* the company as well as third parties.

By contrast ...

A new common director liability regime will be introduced for all types of companies and associations, of which the most remarkable aspect is perhaps a "cap" on director liability. For certain faults, the possible liability of directors can from now on indeed be limited to a maximum amount.

But what exactly is the impact of this new liability regime and "cap"?

Below you will find the key takeaways.

- **Joint and several liability becomes the rule**. Under our current corporate laws, a director's liability is in principle personal and individual, except in particular circumstances. In the new Code, joint and several liability will become the default rule. In principle, directors shall be jointly and severally liable for management faults if they are a member of a collegial governing body, and, in any event (even if no collegial governing body is installed), if a violation of the new Code or the articles of association is committed. In such events, each director can thus be sued for the full amount of the damage. An individual director can only avoid such joint and several liability, provided that he/she (i) has not taken part in the fault and (ii) has reported such fault to the board of directors or the other directors if no board is installed (and no longer to the general shareholders' meeting as is required today).

- **Limited judicial review confirmed**. The new Code confirms that a court should exercise restraint when reviewing the acts or decisions of directors (*marginale toetsing*/*principe de l'appréciation marginale*). Directors can indeed only be held liable if their decisions or acts are manifestly outside the margin within which reasonably prudent and careful directors, placed in the same circumstances, could reasonably disagree.

- **"*De facto*" directors can now also be held liable**. The new Code stipulates that also "*de facto*" directors, persons exercising the tasks and responsibilities of a director without officially being appointed as director, can be held liable for management faults.

- **Insolvency-related grounds for director liability relocated to Economic Law Code / new liability ground for "wrongful trading"**. The specific grounds for director liability in the context of insolvency have been relocated from our current Companies Code to Book XX of the Economic Law Code. This concerns, in particular, the possible joint and several liability of directors for all or part of the company's debts, if it is established that their manifest gross fault (*kennelijke grove fout/faute grave et caractérisée*) has contributed to the company's bankruptcy (which liability ground was previously included in articles 265, 409 and 530 of the Companies Code). The most significant change in this respect, however, is the introduction in the same Book XX of the Economic Law Code of a new ground for director liability for "wrongful trading" in the event of bankruptcy. This ground for (possible joint and several) liability may apply in the event that it is established that the directors knew (or should have known) at any time before the bankruptcy that there was manifestly no reasonable perspective that a bankruptcy could be avoided and the directors nevertheless did not act as normally prudent directors in that situation.

- **Cap on director liability**. The most notable innovation of the new liability regime, is that the directors' liability is from now on limited to a maximum amount. A similar liability cap already exists for the statutory auditor, which served as an inspiration for the new cap on director liability. The amount of the cap depends on the size of a company, based on the turnover and balance sheet total (calculated over the last 3 financial years). The cap amount ranges from

125,000 euros for the smallest companies to 12 million euros for the largest companies and public interest entities ("*organisaties van openbaar belang*"/"*entités d'intérêt public*"). The cap is an aggregate cap that applies to all directors jointly, regardless of the number of claimants, and concerns each individual fact but also a combination of facts that gives rise to a liability. The cap covers any type of liability, both *vis-à-vis* the company as well as third parties.

- **Exceptions to liability cap**. The cap will not apply in case of fraudulent intent (*bedrieglijk opzet*/*l'intention frauduleuse*) or intent to cause harm (*oogmerk om te schaden*/*à dessein de nuire*). Due to a last minute amendment of the new Code, the cap will moreover not apply in case of gross negligence (*zware fout*/*faute grave*) and repeated minor faults (*lichte fout die eerder gewoonlijk dan toevallig voorkomt*/*faute légère présentant dans leur chef un caractère habituel plutôt qu'accidentel*). Concretely, directors will therefore only be able to successfully rely on the cap in the event of a minor accidental fault (*lichte toevallige fout*/*faute légère occassionnelle*). The cap also does not apply in the event of a breach of particular indemnification obligations included in the Code (*e.g.* a director's indemnification obligation in the event of an invalid subscription to a capital increase). Furthermore, the cap cannot be relied upon in respect of liabilities *vis-à-vis* the National Social Security Office (for unpaid social security contributions) or the tax authorities (for unpaid VAT or withholding tax).

- **No further limitations of directors' liability allowed**. The directors' liability may not be further limited than the amounts of the cap. In addition, the new Code explicitly prohibits a company to exempt or hold harmless its directors in advance from their liability. This is also forbidden for the company's subsidiaries, but not for third parties, such as its shareholders or insurers.

The new cap on director liability is noteworthy and is designed to improve the predictability of a director's liability in order to facilitate D&O insurance and the appeal of a director mandate in a Belgian company. However, in view of the significant exceptions to the cap, directors should be warned that the cap may not protect them in all situations.

The new director liability regime and the cap will apply to all legal entities, thus also to not-for-profit entities. Keep an eye out for our next "In a Nutshell" newsletter for more information on the new Code's other innovations for not-for-profit entities.

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