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Corporate Governance in the Netherlands

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1. General Information on Corporate Governance in the Netherlands

The corporate governance system in the Netherlands has witnessed important changes over the last decade. Following a very public debate about the maintenance of the wide arsenal of defensive measures against takeovers in the first half of the 1990s, a first attempt was made to produce corporate governance recommendations for listed companies. The 40 recommendations of the Peters Committee, published in 1997, triggered general awareness of corporate governance questions.

The discussions on corporate governance were held against the background of the Dutch corporate law system that imposes a stakeholder rather than shareholder orientation of executive and supervisory boards of companies. The Dutch corporate law system includes distinct elements of employee co-determination: far-reaching works council powers and the Dutch structure regime for large companies, allowing employees to have a say in the appointment of supervisory directors. Dutch corporate law also, in general, allows a wide-ranging set of mechanisms that can be used to not only defend companies against hostile takeovers, but also substantially reduce shareholders' involvement in corporate affairs under normal circumstances, including non-voting depositary receipts for shares, priority shares with special control rights, and structural delegation of authorities to the executive board.

The 40 recommendations of the Peters Committee heralded a fundamental overhaul of Dutch corporate law to restore the position of shareholders, through a combination of changes in 2004 to Book 2 of the Dutch Civil Code (DCC), containing the companies act, a Corporate Governance Code issued by the Tabaksblat Committee in 2003 and case law of the Enterprise Chamber of the Amsterdam Court of Appeal (the *Enterprise Chamber*). This court has broad authority to order investigations into the affairs of companies and to order immediate measures to be taken for the duration of the proceedings.

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The 2004 changes of Book 2 DCC included:

- (i) the introduction of the authority of the shareholders meeting to approve major transactions that will have a material impact on the nature of the company, including acquisitions or divestures of a value exceeding one-third of the company's balance sheet total;
- (ii) the right of shareholders holding 1% of share capital or shares with a market value of € 50 million, to submit items for the agenda of the general meeting;
- (iii) the right of holders of depositary receipts for shares to receive a power of attorney to vote on the underlying shares, which can be refused when the company is or will become subject to a takeover threat;
- (iv) the right of the general meeting to adopt the remuneration policy for executive directors and to specifically approve share-based schemes; and
- (v) the right of the general meeting of companies governed by the structure regime to appoint supervisory directors (who previously appointed themselves) and to dismiss the supervisory board as a whole.

Application of the 2003 Corporate Governance Code through a comply-or-explain mechanism was made mandatory in a Royal Decree as of 2004 for Dutch companies with a share listing. The Code was adopted by a committee chaired by Mr. Tabaksblat, consisting of representatives of listed companies, shareholder associations (both retail and institutional) and independent governance experts, which committee was set up by relevant associations of business and shareholders. The acceptance of the Code was helped by corporate governance scandals in 2003, the most prominent of which were the misleading financial statements issued by Royal Dutch Ahold and the oil reserves statements of Royal Dutch Shell.

The Corporate Governance Code includes principles that are held to be generally accepted and detailed best practice provisions on the executive board (key issues: risk management and executive remuneration), the supervisory board (key issues: increased monitoring commitment, committees, independence), the general meeting (call to institutional investors to use their voting rights, procedure), and the auditing process and external auditor. A Monitoring Committee was set up following the adoption of the Code. This Committee has issued annual monitoring reports, reflecting on the level of compliance with the Code. In 2008, the Monitoring Committee also adopted a set of revisions to the Code.¹

In the same period, securities regulation for listed companies has changed fundamentally. Prior to 1990, securities regulation was primarily a self-regulatory affair, with a minimum of rules promulgated by the Amsterdam Stock Exchange. In the 1990s, more and more mandatory rules were introduced into this system, first of all with the introduction of criminal prohibitions on insider trading and notification obligations for substantial holdings. As of 2000, the self-regulatory system was completely overhauled and replaced by mandated securities regulation, of which the core can now be found in the Act on Financial Supervision (*Wet financieel toezicht*; 'AFS') and decrees issued under this Act.

The supervision of compliance with securities regulation, and general supervision of conduct on financial markets, has been delegated to the *Autoriteit Financiële Markten* (AFM), a private body with public law powers of investigation that may also levy administrative fines for non-compliance. The AFM's authority ranges from investigating insider trading and notification of substantial holdings, approving prospectuses for securities issues and offer

¹ The current Corporate Governance Code is available at <http://www.commissiecorporategovernance.nl/page/downloads/DEC_2008_UK_Code_DEF_uk_.pdf>.

documents for public offers as well as supervising the offer procedure to reviewing financial statements of companies with listed securities and supervision of trading on the Euronext Amsterdam exchange, including suspension of trading. Most of the decisions of the AFM are subject to appeal before the administrative court in Rotterdam, which has resulted in the AFM operating in a litigious environment.

Share ownership of listed companies in the Netherlands is mainly dispersed, with a relatively low number of controlling shareholders. Recent numbers indicate that as many as 70% of the shareholders of Dutch listed companies are foreign shareholders. This has made Dutch companies particularly vulnerable to shareholder activism by hedge funds, as seen in the cases of Stork, ASMI and ABN AMRO. In these cases, the Enterprise Chamber intervened with immediate measures mostly to preserve the status quo and allow for an orderly process of debate and conflict resolution. The financial crisis has strengthened sentiments in the media and among politicians that the movement to restore shareholder rights has gone too far, and that this should be curbed since this has made companies subject to excessive short-term activist pressure from certain shareholders. The government has submitted proposals to parliament that seek to increase the transparency provided by investors by lowering the threshold for notification of substantial holdings from 5% to 3% and requiring notifying shareholders to state whether they object to the strategy of the company.² More fundamental revisions have not been announced to date.

2. Internal Corporate Governance

2.1. Boards

2.1.1. One-tier and two-tier Models

Dutch listed companies predominantly apply the two-tier board system, comprising a management board and a supervisory board. This is the classical Dutch board system that can be traced back to the first listed company in the world, the VOC, incorporated in 1602 and that introduced a form of a supervisory board in 1623 following shareholder pressure to improve the company's governance.

The two-tier model is required for companies governed by the structure regime, in which case the employees, through the works council, have the right to nominate candidates for one-third of the members of the supervisory board (see section 2.3.2, below for further information). Most large listed companies are exempt from the structure regime, as a result of which they may opt for a one-tier board. Of the larger listed companies only one has actually adopted the one-tier board, Unilever N.V.

An amendment to Book 2 DCC, which is currently being discussed in parliament, will further facilitate the introduction of the one-tier model, mainly by clarifying that a company's articles of association may distinguish between the roles of executive and non-executive directors, thus also affecting directors' liability.³ The proposed amendment also allows for companies governed by the structure regime to adopt a one-tier board, in which case the co-determination rights of the works council relate to the appointment of non-executive directors. The Corporate Governance Code contains some provisions on the one-tier board, stipulating that the majority and the chairman of the board must be non-executive members.

² Bill amending the AFS, The Act on Transfers of Securities by Giro and Book 2 DCC, *Parliamentary Proceedings II* 2008/09, 32 014, No. 2.

³ Bill amending Book 2 DCC, *Parliamentary Proceedings II* 2009/10, 31 763, No. A.

In practice, the operation of a one-tier and a two-tier board in a Dutch setting may not differ fundamentally. The one-tier board is often associated with a higher number of meetings of the board, more extensive information to non-executives and in general in stronger involvement of non-executive directors. However, all of this can be achieved without any formal difficulty in a two-tier model. The differences appear to exist more in perception than in legal reality. The liability of non-executive directors in a one-tier board is unlikely to differ fundamentally from the liability of supervisory directors in a two-tier board. In the remainder of this paragraph we primarily refer to the two-tier model, as this is the predominant model.

2.1.2. Composition, Size, Term of Office

Book 2 DCC contains little on the composition, size and term of office of the supervisory board. The sole mandatory provision is that only natural persons can be appointed as supervisory directors (Article 140 Book 2 DCC). The Corporate Governance Code provides that a profile of the composition of the board is to be made and that the supervisory board is to aim for a diverse composition in terms of gender and age. The profile is to state what specific objective is pursued by the supervisory board in relation to diversity. Currently, proposals are being debated in parliament to impose a 'comply or explain' provision in the DCC, holding that companies should fulfil a quota of at least 30% women supervisory directors.⁴

The size of the supervisory board is not regulated, apart from companies governed by the structure regime, in which case the minimum size of supervisory board is three members. Typically, supervisory boards range from three to nine members. Larger boards are rare.

The Corporate Governance Code provides that a supervisory director may hold office for a maximum of three four-year terms.

Supervisory directors are typically appointed and re-appointed on the basis of a rotation scheme. Systems of staggered board elections, as far as we are aware, are not applied by listed companies. Instead, listed companies often contain provisions in their articles of association that members of the management board and of the supervisory board can only be dismissed by the general meeting upon the proposal of the supervisory board, or that they can only be dismissed by the general meeting with a majority of two-thirds of the votes cast. Following a provision in the Corporate Governance Code, such provisions have often been replaced by a provision that dismissal is possible on the basis of an absolute majority representing at least one-third of share capital.

2.1.3. Task, Orientation

Article 140 Book 2 DCC expressly provides that the supervisory board is to act in the interest of the company and its enterprise, which is understood to mean to act in the interest of all stakeholders. Case law, among which the recent decision of the Supreme Court in *ABN AMRO*,⁵ confirms that the interests of shareholders do not take priority over the interests of other stakeholders.

⁴ Amendment Kalma et al., *Parliamentary Proceedings II* 2009/10, 31 763, No. 8.

⁵ Supreme Court 13 July 2007, *JOR* 2007, 178.

The duties of the supervisory board are to advise and supervise the management board (Article 140 Book 2 DCC). These duties are elaborated in the Corporate Governance Code. According to the Code, the supervision of the management board at least includes:

- (i) achievement of the company's objectives;
- (ii) corporate strategy on the risks inherent to the business activities;
- (iii) the design and effectiveness of the internal risk management and control systems;
- (iv) the financial reporting process;
- (v) compliance with primary and secondary legislation;
- (vi) the company-shareholder relationship; and
- (vii) corporate social responsibility issues that are relevant to the enterprise.

In addition, the supervisory board is typically charged with setting the executive remuneration under the policy adopted by the general meeting.⁶ Also, supervisory directors are often charged to represent the company when a managing director has a conflict of interests with the company.⁷

In companies governed by the structure regime the supervisory directors are authorised to approve major decisions of the management board, such as large acquisitions or disposals and issuance of share capital.⁸ Similar approval rights are typically also included in the articles of association of companies not governed by the structure regime.

2.1.4. Operation

Book 2 DCC to date does not contain any mandatory rules on the operation of the supervisory board. The Corporate Governance Code contains a number of best practices related to committees, the role of the chairman, induction of new board members and board evaluation. The Corporate Governance Code provides that companies are to have three committees: audit, remuneration and nomination. The function of these committees is to prepare decision-making by the full supervisory board. The committees, therefore, do not have separate powers and do not reduce the responsibility of the full board for these matters.

The audit and remuneration committees may not be chaired by the chairman of the supervisory board (in order for the discussion in the full board to be relevant) or a former member of the management board. In practice, the remuneration and nomination committees are sometimes combined. The audit committee has been made mandatory for listed companies by means of a governmental decree,⁹ as a result of the implementation of the European Statutory Audit Directive.¹⁰

The chairman of the supervisory board ensures a proper functioning of the supervisory board and its committees, ensuring that (i) supervisory directors receive sufficient and timely information, (ii) there is sufficient time for consultation and decision-making by supervisory directors, and (iii) the performance of management board and supervisory board members are assessed annually. The chairman also functions as the main contact for shareholders regarding

⁶ Art. 135 Book 2 DCC.

⁷ Art. 146 Book 2 DCC.

⁸ Issuance of share capital in principle is a shareholder decision but the general meeting can delegate this decision to the management board for a period of up to five years, in which case the decision to issue share capital is often subject to the approval of the supervisory board.

⁹ Decree of 26 July 2008, *Staatsblad* 2008, 323.

¹⁰ Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/ 660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC (*OJ L* 257).

the functioning of the management and supervisory boards. The chairman should not be a former member of the management board. The Corporate Governance Code also provides that a vice-chairman is to be appointed who will replace the chairman when he is absent and who also acts as the main contact for management and supervisory board members concerning the performance of the chairman.

The supervisory board must discuss at least once a year, in a meeting without the executives present, its own functioning and that of the management board. The supervisory board's report in the company's annual report must include how its evaluation has been carried out. There is a growing practice for boards to have evaluations conducted by external agencies at least once every three to four years.

As to information, the Corporate Governance Code provides that the supervisory board and its individual members each has his own responsibility for obtaining from the management board and the external auditor all information the supervisory board needs to properly fulfil its oversight duties. If the supervisory board considers it necessary, it may obtain information from officers (beyond the management board) and external advisors of the company, and may require them to attend meetings.

2.1.5. Independence

The Corporate Governance Code is rather strict on the issue of independence of supervisory board members. All members of the supervisory board must be independent, save for one member, according to the list of independence criteria included in the Code. The independence criteria exclude, among others, employees or members of the management board for a period of five years prior to appointment to the supervisory board, those with an important business relation to the company during the year prior to appointment (including in-house counsel, external auditor, banker), a member of the management board of a company where a member of the management board is a supervisory director, a holder of ten percent or more of the company's shares, or a board member of a company holding ten percent or more of the company's shares, unless such holding company is a group company. Also, for supervisory board committees, the Code provides that only one member may be non-independent according to these criteria.

2.1.6. Audit, Control, Risk Management

The Corporate Governance Code includes extensive provisions on internal control and risk management, and audit. The internal control and risk management system is to at least include:

- (i) risk analysis of the operational and financial objectives of the company;
- (ii) a code of conduct to be published on the company's website;
- (iii) guides for the lay-out of financial reports and procedures to be followed in drawing up the reports; and
- (iv) a system of monitoring and reporting.

The management board must describe in the company's annual report the main risks related to the strategy of the company, the design and effectiveness of the risk management and control systems for the main risks during the financial year, any major failure in these systems observed in the financial year, and any improvements made to the systems as a result. In addition, the management board must also state, concerning financial reporting risks, that the internal risk management and control systems provide reasonable assurance that the financial

reporting does not contain any errors of material importance and that these systems worked properly in the year under review, all with clear substantiation. The supervisory board, and specifically the audit committee, is to supervise all of this.

The external auditor is appointed by the general meeting. The supervisory board nominates a candidate for appointment on the advice of the audit committee and the management board. The supervisory board also decides on non-audit services to be provided by the external auditor, on the recommendation of the audit committee and after consultation with the management board. The external auditor should be present at the general meeting and may be questioned by shareholders.

2.1.7. Duty of Loyalty, Conflict of Interest

Dutch law does not contain an explicit duty of loyalty applicable to the members of the management and supervisory boards. However, the core instruction to act in the interests of the company and its enterprise can certainly be understood to mean that no director should be guided by his or her own interests. The Corporate Governance Code has increased the responsibility of dealing with conflicts of interest. For both management and supervisory board members, there are provisions in the Code to the effect that a board member with a personal, direct or indirect conflict of interest may not participate in the debate and decision-making of the board on the relevant subject matter, as is discussed in detail below. The Netherlands Supreme Court held these provisions to be mandatory as a matter of law in *Versatel*, also discussed in detail below.¹¹ The proposal now pending in parliament introducing new rules on the one-tier board also provide for a mandatory provision that managing and supervisory directors may not participate in the debate and decision-making when they have a personal, direct or indirect conflict of interest with the company.

2.1.8. Business Judgment Rule, Standard of Care

The US style business judgement rule does not exist as such in the Netherlands. But it is clear from case law on liability that managing and supervisory directors have a natural discretion in performing their duties. Liability only arises when a director has performed his duties improperly, for which serious personal culpability must be established. There will be an improper performance of duties if a director acted in a way that no reasonable director in similar circumstances would have acted. This standard has been lowered from gross negligence in the 1980s.

The standard applied in inquiry proceedings by the Enterprise Chamber as to whether to grant an inquiry is that there must be sound reasons to doubt the proper policies of the company and/or the conduct of its business (*gegronde redenen om aan een juist beleid te twijfelen*). If the Enterprise Chamber, after inquiry by experts, finds that there has been mismanagement (*wanbeleid*), it is authorised take certain measures, including dismissal of directors. In deciding whether or not there has been mismanagement, the Enterprise Chamber reviews whether elementary principles of responsible entrepreneurship have been breached (*elementaire beginselen van verantwoord ondernemerschap*). All of these terms again suggest a level of discretion for managing and supervisory directors in performing their duties.

¹¹ Netherlands Supreme Court 14 September 2007, *JOR* 2007, 237.

2.1.9. Remuneration

The remuneration of supervisory directors is typically decided by the general meeting. There are no mandatory rules or limitations on this remuneration. The Corporate Governance Code provides that supervisory directors may not be granted shares or stock options as a form of remuneration. Shares held by supervisory directors should be held for the long term. The company may also not extend personal loans or guarantees to supervisory directors unless in the normal course of business.

The remuneration of managing directors in practice is determined by the supervisory board within a policy adopted by the general meeting.¹² Stock option schemes and other share-based incentive schemes require the specific approval of the general meeting. In practice, many listed companies remunerate their managing directors through a combination of fixed pay, cash bonus, stock options or long-term incentive share grants. In addition, pension contributions are often substantial. The pay of individual directors must be disclosed in the annual accounts.¹³

The Corporate Governance Code contains a number of provisions on executive remuneration, focused mainly on process and transparency. One significant provision is that the severance payment of a managing director after his dismissal may not exceed his fixed annual pay. The relation between fixed and variable pay should be reasonable, but recent recommendations for banks in a separate Code for Banks include that variable pay should not exceed fixed pay.¹⁴

2.1.10. Liability

Liability of directors under Dutch law is primarily liability towards the company. Managing and supervisory directors are liable towards the company if they have improperly performed their duties. Liability only arises if there is serious personal culpability that can be attributed to a director. In such case, the director or directors are liable for the damages caused to the company.

Shareholders cannot sue directors directly for losses they have incurred as a result of damages caused to the company. Moreover, shareholders are unable to file a derivative suit for those damages on behalf of the company. Shareholders are able, however, to claim damages from managing and supervisory directors when the company has published misleading annual accounts, and from managing directors for misleading interim financial statements. Case law on this basis is relatively scarce to date, although the provision has been part of Dutch company law since 1928.

In bankruptcy, the liability of managing and supervisory directors may extend to the whole deficit of the bankrupt estate, if the trustee in bankruptcy provides evidence that it is plausible that apparent improper management (or supervision of management) has been an important cause of the bankruptcy. Lack of proper bookkeeping and publication of the required financial statements is deemed to constitute improper management and creates an assumption of apparent improper management being an important cause of the bankruptcy. These specific provisions have been applied often in bankruptcy, leading to extensive case law, often with smaller, non-listed companies. In the case of a bankrupt listed company, the

¹² Art. 135 Book 2 DCC.

¹³ Art. 383b and Art. 383c Book 2 DCC.

¹⁴ See the Code for Banks, para. 6.4.2, available at <<http://www.nvb.nl/index.php?p=291464>>.

District Court of Utrecht has recently found managing and supervisory directors liable for improper management.¹⁵

Creditors of the company can hold managing directors liable on the basis of tort if these directors engaged in transactions for the company when they knew or should have known that the company would not be able to pay the resulting debts (wrongful trading).¹⁶ This tort-based liability of managing directors has been extended to a wide range of actions, including a recent case where the director of a company that owned shares in another company had induced another shareholder of that company to assume a risk of liability towards the bank financing the company, and when this risk was considerably higher than the third party knew or could have known, also in considering the (lack of) recourse against the other company-shareholder.¹⁷

2.2. *Shareholders*

As indicated earlier, shareholders continue to play an increasingly important role in the governance of Dutch listed companies. Contemporary thinking about the role of shareholders is reflected in the Corporate Governance Code, which states that

‘The management board is responsible for weighing up the different interests with respect to the company’s strategy, while the supervisory board must oversee this process. Both these organs are accountable to the general meeting for the performance of their roles. Unlike the management board and the supervisory board, the other stakeholders of the company are not in principle guided exclusively by the interests of the company and its affiliated enterprise. For example, shareholders can give priority to their own interests with due regard for the principle of reasonableness and fairness. The greater the interest that the shareholder has in a company, the greater is his responsibility to the company, the minority shareholders and other stakeholders. (...) [These] principles can cause tension (...). How this tension should be resolved will differ from case to case’.¹⁸

The Dutch government recently endorsed this view, and has added that shareholders can express their opinion on the company’s strategy by making use of the rights conferred upon them, amongst others, at the general meeting of shareholders.¹⁹ Perhaps the most significant of these rights, at least in terms of corporate governance, is the right to appoint and dismiss members of the management and supervisory boards (Articles 132/134/142/144 Book 2 DCC). Different rules apply if the company is governed by the structure regime, as discussed in detail below. This article focuses on the various powers of shareholders in Dutch listed companies and the standards that apply to shareholders when exercising these powers.

2.2.1. *Fiduciary Duties of Controlling Shareholders*

While Dutch law does not explicitly state that controlling shareholders have a fiduciary duty towards minority shareholders, a controlling shareholder’s behaviour is subject to certain legal norms. In particular, stakeholders (e.g., the board, shareholders, and employees) in

¹⁵ District Court of Utrecht, 12 December 2007, *JOR* 2008, 66.

¹⁶ Supreme Court 6 October 1989, *NJ* 1990, 286 (*Beklamel*).

¹⁷ Supreme Court 26 June 2009, *NJ* 2009, 148 (*Eurocommerce*).

¹⁸ Dutch Corporate Governance Code (2008), at 7.

¹⁹ *Parliamentary Proceedings II* 2008/09, 32 014, No. 3.

Dutch companies are required by law to behave towards one another in a manner that is reasonable and fair (Article 8 Book 2 DCC). Inquiry proceedings before the Enterprise Chamber – including the ability to request provisional measures, see below – provide minority shareholders with an efficient means to subject the controlling shareholder's behaviour to judicial scrutiny if they believe the principle of reasonableness and fairness is violated.²⁰

Indeed, the responsibility of large shareholders is a subject that is receiving increasing attention from courts as well as policymakers. In 1999, in a case dealing with the controversial takeover of luxury goods manufacturer Gucci, the Enterprise Chamber held that Article 8 Book 2 DCC implies that the acquirer of a significant stake should, in his dealings with the company, take into account not only his own interests but also the interests of the company and its stakeholders.²¹ This notion is now reflected in the preamble of the Corporate Governance Code, which, as mentioned earlier, states that '[t]he greater the interest which the shareholder has in a company, the greater is his responsibility to the company, the minority shareholders and other stakeholders'. The Dutch Cabinet recently endorsed this principle.²²

Once the acquisition has been completed, Article 8 Book 2 DCC implies, for example, that if a controlling shareholder tries to squeeze out the minority by initiating a merger between the company and another one of its subsidiaries (instead of following the regular squeeze-out procedure as discussed below), this may be considered a violation of the principle of reasonableness and fairness.²³

The principle of reasonableness and fairness may also be violated if the controlling shareholder uses his power not to directly determine the company's course of action, but to appoint directors. This is illustrated by a recent case concerning telecommunications company Versatel, which had been the subject of a public offer by Tele2. Subsequent to the offer, Versatel had a controlling shareholder (Tele2) and several minority shareholders, notably hedge funds that were opposing the triangular merger initiated by Tele2 in order to squeeze out the minority. Tele2 intended to use its power to change the composition of the supervisory board such that it would consist of four supervisory directors who were also executive directors of Tele2 and one director unaffiliated with Tele2. The Supreme Court confirmed that as a general matter, Article 8 Book 2 DCC requires that the company (in this case Versatel) act in a prudent manner vis-à-vis the interests of *all* of its shareholders, and prevent unacceptable conflicts of interest.²⁴ In the case at hand, the Supreme Court then considered that such conflict of interest existed as a mere consequence of the fact that the relevant supervisory directors had irreconcilable interests, raising doubt as to whether, in acting as supervisory directors of Versatel, they would be guided solely by the interests of Versatel. Accordingly, the Supreme Court upheld the lower court's decision to, by way of a provisional measure, prevent Tele2 from appointing the conflicted supervisory directors and to instead appoint three independent supervisory board members with broad-ranging powers. The case thus serves as a strong reminder that controlling shareholders' ability to exercise their statutory powers is limited by the requirement to act in a manner that is reasonable and fair towards the other shareholders.

²⁰ For a discussion of two such cases, see Timmerman 2002, p. 409, p. 415.

²¹ Enterprise Chamber 3 March 1999, *JOR* 1999, 87 (*Gucci I*).

²² Letter from the Dutch Minister of Finance dated 25 May 2009 (*Kabinetsreactie op de geactualiseerde Nederlandse corporate governance code*) (FM/2009/706), at 8.

²³ Enterprise Chamber 20 December 2007, *JOR* 2008, 36 (*Shell*).

²⁴ Supreme Court 14 September 2007, *JOR* 2007/ 237 m. nt. Bartman (*Versatel*), r.o. 4.3.

To be sure, this requirement applies not only to controlling shareholders, but also to other shareholders, whose conduct too can become subject to scrutiny. This is exemplified by a recent case involving industrial company Stork. In this case, the Enterprise Chamber ordered an investigation into the affairs of Stork that would take into account the conduct of Centaurus, an activist hedge fund that had played a major role in the governance crisis that occurred at Stork.²⁵ The conduct of shareholders may become subject to closer scrutiny in the future, in light of pending bills before the parliament to grant companies the right to request the Enterprise Chamber to order an investigation into the affairs of a company, including the conduct of shareholders. The right to request such investigation is currently granted to shareholders only.

2.2.2. Conflicted Transactions, Transfer of Assets and Profits out of Firms for the Benefit of their Controlling Shareholders ('tunnelling')

As far as conflicted transactions are concerned, as mentioned earlier Article 146 Book 2 DCC provides that in case of a conflict of interest between the company and *members of the management board*, the company shall be represented by a member of the supervisory board, unless the articles of association provide otherwise (which they frequently do). In any event, the general meeting of shareholders is authorised to designate a person who will represent the company. This implies that the board has a duty to timely notify the general meeting of shareholders that there is a conflict of interest. A conflict of interest is deemed present not only in case of a transaction between the company and a member of the management board, but also in case of a transaction between the company and third party that a member of the management board is affiliated with (an 'indirect conflict of interest').

If a transaction has been entered into on behalf of the company by a member of the management board who, due to a conflict of interest, was unauthorised to represent the company, only the company can invoke the nullity of the transaction. Conflicted transactions are thus not subject to prior approval by (disinterested) shareholders nor can they, in principle, be declared null at the initiative of shareholders. However, case law has produced a set of norms that should be adhered to in case of conflicts of interest, relating to, for example, transparency and the involvement of independent experts.

In addition, the Corporate Governance Code sets forth the principle that any conflict of interest or apparent conflict of interest between the company and management or supervisory board members must be avoided (principles II.3 and III.6). The Code also reflects a number of related best practices, including that board members may not provide unjustified advantages to third parties to the detriment of the company, may not take advantage of business opportunities to which the company is entitled and must immediately report any potential conflict of interest. Conflicted transactions should be (i) agreed on terms that are customary in the sector concerned, (ii) approved by the supervisory board and (iii) published in the annual report.

Importantly, the Corporate Governance Code provides that transactions between the company and legal or natural persons *who hold at least ten percent of the shares in the company* are subject to the same requirements. If these norms are not adhered to, this could, depending the circumstances, result in a court rescinding the resolution to enter into the transaction at the request of one or more (minority) shareholders, on the basis that the principle of reasonableness and fairness of Article 8 Book 2 DCC has been violated (Article 15(1)(b) Book 2 DCC).

²⁵ Enterprise Chamber 17 January 2007, *JOR* 2007/42 (*Stork*), r.o. 3.9.

The Corporate Governance Code also considers best practice that a management or supervisory board member may not take part in any discussion or decision-making that involves a subject or transaction in relation to which he has a conflict of interest with the company. In a bill that is currently pending before parliament, the Dutch Cabinet has proposed to introduce a statutory provision to the same effect.²⁶ As a result of this amendment, minority shareholders who wish to oppose a conflicted transaction will be able to request a court to rescind the resolution to enter into the transaction, on the basis that the applicable procedural rules governing the decision-making in the management board or supervisory board were violated (Article 15 (1)(a) Book 2 DCC).

It should be borne in mind that the rescission of the underlying resolution does not directly affect the validity of the conflicted transaction. It does, however, represent a first step in terms of enabling the company to claim damages from those who have committed a wrongful act by entering into the transaction, such as the conflicted director or the counterparty that knowingly benefited from the conflict (Article 9 Book 2 DCC and 162 Book 6 DCC, respectively).

2.2.3. Shareholder Rights and Minority Protection, in Particular Information Rights

Perhaps the most important provision in terms of minority shareholder protection is the principle that shareholders must be treated equally (Article 92 (2) Book 2 DCC), as also reflected in the Second EC Company Law Directive and the EC Shareholders' Rights Directive.²⁷ Specifically, this principle requires that the company treat shareholders *who are in equal circumstances* in an equal way. The principle derives from the broader principle of reasonableness and fairness discussed earlier.

There are three main ways through which (minority) shareholders can obtain company-specific information, including information on conflicted transactions. The first is through mandatory disclosures by the company. As discussed in greater detail below, annual accounts of listed companies have to be prepared in accordance with the International Financial Reporting Standards as endorsed for use in the EU (IFRS). This includes IAS 24, which requires extensive related party disclosures. At its core, the requirement of IAS 24 has already existed as part of Dutch law on financial reporting for quite some time. In a 1980 case that essentially involved tunnelling by the controlling shareholder, the Enterprise Chamber held that if the extent of the company's revenues is influenced by the relation between a company and its controlling shareholder, the explanatory notes to the company's annual accounts should indicate this fact, and explain the nature and terms of the relevant transactions.²⁸

Second, pursuant to Article 2:107 (2) Book 2 DCC (and pursuant to the Corporate Governance Code), shareholders may ask questions during the general meeting of shareholders, and the board is required to provide answers to such questions unless this would be contrary to an overriding interest of the company.

Lastly, inquiry proceedings provide a powerful tool for minority shareholders to obtain information, since one of the purposes of the right of inquiry is indeed to obtain clarity with respect to the affairs of the company.

²⁶ Bill amending Book 2 DCC, *Parliamentary Proceedings II* 2008/09, 31 763, No. 2.

²⁷ For an extensive discussion of minority shareholder protection in general, see Timmerman & Doorman 2002.

²⁸ Enterprise Chamber 27 March 1980, *NJ* 1981/64 (*Dufour*).

2.2.4. Shareholder Activism

The issue of shareholder activism has received considerable attention in the Netherlands in recent years for two related reasons. First, the recent wave of shareholder activism was preceded by a series of legislative reforms aimed at expanding the rights of shareholders, as discussed earlier. In some respects, these reforms constituted a move away from the 'stakeholder model' towards the more shareholder-oriented model that prevails in the US and the UK. For this reason, the legislative forms have deeper cultural and societal meaning. Second, the recent wave of shareholder activism has involved some high profile cases that have sparked controversy, notably the activism of hedge fund TCI, which set in motion a string of events that led to the hostile takeover of a major Dutch bank, ABN AMRO, by a consortium of three banks, including another Dutch bank, Fortis. This takeover, combined with the recent financial crisis, ultimately led to Fortis's demise, necessitating a bailout by the Dutch government and fuelling public scepticism of shareholder activism.

The fact that shareholder activists have been able to have a real impact on a number of companies is due to some extent to the various powers conferred upon them by statute and to another extent to the ownership structure of Dutch firms.²⁹

2.2.4.1. Ownership Structure of Dutch Firms

The ownership of Dutch firms is relatively dispersed. A 2009 Risk Metrics study showed that Dutch listed companies had the lowest(!) degree of ownership concentration in Europe. Shareholders with a stake of 5% or larger together held, on average, 20.8%, while the European average was 35% and the percentage for Italy, for example, was 53.2%.³⁰ Moreover, by 2007, no less than 70% of market capitalisation was owned by foreign investors.³¹

2.2.4.2. Shareholder Powers

In terms of shareholder powers, one statutory right (other than the right to dismiss and appoint directors) that has significantly facilitated the efforts of shareholder activists is the right to put items on the agenda. Pursuant to Article 114a Book 2 DCC, shareholders holding shares representing at least 1% of market capitalisation or a value of EUR 50m have such right. Another relevant shareholder right is the right to approve major transactions entered into by the company (Article 107a Book 2 DCC).

Also noteworthy is the statutory requirement that companies have a remuneration policy that is approved by the general meeting of shareholders (Article 135 Book 2 DCC). Led by institutions such as Risk Metrics and the influential association of securities owners, the *Vereniging van Effectenbezitters*, (VEB) discussed below, shareholders have recently rejected the remuneration policies of companies such as Philips and VastNed Retail. Corporate Express, another blue chip company, recently decided to withdraw the proposed remuneration policy out of fear that shareholders would reject it, which suggests that this statutory power has broader impact than can be deduced only from those instances where the remuneration policy has actually been rejected. The developments at the companies mentioned above are consistent with shareholder dissatisfaction with remuneration practices at foreign companies,

²⁹ For an empirical analysis of shareholder activism in the Netherlands, see De Jong, Roosenboom, Verbeek and Verwijmeren 2007.

³⁰ Risk Metrics Group 2009.

³¹ Federation of European Securities Exchanges (FESE) 2008.

as illustrated by the recent rejection by shareholders of the remuneration report of Royal Dutch Shell, an English plc with a large Dutch shareholder base.

Finally, shareholder activists have frequently initiated inquiry proceedings, requesting the Enterprise Chamber to intervene in, for example, takeover situations, by taking provisional measures.³² Such measures may include prohibiting the company from taking defensive measures (discussed in more detail below), or appointing independent members to the supervisory board. The Enterprise Chamber has intervened with various decisions in two drawn-out cases, Stork and ASMI, in which activist shareholders attempted to force companies to change their strategy by selling off parts of their business.³³

Two conclusions can be drawn from these cases: (i) setting the strategy of the company is the authority of the management board subject to the approval of the supervisory board and is not the power of the general meeting, (ii) when there is a major disagreement with shareholders on the strategy of the company in the end a solution must be found, which the Enterprise Chamber typically tries to resolve through a process of preserving the status quo, denying management and shareholders from taking irreversible acts and instructing the parties to continue to find a solution, where necessary aided by independent outsiders.

A revised Corporate Governance Code was published in 2008, which states that the Corporate Governance Code 'is based on the principle accepted in the Netherlands that a company is a long-term alliance between the various parties involved in the company,' and emphasises the fact that the management and supervisory boards have a responsibility to weigh these various interests, with a view to 'ensuring the continuity of the enterprise, while the company endeavours to create long-term shareholder value'.³⁴ This translates into several provisions that appear to be aimed at mitigating the influence of activist shareholders. An example is the provision stipulating that if a shareholder intends to put an item on the agenda that may result in a change in the company's strategy, the management board 'shall be given the opportunity to stipulate a reasonable period in which to respond,' which may extend to 180 days (best practices II.9/IV.4.4). The Dutch Cabinet has generally approved of the revisions, and, as mentioned earlier, has recently proposed additional legislative measures that have the practical effect of limiting shareholder power, such as increasing the threshold for shareholders who are entitled to put an item on the agenda from 1% to 3% and expanding disclosure requirements of major shareholders. This also includes lowering the threshold for initial disclosure from 5% to 3% and introducing a much criticised requirement for notifying shareholders to indicate whether or not they agree with the company's strategy.³⁵

2.2.5. Proxy Voting

Proxy voting is still in a development stage in the Netherlands. Recent legislative amendments have enabled shareholders to issue proxies electronically (Article 117 (6) Book 2 DCC), and permitted companies who so desire to amend their articles of association in order to allow shareholders to vote electronically (Article 117a (1) Book 2 DCC). The implementation of the European Shareholder's Rights Directive, which implementation is expected fairly soon, will further enable proxy voting, for example by introducing a uniform voting record date 21 days prior to the general meeting of shareholders.³⁶ Still, major

³² In the case of *Versatel*, for example, the Enterprise Chamber intervened several times on behalf of minority shareholders to stop a post public offer squeeze-out merger that would prejudice minority shareholders.

³³ *Centaurus v. Stork*, *supra* note 8 and Enterprise Chamber 6 August 2009, *LJN*: BJ4688 (*ASMI*).

³⁴ Corporate Governance Code (2008), at 6 (2008).

³⁵ *Parliamentary Proceedings II* 2008/09, 32 014, No. 2.

³⁶ *Parliamentary Proceedings II* 2008/09, 21 746, No. 2 (proposed amendment to Art. 119 Book 2 DCC).

obstacles to the development of a well-functioning proxy voting system remain. Notably, due in large part to the fact that most shares in Dutch listed firms are dematerialised bearer shares, companies are still having difficulties in tracing the identity of their shareholders. This makes it difficult for companies (and others who wish to reach out to the shareholders) to distribute information and solicit proxies.

Two significant attempts have been made to address this issue. The first is a private sector initiative (*Communicatiekanaal aandeelhouders*, or 'CA') that channels information from participating companies to shareholders who have indicated they wish to receive such information, and channels voting instructions from these shareholders to the company, in each case without disclosing their identity to the company. The CA is also actively promoting electronic voting.

The second attempt is currently being made by the Dutch Ministry of Finance, which has proposed legislative amendments that should enable issuers to request information on the identity of their (ultimate) investors from financial intermediaries, so they can distribute information to their shareholders prior to the general meeting.³⁷ The proposal will also enable investors to communicate with one another. Investors individually or collectively holding 10% of the shares will be entitled to request the issuer to collect information on the identity of its investors, and once that information has been collected (at the issuer's own initiative or at the request of these 10% shareholders), investors individually or collectively holding 10% of the shares will be entitled to request the issuer to distribute, on their behalf, information to the shareholders. While this proposal potentially represents a significant step forward, it also leaves many technical issues unresolved, and as a result it remains to be seen whether the proposal will translate into tangible benefits for issuers and shareholders in the short term.

2.3. Labour

Employees play a relatively prominent role in Dutch corporate governance. The influence of employees within companies is mainly exercised through works councils and trade unions.

2.3.1. Works Councils

Works councils are corporate bodies, in addition to the managing board, the supervisory board and the general meeting of shareholders. Under the Works Councils Act (*Wet op de Ondernemingsraden; WCA*) a company established in the Netherlands – regardless of its legal form – is obligated to institute a works council if, in short, it employs more than 50 employees within the Netherlands (Article 2 WCA).

Most Dutch listed companies have a works council. However, since a works council must be instituted if a company employs more than 50 employees *within the Netherlands*, a works council is often instituted at the level of the Dutch top holding, and not at the level of the international top holding. As a result, a works council may not be able to exercise its rights at the international level, but only at the Dutch top holding level.³⁸ Depending on the size of the company, a works council has from 3 to 15 members who are elected by and from among the employees (Article 6 WCA).

The works council is entitled to discuss the general affairs of the company twice a year and initiate additional discussions between itself and management on virtually any issue that requires discussion according to the works council (Article 23 WCA). In addition, the

³⁷ *Parliamentary Proceedings II* 2008/09, 32 014, No. 2.

³⁸ There are situations, however, in which a Dutch top holding works council will be able to exercise its influence at the international top holding level as well.

company is required to enable the works council to advise on the appointment and dismissal of managing directors (Article 30 WCA). Management also needs the consent of the works council for a number of decisions that directly affect employees, such as decisions on pensions, working hours, remuneration systems, employment conditions, etc. The works council is entitled to nullify these types of decisions if made without its consent (Article 27 WCA).

The rights described in the preceding paragraph establish a prominent role for the works council within companies established in the Netherlands. The most prominent role of the works council in Dutch corporate governance, however, is revealed in relation to major corporate decisions, such as decisions regarding a change of control over the company, a change of the companies' business or organization, large investments and divestments, a discontinuation of operations and obtaining or granting important loans. With respect to these types of decisions, the WCA provides for a mandatory advice procedure (Article 25 WCA). If the works council is not consulted in accordance with the applicable rules, this may seriously endanger or delay the execution of the decision. For even though the works council's advice is not binding, if the management's decision conflicts with the advice or if the management has not properly informed the works council in connection with the advice, the works council may have the decision reviewed by the Enterprise Chamber (Article 26 WCA). The Enterprise Chamber may require management to withdraw (parts of) the decision or to undo any consequences and may even prohibit management from executing the decision. The Enterprise Chamber will not, however, easily impose these sanctions. It will generally only do so if explicitly requested by the works council and if the management could not reasonably have taken its decision after balancing the interests connected with the decision.

If the interests of the managing board and the works council run parallel, for example in fending off a hostile takeover, the management may grant the works council the right to institute inquiry proceedings (Article 346(c) Book 2 DCC). If so, the works council can request that the Enterprise Chamber assess the conduct of different corporate bodies of the company.

Currently, a bill to enhance the rights of the works council of listed and non-listed public companies with respect to decisions of the general meeting of shareholders is pending before the Dutch parliament.³⁹ The bill establishes a right for the works council to be given the opportunity to form an opinion on a request for the consent of the general meeting of shareholders on corporate decisions regarding important changes in the identity or the character of the company, and on proposals to the general meeting of shareholders regarding the appointment, suspension or discharge of managing and/or supervisory directors, and the remuneration policy.

The written opinion of the works council must be provided to the general meeting at the same time that the request or proposal is presented to it. The chairman of the works council, or another member appointed by him, will have the right to explain the opinion of the works council in the general meeting. It does not affect the decision of the general meeting if no opinion of the works council is rendered. For international situations, the bill establishes that the enhanced rights of the works council will only apply if the majority of the employees of the group are employed within the Netherlands. Notably, the bill and the WCA are not aligned. If the bill is passed, situations will occur in which the works council does not have a right to advise on the basis of Article 25 WCA, but does have the right to form and express an opinion on a certain request or proposal to the general meeting.

³⁹ Bill amending Book 2 DCC, *Parliamentary Proceedings II* 2009/10, 31 877, No. A.

2.3.2. Works Councils – the Structure Regime

The rights of works councils are even enhanced in the structure regime. This regime is designed to apply to large companies and was introduced in 1971 to stabilise the decision-making process in large listed companies and enhance the position of employees in the decision-making process. Under the structure regime, the appointment and dismissal rights of the general meeting of shareholders are restricted to a large extent.

The structure regime applies if:

- (i) the issued share capital and the reserves of an issuer amount to EUR 16 million or more, according to its latest balance sheet (including explanatory notes);
- (ii) the issuer, or one of its ‘dependent companies’ (see Appendix), has set up a works council pursuant to a legal obligation to do so; and
- (iii) the issuer, together with its dependent companies, normally employs at least 100 employees in the Netherlands.

If the structure regime applies, the otherwise optional institution of a non-executive board becomes mandatory (Articles 153 and 158 Book 2 DCC). This mandatorily instituted supervisory board (and not the general meeting of shareholders) appoints, suspends and dismisses the executive directors (Article 162 Book 2 DCC). The general meeting of shareholders appoints the supervisory directors.⁴⁰ Candidates must, however, have been nominated by the supervisory board, in accordance with a ‘profile’. The supervisory board must discuss the ‘profile’ in the general meeting of shareholders and with the works council, but the approval of shareholders or the works council is not required. The general meeting of shareholders has the right to reject the non-executive board’s nominated candidate by a simple majority of the votes cast representing at least one-third of the issued share capital, upon which rejection the procedure will start over again.

The general meeting of shareholders and the works council have a right of recommendation with respect to the candidates put forward by the supervisory board. The works council has an enhanced right of recommendation with respect to one-third of the members of the supervisory board.

Shareholders may dismiss the entire supervisory by adopting a resolution of no-confidence, which requires a simple majority of the votes cast representing at least one-third of the issued share capital. A no-confidence resolution may not be adopted unless the competent works council has been allowed the opportunity to express its views (Article 158 Book 2 DCC).

In addition, under the structure regime, a number of executive board actions require prior approval by the supervisory board (Article 164 book 2 DCC), including but not limited to:

- (i) the issue and acquisition of shares and bonds in the issuer;
- (ii) application for listing or delisting on the official list of any stock exchange of shares or, as the case may be, depositary receipts for shares or bonds issued by the issuer;
- (iii) a proposal to amend the articles of association;

⁴⁰ The bill described in the preceding paragraph entitles works councils of companies governed by the structure regime to have the opportunity to form and express an opinion on such appointments as well.

- (iv) a proposal to dissolve the issuer;
- (v) the filing of a petition for bankruptcy and for a suspension of payments ('moratorium'); and
- (vi) a proposal to reduce the issued share capital.

A full exemption to the structure regime applies, among other things, if the relevant company is, substantially, purely a financing and holding company, provided that the majority of its employees and the employees of the companies which belong to its group are employed or resident outside the Netherlands (Article 153 (3) Book 2 DCC). As a result of this exemption, most large listed companies are exempted from the structure regime. Instead, the structure regime is often only applied at the Dutch top holding level, and not at the international top holding level.

A partial exemption, allowing a 'mitigated structure regime', will apply, in short, if at least 50% of the issued share capital of the company is held by a legal entity, the majority of whose employees (or of the employees of its dependent companies) are employed outside the Netherlands (Articles 155 and 155a Book 2 DCC). The mitigated structure regime differs from the full structure regime in that the members of the executive board of companies subject to the mitigated structure regime are appointed, suspended and dismissed by the general meeting of shareholders. Otherwise, the mitigated regime is in its effect more or less the same as the full structure regime.

2.3.3. Trade Unions

Trade unions generally have less influence on Dutch corporate governance than works councils. At a sector level, trade unions may be dominant in negotiations on collective labour agreements, which can be declared generally applicable in certain (private or public) sectors. At the level of individual companies, trade unions may play a role as negotiators on behalf of (a part of) the employees in connection to decisions that directly affect employees, such as decisions regarding reorganisations and lay-offs.

Most relevant in connection to Dutch corporate governance, however, is the institutionalised role of trade unions through the Merger Code (*SER Fusiegedragsregels 2000*). This code, which is non-binding, serves to protect the interests of employees by ensuring that trade unions are timely involved in the process of a takeover by or of a Dutch company.

The Merger Code applies where there is a direct or indirect change of control in an enterprise (with at least 50 employees in the Netherlands) or any part of the enterprise, regardless of how such change was effected (Article 2 Merger Code). A key principle is that the trade unions must be given an opportunity to discuss the acquisition, insofar as it may affect employees' interests, with the parties concerned (Article 4 Merger Code). Unlike the works council, the trades unions are not entitled to render advice or to have the decision of the management reviewed by a court. The Merger Code itself does, however, provide for a tribunal (Section 6 Merger Code). And although the Merger Code lacks statutory force, if the tribunal finds that certain acts of the acquirer or the company are not in accordance with the Merger Code, the tribunal may issue a public reprimand.

Trade unions or other employee associations that have full legal capacity, whose members are employed by the company, are (generally) entitled to institute inquiry proceedings (Article 347 Book 2 DCC). Therefore trade unions may request that the Enterprise Chamber assess the conduct of different corporate bodies of the company. However, trade unions instituting inquiry proceedings seldom occurs.

2.4. *Audit*

2.4.1. **Mandatory Auditing by External Auditors**

Mandatory auditing by external auditors of the annual accounts of Dutch companies is based on Article 393 Book 2 DCC. Article 393 (1) Book 2 DCC requires the company to assign an external auditor to audit its annual accounts. An external auditor in the meaning of this subsection can be either a natural person approved to carry out statutory audits or an auditing firm.

According to Article 393 (2) Book 2 DCC, the general meeting of shareholders is authorised to appoint the external auditor. If the general meeting fails to appoint an auditor, the supervisory board or the management board is then authorised to do so. The external auditor may be appointed for one year or for an indefinite period. Although the corporate body that appoints the external auditor preserves the right to terminate the engagement at any time, termination only can occur on the basis of 'well-founded reasons'. These reasons do not include disputes concerning accounting principles or auditing activities.

Article 393 Book 2 DCC does not limit the number of consecutive financial years for which the external auditor may audit the company's accounts. Such a limitation is, however, included in the Audit Firms Supervision Act ('AFSA'). Based on the AFSA, the AFM supervises auditing entities that provide audit reports relevant to the Dutch capital markets. Article 24 AFSA states that an audit firm may not allow a statutory audit to be conducted by an external auditor who has been responsible for conducting statutory audits for that public interest entity during the previous seven consecutive financial years.

2.4.2. **Auditors' Tasks**

The tasks of external auditors derive from Article 393 (3), (4) and (5) Book 2 DCC, which provisions in their turn form the implementation of articles 51 and 51a of the Fourth Council Directive on Company Law.⁴¹ The audit of the external auditor, according to Article 393 (3) Book 2 DCC, consists of the determination as to whether the annual accounts give a true and fair view in accordance with the relevant financial reporting framework. Furthermore, the external auditor is to examine whether the annual accounts as presented in the annual report meet the requirements of Book 2 DCC and are consistent with the company's own annual accounts for that financial year.

The external auditor reports his results to the supervisory board and to the management board. The results of the audit are to be reflected in the audit report. The audit report must include the auditor's opinion as to whether the annual accounts give a true and fair view in accordance with the relevant financial reporting framework and an opinion concerning the consistency or otherwise of the annual report with the annual accounts for the same financial year. Furthermore, Article 393 (5) Book 2 DCC requires the external auditor to include in the audit report at least:

- (i) an introduction which identifies the annual accounts that are the subject of the audit, together with the financial reporting framework that has been applied in their preparation;
- (ii) a description of the scope of the audit which identifies the auditing standards in accordance with which the audit was conducted; and

⁴¹ Fourth Council Directive 78/660/EEC of 25 July 1978 based on Art. 54 (3) (g) of the Treaty on the annual accounts of certain types of companies (*Official Journal* L 222, 14/08/1978, as amended).

(iii) a reference to any matters which the statutory auditors may wish to emphasise without qualifying the auditor's opinion.

Article 393 (6) Book 2 DCC states that the auditor's opinion may be either unqualified, qualified, an adverse opinion or, if the external auditors are unable to express an opinion, a disclaimer of opinion. The audit report must be signed and dated by the external auditors.

2.4.3. Auditors' Independence

Several new provisions have been added to Dutch legislation recently concerning external auditors' independence. These provisions can be found in the AFSA, which implements the provisions of the European Statutory Audit Directive. The AFSA includes rules concerning the qualifications of auditing entities and auditors. Based on the AFSA, the government issued the Decree on the Supervision of Audit Firms, which also includes detailed rules. These detailed rules derive from the requirements included in the International Standard of Quality Control, a standard of the International Federation of Accountants (IFAC).

With regard to external auditors' independence, the AFSA distinguishes between requirements applicable to auditing firms and to natural persons. Auditing firms, pursuant to Articles 14 and 15 AFSA, must ensure that the external auditors employed by or affiliated with the firm comply with the requirements prescribed in the Act. In addition, the integrity of the persons who determine or co-determine the day-to-day policies of the auditing firm is to be beyond any doubt. Article 16a AFSA also states that the majority of the voting rights in the auditing firm must be held by auditing firms, auditing entities or persons that meet the requirements in regard to their (auditing) competence. The auditing firm is also required to meet the requirements in the AFSA regarding independence.⁴²

Finally, other provisions on the independence of auditing firms and external auditors are included in Articles 23 and 24 AFSA. These include that an auditing firm may not conduct a statutory audit for a public interest entity, which includes Dutch listed companies, if in regard to that organisation the auditing firm compiled the financial accounts on which the statutory audit is based at any time during the previous two years or if the auditing firm was responsible for a substantial part of the financial administration during the period to which the financial accounts refer and on which the statutory audit will be based. As has already been mentioned above, the auditing firm may not allow an external audit to be conducted by an external auditor who has been responsible for conducting statutory audits for the same company during the previous seven consecutive financial years.

The AFSA requires individual external auditors to meet the requirements regarding competence, independence, objectivity and integrity.⁴³ The AFSA also prohibits individual external auditors from accepting a position as a policymaker of a company that qualifies as a public interest entity within two years after termination of his position as external auditor for that company.⁴⁴

⁴² Art. 19 AFSA.

⁴³ Art. 25 and 25a AFSA.

⁴⁴ Art. 29 AFSA.

2.4.4. Direct Liability towards the Company and Shareholders (Third-party Liability), Caps, Concrete Cases

There is no specific provision in the DCC, or in other Dutch legislation, which deals with the liability of external auditors. Thus the general rules of civil liability are applicable. This means that liability towards the company can arise in case of breach of contract and on the basis of tort. Since it is the company that is party to the contract, only the company itself can initiate proceedings for breach of contract. In this respect, individual shareholders are considered a third party.

Whether third parties, including individual shareholders, can rely on the information of the audit report has led to academic discussions and several legal proceedings. In an important and recent case,⁴⁵ the Netherlands Supreme Court stated that an audit report has a type of public character. The purpose of the audit report is to inform the general meeting and the shareholders of the true and fair view of the annual accounts. Third parties may expect that if the annual accounts are published with an unqualified auditor's opinion, the external auditor's opinion is that the annual accounts give a true and fair view and are in accordance with the relevant financial reporting framework. However, if subsequently the audited annual accounts are found to be misleading or inaccurate, this does not automatically lead to liability of the external auditor towards third parties on the basis of tort. External auditors are only liable towards third parties if there are specific circumstances showing breach of a duty of care that the external auditor owes to the third parties, for instance if the external auditor has made a professional error in the audit.

There is no statutory liability cap, but the auditor and the audited company can set a liability cap by limiting the obligations of the external auditor in the engagement contract. Nevertheless, liability for gross negligence or wilful misconduct cannot be excluded and setting a cap has no effect on third parties.

3. External Corporate Governance

3.1. General Overview

The rules applicable to takeovers and disclosure obligations stem from Book 2 DCC and the AFS, as well as case law. The DCC contains requirements that apply to Dutch companies, i.e. companies incorporated in the Netherlands. The AFS focuses on listed companies, Dutch and foreign, which have their securities admitted to trading on a regulated market in the Netherlands (Euronext Amsterdam by NYSE Euronext). The AFS includes some provisions that are applicable only to Dutch listed companies, as well as provisions implementing the EU Takeover Directive, the EU Prospectus Directive, the EU Market Abuse Directive and the EU Transparency Directive.

3.2. Takeover Regulation

3.2.1. Mandatory Bid and Bid Price

An obligation to make a bid is triggered upon acquiring 'control' of a Dutch listed company that has its shares admitted to trading on a regulated market (Article 5:70 AFS). 'Control' is defined as the ability to exercise at least 30% of the voting rights in the general meeting of shareholders. There are a number of exceptions to the mandatory bid rule, such as an

⁴⁵ Supreme Court, 13 October 2006, *JOR* 2006/296 (*Vie d'Or*).

exception for parties who have control at the time of the company's shares are first admitted to trading on a regulated market.

Acquisition of control by acting in concert with other parties also triggers a mandatory bid. Parties will be deemed to 'act in concert' if they enter into an explicit or implicit agreement aimed at acquiring control or frustrating an offer for the company. This implies that parties who are merely exchanging information, or having discussions on corporate governance related issues with a view to arriving at a joint position, will not be considered to be 'acting in concert' for purposes of the mandatory bid rule, as long as their cooperation is not geared towards acquiring control.

The mandatory bid can be made in cash, equity or a combination of the two, and should be made at an equitable price. If the bidder has acquired any target securities in the year prior to the bid, the equitable price will be the highest price paid by the bidder for such securities during that year (Article 5:80a (2) AFS). If the bidder has *not* acquired any target securities in the year prior to the bid, the equitable price will be the average share price during that year (Article 25 (2) of the Decree on Public Offers). Notwithstanding these rules, in each case, the Enterprise Chamber can be requested to determine the equitable price at its sole discretion. In 2008, a Dutch organisation representing minority shareholders filed the first such request in a case concerning the takeover of the retailer Schuitema.⁴⁶ Part of the consideration paid by the acquirer to the seller of the majority of the Schuitema shares (i.e. retail giant Ahold) was in kind, as a result of which it was not immediately clear what the equitable price to be paid to the minority shareholder was. Based on expert advice, the court decided that the price paid by the bidder to Ahold (the presumed equitable price) was in fact higher than the price subsequently offered by the bidder in the mandatory bid.⁴⁷

3.2.2. Post-bid: Anti-frustration or 'just say no' Rule, Breakthrough, Options, Reciprocity

The Dutch legislature has implemented the board neutrality rule and the breakthrough rule contained in the Takeover Directive in such a way that companies can choose whether they wish to include these rules in their articles of association, and whether adherence to the rules is subject to reciprocity. Since few, if any, companies have amended their articles of association accordingly, the two rules have little to no relevance in practice.

By contrast, case law on the permissibility of post-bid defensive measures is highly relevant. In a landmark case concerning the real property fund Rodamco, the Netherlands Supreme Court, perhaps inspired by the Delaware Chancery Court's decision in *Unocal*, held that defensive measures can be justified if they are necessary with a view to the (long-term) continuity of the company and its various stakeholders, provided that the measures are taken in order to maintain the status quo pending negotiations between the target and the bidder, and provided that they constitute an adequate and proportional response.⁴⁸ The deployment of defensive measures for an indefinite amount of time will, as a general matter, not be justified.

In 2007, in a high-profile case dealing with the sale of LaSalle bank by ABN AMRO, which some felt amounted to a 'crown jewel sale' defence, the Supreme Court, while acknowledging the importance of a level playing field between competing bidders, held that

⁴⁶ Enterprise Chamber 23 October 2008, *RO* 2009/4, *Ondernemingsrecht* 2008/17 (*Schuitema*).

⁴⁷ Enterprise Chamber 21 August 2009, *LJN*: BJ5764 (*Schuitema*). Because the difference between this higher amount and the average share price in the three months prior to the filing of the request was less than 10% of the average share price, the request that the court determine the equitable price at its sole discretion was inadmissible.

⁴⁸ Supreme Court 18 April 2003, *JOR* 2003, 110 m.nt. Blanco Fernandez (*RNA*), r.o. 3.7.

in responding to an offer, the target board should ultimately be guided by the interests of the (long-term) continuity of the company and its various stakeholders, and thus not only by the interests of the shareholders.⁴⁹ Nevertheless, the case did not overthrow the principle set forth in *Rodamco* (i.e. that the deployment of defensive measures for an indefinite period of time will generally not be justified), which continues to be the guiding principle in terms of permissibility of defensive measures.⁵⁰

The most common post-bid defensive measure is the issuing of preference shares to a friendly foundation. Because the preference shares are issued at par value and need not be fully paid up, a large number of shares can be issued to the foundation at relatively low cost. Since, under Dutch law, voting rights depend on the nominal value of the share (regardless of whether the shares are fully paid up and of their market value), this enables the foundation to obtain a large voting block cheaply, thus in effect neutralising the hostile bidder's (or activist shareholder's) actual or anticipated voting power.

Two recent court decisions in high-profile cases – involving blue chip companies *Stork* and *ASMI* – have specified the factors that are relevant in determining whether such a defensive measure is permissible. Two factors are particularly important.

First, the scope of the resolution by which the general meeting of shareholders has delegated the authority to issue shares to the board. Key issues in this respect are whether the delegated authority includes the authority to grant a call option (to a friendly foundation), and if so, the circumstances under which the call option may be exercised according to the resolution. Typically, the call option may be exercised to fend off unsolicited takeovers, i.e. to prevent raids. In *Stork*, the court held that the mere intended use by a major shareholder of the statutory right to dismiss the entire supervisory board of a company subject to the structure regime, did not qualify as a 'raid' in this sense.⁵¹ By contrast, in a case concerning computer chip manufacturer *ASMI*, the court essentially held that the intended use by a major shareholder of the statutory right to replace certain members of the executive board including the CEO, as well as the entire supervisory board, *did* qualify as a raid, and therefore justified the exercise of the option right.⁵²

Second, the foundation's objective in exercising the option. Typically, the foundation's objective, at least formally, is to ensure the independence and (long-term) continuity of the company, with a view to safeguarding the interests of the company and its various stakeholders. In case of an unsolicited takeover, the foundation may deem it necessary to serve this purpose by exercising the option, thus diluting the bidder's (potential) voting power in the target.⁵³ In *Stork*, the court held that the intended effect should be to maintain the status quo pending negotiations between the target, the bidder and other shareholders and pending the exploration of alternative options by the board.⁵⁴ In *ASMI*, the court found, on a preliminary basis, that the foundation that had exercised the option acted insufficiently independently of the board, and therefore appeared to have exercised the option with a view to protecting the incumbents rather than maintaining the status quo.

⁴⁹ Supreme Court 13 July 2007, *RO* 2007, 69 and *NJ* 2007, 434 m.nt. Maeijer (*ABN Amro*).

⁵⁰ In fact, *ABN AMRO* did not deal directly with the permissibility of defensive measures, only with the question of whether the relevant transaction was subject to shareholder approval.

⁵¹ *Centaurus v. Stork*, *supra* note 25, r.o. 3.12.

⁵² *ASMI*, *supra* note 33, r.o. 3.25.

⁵³ The foundation's purpose is determined by its articles of association, and will also be referred to in the agreement pursuant to which the option is granted by the company to the foundation.

⁵⁴ *Centaurus v. Stork*, *supra* note 25, r.o. 3.12. This standard is broadly consistent with the standard set forth by the Supreme Court in *RNA* mentioned earlier, and underlines that in order to be permissible, defensive measures should be of temporary nature.

3.2.3. Pre-bid: most important Defensive Measures

The most common pre-bid defensive measures are priority shares and depositary receipts for shares. While the administration office holding the underlying shares is required by law to issue proxies to holders of depositary receipts who so request, Article 2:118a DCC permits the administration office to refuse to issue proxies in a hostile scenario. The Corporate Governance Code, however, is less forgiving towards the use of depositary receipts. The Code stipulates the principle that depositary receipts for shares may not be used as an anti-takeover measure, and that the management of the administration office must issue proxies in all circumstances and without limitation to the holders of depositary receipts who so request.⁵⁵

Research indicates that the number of companies using depositary receipts for shares has significantly declined over the recent years.⁵⁶ More generally, it has become less common for companies to accumulate various types of defensive measures.⁵⁷

3.2.4. Takeover Bids from Abroad

The applicability of Dutch rules primarily depends on whether the target shares are admitted to a regulated market in the Netherlands. From this perspective, the nationality of the bidder is irrelevant.

If the bidder wants to make an offer for a company whose shares are admitted to a regulated market in the Netherlands by using an offer document that has been approved by a regulator of another EU Member State, the AFM may require that additional, specific information be included in the offer document, and that parts of the offer document are translated into Dutch (Article 11 (3) Decree on Public Offers).

Finally, if a bidder wants to make an offer for a Dutch company, certain rules of Dutch company law will apply regardless of whether the offer is subject to Dutch takeover rules or foreign takeover rules. Notably, the target company is required to convene a meeting of shareholders to discuss the offer, and to publish, prior to such meeting, certain information regarding its position on the offer (Article 18 Decree on Public Offers). In addition, the target is required to provide its employees with certain information regarding the offer (Article 27 Decree on Public Offers).

3.2.5. Squeeze-out and Sell-out, other Exit Rights, Compensation

In addition to the conventional squeeze-out right of shareholders who own at least 95% of the share capital (Article 92a Book 2 DCC), the implementation of the EU Takeover Directive has resulted in an additional squeeze-out right for shareholders who have acquired at least 95% of the share capital and of the voting rights pursuant to a public offer (Article 359c Book 2 DCC). The distinctive feature of the latter squeeze-out right is that the law provides that the minority shareholders should receive an equitable price for their shares, which price is presumed to be equal to the offer price. However, this presumption applies only if the bidder acquired, through the offer, at least 90% of the shares not otherwise acquired by him.⁵⁸

⁵⁵ Principle IV.2 of the Dutch Corporate Governance Code.

⁵⁶ Raaijmakers, Van der Elst & De Jong 2007, p. 56 (showing that in 1992, 39% of the listed companies had issued depositary receipts for shares, against 15% in 2006).

⁵⁷ Raaijmakers, Van der Elst & De Jong 2007, p. 57 (showing that in 1992, listed companies that were governed by the structure regime on average had approx. 2.1 defensive structures in place (approx. 1.6 for regular companies), against approx. 1.7 in 2003 (approx. 1.0 for regular companies in 2006).

⁵⁸ Art. 359c (6) Book 2 DCC and OK 28 October 2008, *JOR* 2008/335 (*Danone*).

Conversely, minority shareholders who are confronted with a shareholder that has acquired at least 95% of the share capital and of the voting rights pursuant to a public offer, have a sell-out right (Article 359c Book 2 DCC). The same equitable price requirement applies, and both the squeeze-out right and the sell-out right should be exercised within three months of the expiration of the offer period.

3.3. Disclosure and Transparency

3.3.1. Annual Financial Information

In general, Dutch companies have to file their annual accounts with the Trade Register of the Chamber of Commerce within eight days after adoption of the annual accounts by the general meeting of shareholders. Article 101 Book 2 DCC requires the company's management board to prepare the annual accounts, in principle, within five months after the end of the financial year. For Dutch listed companies, Article 5:25c AFS contains a more specific provision that requires an annual financial report be published within four months after the end of each financial year, which period cannot be extended.

Article 5:25c AFS includes the implementation of Article 4 of the EU Transparency Directive. Article 5:25c AFS states that the annual financial report must include:

- (i) the audited annual accounts, together with the auditor's report;
- (ii) the annual management report (within the meaning of Article 391 Book 2 DCC); and
- (iii) statements of the persons responsible for the annual financial report indicating that, to their knowledge:
 - a. the annual accounts give a true and fair view of the assets, liabilities, financial position and profit or loss of the listed companies and their consolidated companies; and
 - b. the annual management report gives a true and fair view of the position as per the balance sheet date and the state of affairs of the listed companies and their affiliated companies to which the report relates during the financial year and the principal risks the listed companies faces.

At the time of publication of the annual financial reports, the annual accounts do not already need to be adopted by the general meeting of shareholders. The annual financial report must remain publicly available for at least five years.⁵⁹

The annual accounts in principle comprise the consolidated accounts and the company annual accounts.⁶⁰ The requirement to prepare consolidated accounts – accounts which include the financial data of subsidiaries and other group companies or legal entities that these companies control – derives from Book 2 DCC.⁶¹ Consolidated annual accounts have to be prepared in accordance with IFRS.⁶² Dutch companies may, at their option, prepare their company annual accounts in accordance with Dutch GAAP, IFRS, or Dutch GAAP using the recognition and measurement principles set out in IFRS.⁶³

⁵⁹ Art. 5:25c (1) AFS.

⁶⁰ In the extremely rare case a listed company is not required to prepare consolidated accounts, the annual accounts must comprise the company's annual accounts.

⁶¹ Art. 101 (1) in connection with Arts. 361 (1) and 406 Book 2 DCC.

⁶² Art. 4 IAS Regulation (EC 1606/2002).

⁶³ Art. 362 Book 2 DCC.

3.3.2. Semi-annual Financial Information

Article 5:25d AFS implements Article 5 of the EU Transparency Directive, and requires Dutch listed companies to prepare semi-annual financial reports that include:

- (i) the semi-annual accounts;
- (ii) the semi-annual management report, including at least
 - a. an indication of important events that have occurred during the first six months of the relevant financial year, and their impact on the semi-annual accounts;
 - b. a description of the principal risks and uncertainties for the remaining six months of the relevant financial year;
 - c. major related party transactions;
 - d. statements of the persons responsible for the semi-annual financial report, with more or less the same information as in the statements on the annual financial information.

The semi-annual accounts do not need to be audited. If the semi-annual accounts have been audited or reviewed, the auditor's report must be made public together with the semi-annual financial report.⁶⁴ If the semi-annual accounts have not been audited or reviewed, this should be stated in the semi-annual management report.⁶⁵

The semi-annual financial reports have to be made public as soon as possible and at the latest two months after the end of the first six months of the financial year.⁶⁶ They must remain publicly available for at least five years.⁶⁷ If a company is required to prepare consolidated accounts, it must prepare its semi-annual accounts as well in consolidated form and in accordance with IFRS.⁶⁸

3.3.3. Interim Statements

Dutch listed companies are required to make public an interim statement during the first and the second half of their financial year.⁶⁹ This interim statement must contain information covering the period between the beginning of the relevant six-month period and the date of publication of the statement. It must provide an explanation of the important events and transactions that have taken place during the relevant period and a general description of the financial position and performance of the company and its controlled undertakings during the relevant period. The interim statements must be made public in the period between ten weeks after the beginning and six weeks before the end of the relevant six-month period.

3.3.4. Publication of Price-sensitive Information

Based on Article 5:25i AFS and Article 5:53 AFS, Dutch listed companies are required to promptly disclose price-sensitive information. The AFS defines 'price sensitive information' as any information of a precise nature, relating directly or indirectly to an issuer or to the trade in the financial instruments of the issuer concerned, which information has not been made public and publication of which could significantly affect the trading price of those financial

⁶⁴ Art. 5:25d (3) AFS.

⁶⁵ Art. 5:25d (4) AFS.

⁶⁶ Art. 5:25d (1) AFS.

⁶⁷ Art. 5:25d (1) AFS.

⁶⁸ Art. 5:25d (5) (a) AFS.

⁶⁹ Art. 5:25e AFS.

instruments (irrespective of any movement in price). Under specific circumstances, publication of price-sensitive information may be postponed.

3.3.5. Other Transparency Requirements

The AFS includes several other transparency requirements for Dutch listed companies. These requirements are:

- (i) publication of a prospectus if securities are offered to the public or admitted for trading on a regulated market in the Netherlands;⁷⁰
- (ii) publication of an annual disclosure document, including information on, or referring to, all information that the company has made generally available during the preceding twelve months pursuant to the securities supervision laws of any state;⁷¹ and
- (iii) prompt disclosure of all information on amendments to rights attached to a particular class of ordinary shares, such as changes in rights pursuant to the articles of association.⁷²

Besides these transparency requirements, listed companies are required to publish their strategy on their own websites.

3.3.6. Notification Requirements

The AFS provisions on the disclosure of holdings and capital interests in companies impose requirements on both the issuer and the holder of an interest. The most important requirement is in Article 5:38 AFS. This article provides for any person who acquires or transfers shares or whose voting rights are increased or diminished as a consequence of which his interest in the capital or voting rights reaches, exceeds or falls below – as he knows or should know – any of the thresholds of 5%, 10%, 15%, 20%, 25%, 30%, 40%, 50%, 60%, 75% and 95%, to promptly notify the AFM (the ‘numerator notification’). In addition, a person must notify the AFM if his interest in capital or voting rights reaches, exceeds or falls below any of these thresholds as a result of a ‘denominator notification’. The latter notification must be made not later than the fourth business day after the publication of the denominator notification in the AFM’s register.⁷³ As mentioned earlier, it is expected that the threshold of 5% will be lowered to 3% in the near future, and persons exceeding this threshold of 3% will be required to disclose whether or not they agree with the published strategy of the company. If these persons change their opinion on the strategy, this also has to be disclosed promptly.

A person who acquires or transfers one or more shares to which special controlling rights are attached (such as priority shares or ‘golden shares’) must forthwith notify this to the AFM. To make these notifications work in practice, listed companies must promptly notify the AFM if certain changes in their capital occur.⁷⁴ Companies also must periodically, i.e. within eight days after the end of each quarter, notify the AFM of changes in their capital in the previous quarter that did not result in a change in their capital totalling 1% or more. Finally, listed companies are to notify the AFM of changes in voting rights attached to their outstanding shares and of changes in the outstanding amount of depositary receipts for shares or similar tradable instruments that are or were issued with the relevant company’s cooperation.

⁷⁰ Art. 5:2 AFS.

⁷¹ Art. 5:25f AFS.

⁷² Art. 5:25h AFS.

⁷³ Art. 5:39 AFS.

⁷⁴ Art. 5:34(1) AFS.

There are several notification requirements for persons related to listed companies. Article 5:48 AFS requires notifications to be made in relation to the shares or voting rights held by members of the management and supervisory boards of listed companies. The most important notifications are the following:

- (i) a newly appointed member of management or supervisory board must notify his shares and voting rights to the AFM within two weeks after his appointment;⁷⁵
- (ii) a member of the management or supervisory board must forthwith notify the AFM of each change in his shares or voting rights. A notification must be made both in case of a change in the number and in the type of interest.

In addition to this requirement, a notification requirement under Article 5:60 AFS applies. Under this article, persons related to listed companies – such as management board members, members of the supervisory board and their spouses, registered partners, dependent children and other relatives who share the same household – are required to notify a transaction in shares in the capital of the company (or in financial instruments of which the price is co-determined by the price of these shares) to the AFM within five business days after that transaction. There might be – and often will be – concurrence between the disclosure requirements of members of the management and supervisory boards under Articles 5:60 and/or 5:38 AFS. Under certain circumstances no duplicate notifications need to be made.

4. Enforcement

4.1. Available Sanctions and their Relevance

4.1.1. Civil Law, Administrative Law, Criminal Law

The enforcement of corporate governance in the Netherlands can be described as a mixed model. Based on civil law, more in particular in company law, the (general meeting of) shareholders can influence the corporate governance of companies by using their approval rights for certain decisions. Also, enforcement ex post can take place, in the form of litigation by shareholders. Part C elaborates on this below.

Administrative law, on the other hand, plays a smaller role. Most enforcement decisions of the AFM are embedded in administrative law. These AFM decisions, however, usually are not related to direct subjects of corporate governance, but only involve corporate governance in an indirect way. For example, if the AFM imposes an administrative fine, or makes a company subject to an incremental penalty for not publishing information on time.

Criminal law hardly plays a role in enforcement of corporate governance in the Netherlands, although some forms of corporate conduct is subject to criminal liability. Two executive directors and one supervisory director of Royal Dutch Ahold NV have recently been held criminally liable for forgery in relation to the publication of consolidated accounts on the basis of fabricated control letters and were sentenced to pay criminal fines and, in the case of the former CFO of Ahold, to a prison sentence with probation.⁷⁶

An important enforcement tool of the AFM is based on the Act on Supervision of Financial Reporting (*Wet toezicht financiële verslaggeving*) ('ASFR'). Based on the ASFR, the AFM supervises the correct application of statutory accounting requirements by Dutch listed companies. The AFM has the authority to demand listed companies to provide

⁷⁵ Art. 5:48(3) AFS.

⁷⁶ Court of Appeal Amsterdam 28 January 2009, *NBStraf* 2009, 101-104.

information if the AFM doubts the correct application of the accounting requirements in annual or semi-annual financial reports. After having received the information,⁷⁷ the AFM can conclude that the reports do not satisfy the standards and recommend that the company make a public statement. Once the company in question has followed the AFM's recommendations, it must file the statement with the AFM. The statement will subsequently be included in the public register held by the AFM. If a company does not follow the AFM's recommendations, or does this to an insufficient extent, the AFM may request the Enterprise Chamber to order the company to further explain its financial reports.⁷⁸

4.1.2. Non-legal Sanctions, such as Naming and Shaming, Peer Pressure, Market Constraints

There is an element of a non-legal sanction in the 'comply or explain' principle, which is applied in the Corporate Governance Code. Companies subject to the Code must comply with the 'comply or explain' rule: that is, they must comply with its provisions or expressly explain any deviation from the Code. Expectedly, peer pressure will influence the decisions of companies to comply with the best practices.

Enforcement of the 'comply or explain' principle in the Corporate Governance Code cannot, strictly speaking, be seen as 'non-legal'. Dutch listed companies are required to include in their annual report a corporate governance statement in which they explain to what extent they apply the Code and explain any deviations. If a company does not include this statement, a shareholder can request the Enterprise Chamber to order the company to further explain its application of accounting requirements. Based on the ASFR, the AFM too can make this request to the Enterprise Chamber. In this way the AFM enforces, in an indirect manner, the 'comply or explain' principle in the Code. The Dutch legal framework is based on the assumption that the AFM does not assess the corporate governance of Dutch listed companies directly – that is to say: the AFM does not make its own judgement on the 'quality' of corporate governance of Dutch companies and does not assess the correctness of the corporate governance statement – but only indirectly, by assessing whether companies provide a corporate governance statement in which they set out their application of the Code. In practice, the AFM's supervision seems to take place in accordance with this assumption in the legal framework.

4.2. Supervision

4.2.1. Capital Market Authority and the Relevance for Corporate Governance

In the Netherlands, the AFM is viewed as the market supervisory and regulatory authority. The AFM has no direct involvement in corporate governance enforcement. However, its decisions in approving prospectuses and offer memoranda, as well as its ability to request the Enterprise Chamber to order companies to further explain their application of accounting requirements, do have relevance for corporate governance.

⁷⁷ If the company does not provide the information requested, the AFM may request the Enterprise Chamber on the basis of Art. 452 Book 2 DCC to obtain this information by means of a legal order. The fact that the AFM is making a request will be made public.

⁷⁸ Art. 447 Book 2 DCC.

4.2.2. Takeover Panel or other Self-regulatory Body

With regard to the regulation of takeovers in the Netherlands, the Enterprise Chamber and the AFM each have a role. The Enterprise Chamber may take provisional measures or issue orders if a party that acquires control refuses to make a mandatory bid. Supervision of the bidding process, including approving the offer memorandum, is exercised by the AFM. In addition, the tribunal on the basis of the Merger Code plays a role in the process of a takeover by or of a Dutch company. Besides these actors, there is no other self-regulatory body involved in takeover regulation in the Netherlands.

In the aftermath of the takeover of ABN AMRO, some politicians and scholars made a plea for introducing a takeover panel in the Netherlands. The suggested task and powers of this panel would be comparable to the UK Takeover Panel, for instance by having this panel be self-regulatory, with exclusive powers to regulate the takeover process, including the power to issue 'put or shut up' notices. Recently, the Minister of Finance stated that introducing a takeover panel in the Netherlands is likely to be unnecessary. The Minister stated that the current framework for regulation of takeovers, with roles for the Enterprise Chamber and the AFM, in principle is sufficient. However, some improvements of the takeover process seem to be desirable, in particular with regard to the length and orderly development of the process. The Minister therefore announced the introduction of a 'put up or shut up' rule in the Decree on Public Offers.

4.2.3. Relevance of Courts

Judicial intervention, in particular inquiry proceedings before the Enterprise Chamber, are extremely relevant for corporate governance in the Netherlands. Inquiry proceedings are discussed immediately below.

4.3. Shareholders

4.3.1. Inquiry Proceedings

The most effective mechanism at the disposal of shareholders to enforce rules and principles of corporate governance are inquiry proceedings before the Enterprise Chamber (Article 344-359 Book 2 DCC). As stated earlier, inquiry proceedings are an effective tool for shareholders to acquire information on the company's state of affairs and its management, which would otherwise not be available to the shareholders.

Inquiry proceedings proceed in two stages. In the first stage, a request is filed with the Enterprise Chamber to appoint one or more experts to investigate the policy of the company and the conduct of its business. The Court will award the request and grant an inquiry if there are sound reasons to doubt the policies of the company and/or the conduct of its business. If the request is awarded, the Enterprise Chamber appoints one or more investigators. The investigators produce a report that is filed with the Enterprise Chamber and is made publicly available if the report relates to a listed company.

In the second stage, the plaintiffs, the Attorney General in the public interest, and, in case of a listed company, any other party who meets the requirements to request an inquiry, may request the Enterprise Chamber to conclude that the report indeed demonstrates 'mismanagement' and to order remedies to address these problems. Such remedies can be far-reaching and may be, amongst others,

- (i) nullification of one or more resolutions of a corporate body of the company;
- (ii) suspension or dismissal of one or more managing or supervisory directors;
- (iii) appointment of one or more temporary managing or supervisory directors;
- (iv) temporary deviation from one or more provisions of the articles of association of the company;
- (v) temporary transfer of shares; and
- (vi) dissolution of the company (Article 356 Book 2 DCC).

Shareholders are entitled to file an inquiry request if they, individually or collectively, hold shares or depositary receipts representing at least 10% of the issued share capital or with a par value of EUR 225,000 (or less if provided for in the articles of association) (Article 366 Book 2 DCC). The Ministry of Justice has recently proposed that for large companies, the thresholds be amended such that shareholders will need to hold at least 1% of the issued share capital or shares with a market value of at least EUR 20 million.⁷⁹

In addition, inquiry requests may be filed by (i) trade unions representing persons employed by the company, (ii) persons empowered to do so on the basis of the articles of association or of an agreement with the company or (iii) the Attorney-General at the Court of Appeal in Amsterdam for reasons of public interest. A plaintiff should give advance written notice to the management board (and the supervisory board, if any) of his objections to the company's policy or the conduct of the business (Article 349 Book 2 DCC). Ample time should be given to the company to examine the objections and to address the underlying problems.

Finally, as mentioned earlier, the Ministry of Justice has also proposed that companies will be entitled to file an inquiry request.

Over the last 30 years, the Enterprise Chamber has developed a rich case law as to the question of what may amount to 'mismanagement'. This includes the purchase (or sale) of subsidiaries without a proper assessment of their value, transactions between the company and its directors without having secured that there is no conflict of interest, failure of the company and/or its directors to provide correct information to the general meeting of shareholders, neglecting the interests of minority shareholders, issuance of a controlling block of shares to a third party without sound business reasons, etc. An important category of cases relates to deadlocks in the board of directors, and often in those situations in the general meeting as well. Indeed, 'mismanagement' does not necessarily require acts by the board of directors. Decisions made by the shareholders' meeting, for example, are attributed to the company and may also be deemed 'mismanagement'.

In addition, when ordering an inquiry, the Enterprise Chamber may limit the scope of the investigation to a part of the company's policy or to a specific period in time. The inquiry may focus on the policy of (the members of) the managing board and/or supervisory board, but this is not always the case. It may in some cases focus on other corporate bodies of the company, or even on the role played by specific shareholders.

It is important to note that even before the Court orders an investigation and/or before the investigation has ended, the Court may order all provisional measures it may deem fit. Such provisional measures may include:

- (i) the suspension of voting rights of certain shareholders;
- (ii) orders not to execute certain resolutions or business decisions;
- (iii) the suspension of managing and/or supervisory directors, and

⁷⁹ The proposal is available at <<http://www.internetconsultatie.nl/enqueterecht>>.

(iv) the appointment of interim managing and/or supervisory directors.

The Court has repeatedly demonstrated a willingness to act fast and take rigorous action.

Inquiry proceedings are not meant to establish the liability of (former) managing and supervisory directors for damages that the company or shareholders may have suffered as a result of mismanagement. However, since the report drawn up by the investigators is likely to be made public, the plaintiffs or other claimants may use the information compiled in the course of the inquiry as evidence to support their claim for damages in other proceedings. In practice, inquiry proceedings appear to be a useful stepping stone for plaintiffs seeking damages from (former) managing and supervisory directors.

4.3.2. The Dutch Semi-‘class action’

There is a semi-‘class action’ under Dutch law pursuant to the Regulation for the Collective Settlement of Mass Damages (the ‘RCSMD’) (Articles 907-910 Book 7 DCC). Pursuant to this regulation, a settlement agreement for the compensation of damages caused by an event or by similar events, entered into by a foundation or association possessing full legal capacity with one or more other parties, who undertake thereby to compensate these damages, may, upon the joint request of the parties that have entered into the contract, be declared binding by a court upon the class of persons to whom the damages have been caused, provided that the foundation or association, by virtue of its articles of association, represents the interests of such persons. Persons to whom the damages have been caused also comprise those who have acquired a claim with respect to these damages by general or particular title. The RCSMD can be used by shareholders that have united under a foundation or association. The basis of the regulation, however, is a settlement agreement. The essence of the regulation is that this settlement agreement may be declared binding by a court on the class of persons to whom the damages have been caused. Therefore, this regulation differs widely from US-type class actions pursuant to which a class of shareholders can bring proceedings against an issuer. This is not possible in the Netherlands.

In addition, a foundation or association with full legal capacity may bring proceedings in the Netherlands for the protection of the interests of other parties (e.g. a group of shareholders), provided that this foundation or association, by virtue of its articles of association, represents the interests of such other parties (Article 3:305a-305c DCC). Under this rule it is not possible to claim damages. The RCSMD, however, can be combined with this possibility. For example, a foundation representing the interests of a group of shareholders may bring proceedings against an issuer, claiming a declaratory judgment that the issuer has acted wrongfully. If such judgment is awarded, the shareholders may each individually try to claim damages from the issuer on the basis of the declaratory judgment, but the foundation may also use the declaratory judgment to obtain a favourable settlement, which can subsequently be declared binding under the RCSMD.

For example, in proceedings instituted against World Online for publishing a misleading prospectus with EUR 3 billion damages as a result, a foundation that commenced proceedings against World Online received a declaration that World Online, and the underwriting banks, acted wrongfully against the shareholders. The next step would be to obtain a settlement and have this declared binding upon World Online, the underwriting banks and the shareholders that suffered damages.

Furthermore, the regulation for the RCSMD can be combined with other proceedings. With respect to the damages resulting from Shell decreasing its reserve estimates in the beginning of 2004, shareholders brought class actions in the U.S. to obtain damages. Then the non-U.S. shareholders, combined in a foundation, used the pressure on Shell in the U.S. class

action to obtain a settlement in the Netherlands and have it declared binding under the RCSMD.

4.3.3. Financial Misrepresentations

Managing directors can be held jointly and severally liable by shareholders for damage suffered as a consequence of a misrepresentation in the annual accounts, the annual report or interim figures (Articles 139 and 249 Book 2 DCC). An individual managing director can fend off liability if he proves that he cannot be held culpable for the misrepresentation, but the threshold for such proof is high, since giving a true and fair view of the financial condition of the company through the annual accounts, the annual report or interim figures is an elemental collective duty of the management board. Supervisory directors can be held liable as well for a misrepresentation in the annual accounts (Articles 150 and 259 Book 2 DCC), but not in the annual report or in interim figures. Shareholders rarely institute claims on the basis of Articles 139, 150, 249 or 259 Book 2 DCC. The combination with the semi-class action may, however, lead to an increased application of these provisions as a basis for collective settlements of claims based on misleading financial statements.

4.3.4. Other

Shareholders and other interested parties may try to force the company to organise the annual accounts and the annual report in accordance with statutory requirements (Article 447 Book 2 DCC). This can be done by filing a request to this extent with the Enterprise Chamber. In addition, the AFM may request the Enterprise Chamber to order a Dutch listed company to further explain its application of statutory accounting requirements (Article 447 Book 2 DCC).

Dutch law does not provide for derivative suits brought by shareholders against managing directors. This means that a shareholder cannot hold a managing director personally liable for breach of his fiduciary duties towards the company. A shareholder can, however, hold a managing director personally liable for breach of duties directly aimed at protecting the shareholder, but such liability is rarely established.

That the consent of the general meeting of shareholders is required for the management board to file for bankruptcy is included in the articles of association of many companies. Without this consent, the resolution of the management board to file for bankruptcy may be nullified by the general meeting of shareholders (Article 15 Book 2 DCC). In addition, a company can be dissolved by a decision of the general meeting of shareholders (Article 19 Book 2 DCC). This authority, however, does not play a major role in corporate governance.

4.4. Others

Two shareholder associations play an important role in Dutch corporate governance: VEB and Eumedion.

VEB is an association of securities owners. It aims to protect the interests of shareholders in listed companies through active participation in general meetings (VEB holds shares in most Dutch listed companies) and through legal actions such as inquiry proceedings. VEB often figures prominently in Dutch financial news and has been highly successful in several large court proceedings against, for example, Shell, Ahold, Unilever, Philips, Numico and World Online. Currently, VEB plays an active role in, *inter alia*, proceedings against Fortis. Recently, European Shareholders Group ('ESG'), an organisation of the former director of

VEB, entered the domain of Dutch corporate governance in the Fortis proceedings as well. ESG will possibly try to perform a role in Dutch corporate governance similar to VEB.

Eumedion represents the interests of institutional investors in the field of corporate governance. It is the most prominent voice of institutional investors in the Netherlands. It is the explicit objective of Eumedion to maintain and further develop good corporate governance in the Netherlands and Europe. Eumedion aims to achieve this objective by disseminating publications on shareholder participation in general meetings, encouraging joint consultations between institutional investors and listed companies, consulting with public authorities, and lobbying.

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