

PROTECTION OF MINORITY SHAREHOLDERS | COMMON SOLUTIONS IN DUTCH CORPORATE TRANSACTIONS

Power and control in a company ultimately depend on a shareholder's equity interest in the company and its representation in the board of directors. The larger the shareholding of a shareholder, the more influence it has.

From a shareholding of more than 50 percent of the share capital, a majority shareholder is in principle in a position to elect the board of directors and thus indirectly determine the course of the company's business. Minority shareholders can vote and have their perspectives heard, but as such and without further arrangements their votes are not enough to directly impact a company's decision. As such, minority shareholders face a continued risk of being out-voted by the majority shareholders at the shareholder level – and often at the board level.

These power relations and the often-conflicting interests of majority and minority shareholders can lead to the latter feeling at the mercy of the majority shareholder and the board of directors elected by the latter.

While Dutch law does prescribe minimum voting thresholds required for specific corporate actions and provides remedies for minority shareholders, the regulations are often not sufficient to strengthen the positions and rights of minority shareholders.

That is why investing in a company as a minority shareholder can be a cause of concern for many. In the Netherlands in particular, an exceedingly large number of listed companies is controlled by majority shareholders.

To mitigate such concerns and to create an improved framework for minority shareholder rights, minority shareholders may negotiate contractual protection

clauses to be incorporated in a company's governance documents.

This approach is also in line with recent developments in the Netherlands that, due to the growing shareholder base in the Netherlands and the increasing number of foreign professional investors in Dutch companies, the position of shareholders vis-à-vis the management board of a company is being strengthened more and more.

The most common minority protection clauses that can be put in either a shareholders agreement or the articles of association of a Dutch law capital company (BV or NV) are described on the next pages.



INFORMATION RIGHTS

Minority shareholders often do not have access to the company's books and financial information. As such shareholders do not have such right, only the general meeting of shareholders (algemene vergadering) has. However, only a full insight into operations allows minority shareholders to control spending and to verify that strategic plans are being implemented. Therefore, minority shareholders can negotiate a special right of access to company information and financial documents with reasonable notice and frequency. Linked in with access to financial records is the financial reporting. Monthly and quarterly reporting is common.

RIGHT TO CONVENE A GENERAL MEETING OF SHAREHOLDERS

On the basis of Dutch statutory law, the right to convene a general meeting of shareholders rests with the management board of a company or with the supervisory board, if one exists. It is possible to assign the convocation right to the (minority) shareholder. This can be done by specifically including it in the articles of association of the Company.

VALUATION

If a minority shareholder decides to exit the company and sell its shares, it is useful to establish a valuation method for the sale of these shares in order to adequately take into account the contributions of the minority shareholder and the value of the company at the time of the sale.

RIGHT TO APPOINT BOARD MEMBERS

In general, the board members run the company and make the business decisions, not the shareholders. Therefore, it is beneficial for minority shareholders to negotiate for a right to be appointed as a board member, to nominate a chairman, or at the very least appoint an observer at board meetings. To ensure strategic decision-making and to have independent members on the board, the right to appoint board members can be complemented by provisions which limit the size of the management board, protections against removal of board members, veto rights regarding specified material decisions or even weighted votes of the appointed chairman in the board meeting.



PRE-EMPTIVE RIGHTS AND RIGHTS OF FIRST REFUSAL

Pre-emptive rights ensure that any new shares shall first be offered to existing shareholders including the minority shareholders. This is intended to give minority shareholders the opportunity to participate pro-rata in future financing rounds.

Similarly, right of first refusal ensures that any shares sold by an existing shareholder shall first be offered to other shareholders before they may be sold to a third party.

Both of the above are mechanisms allow the minority shareholders to retain their percentage of equity in the company, to protect their ownership and to avoid dilution - to the extent the minority shareholder(s) has the funds to finance such equity. In this way, the shareholder group can be controlled.

PUT OPTIONS

In a minority investment the minority shareholder does not automatically control the exit process. A minority investor must therefore seek to set out in the shareholders' agreement a clearly defined process for exit that should include put options.

A put option gives minority shareholders the right to sell their shares to another shareholder in certain situations, e.g. in the event of deadlocks or if the company fails to achieve certain agreed milestones. Also, minority shareholders may even be faced with an unexpected discount on their share value – or even the impossibility to share – as no third-party buyers can be found who are interested in acquiring a minority interest. A put option clause then has the advantage that it essentially forces another shareholder to buy out the minority shares.

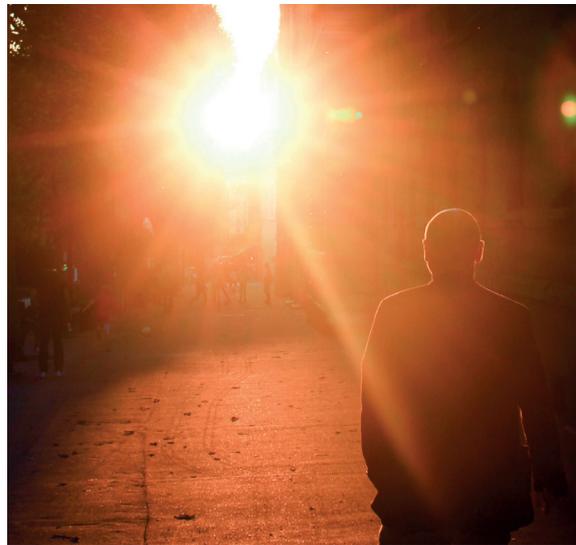
Importantly, a put option clause should not only regulate exactly in which case the shares will be acquired from the minority shareholder at, but also when the option can be exercised, such as upon the occurrence of any event or on a specified date, and when it expires.

TAG-ALONG RIGHTS

The purpose of tag-along-rights is that the majority shareholders who are planning on selling their shares must first allow the minority shareholders to participate in or 'piggy-back' onto the sale of shares on the same terms as the majority shareholders. This helps to protect a shareholder's investment especially in situations where the minority shareholders do not wish to remain in the company with an unknown new shareholder.

PREFERENCE SHARES

A preference share is a share to which various rights can be "attached", such as special voting rights or rights with regard to distributions (dividend). Preference shares are most commonly used by Private Equity parties but may in other transactions also be a useful tool for a minority shareholder.



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