Shareholder disputes in Dutch legal entities (with musical accompaniment)

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Below you will find a bird's eye view of some of the instruments available to shareholders in Dutch entities in the event of corporate disputes – with musical accompaniment, courtesy of the Rolling Stones.

Anybody Seen My Baby?

The Dutch jurisdiction is often chosen for holding companies in international structures. Reasons vary: for its prime location for business in Europe, for operational activities in the Netherlands, for tax reasons or because it is a neutral jurisdiction. The reputation of the Dutch judiciary is ranked among the most efficient, reliable and transparent worldwide. When a Dutch legal entity is chosen (e.g. as a group's holding company), Dutch corporate law will apply not only to the entity, but its corporate bodies as well, including the shareholders' meeting. National and international disputes between shareholders, disputes within the group structure and disputes between shareholders and the board of directors: all may be governed at least in part by Dutch corporate law. Shareholder disputes often contain similar facets whatever the financial interests at stake, and history almost always repeats itself.

One major difference with many other jurisdictions (in particular common-law jurisdictions) is that the Netherlands follows a stakeholder model rather than a shareholder model. A company's board of directors and supervisory directors are legally obligated to pursue the company's

corporate interests. Note that this also applies to trust directors. A company's corporate interests are comprised of the interests of all its stakeholders, including for example the interests of its employees, suppliers and creditors, and sometimes even the public interest. The corporate interests might change in different circumstances, such as financial distress. The corporate interests of a company are therefore not necessarily the same as the interests of its shareholders or even of the group to which the company belongs. The company's interests are usually determined primarily by what is considered necessary for the continued success of its business undertaking.

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When a group is involved, it could be argued that group policy is essential for that success. Indeed, the board of directors will not, without good reason, be allowed to pursue any policies that are wholly incompatible with the corporate group's strategy and in some situations will even be obliged to accept that the company's interests have to be subordinated to the interests of the group as a whole. However, group management is not free to always subordinate the interests of an individual company within the group to what it sees as the interests of the group overall. And even though the shareholders may include an instruction right for the board of directors in the articles of association of a Dutch private limited liability company, that board can never be obligated to act in conflict with the company's own interests. Equally, it is common to see shareholders agreements stating that specific shareholders may appoint one or more supervisory directors and that such directors must act in the interests of the appointing shareholders. The second part of that clause has little meaning in the Netherlands, if any at all: members of both the board of directors and the supervisory board are still legally obliged to act and make their assessments independently from the company's shareholders.

But that is not all. Dutch law states that legal entities and all parties involved in their organization (such as shareholders and directors) must behave towards each other in accordance with what is required by standards of reasonableness and fairness. Any rules that are in place

between them have no effect as far as their consequences, in the given circumstances, are unacceptable by standards of reasonableness and fairness. This legal principle plays a major role in almost all corporate governance litigation, and should therefore be top of mind even when the merest hint of a potential dispute arises and in any efforts to settle the dispute. It also entails that, although shareholders of a Dutch entity may act in their own best interests when exercising their voting rights, to a certain extent they will have to make allowance for the company's "own" interests and even take into account a duty of care towards other individual shareholders.

However carefully aligned parties may seem initially, interests can diverge at any given time. The future might not turn out as expected, or persons or parties might not perform as expected. Cultural differences could come into play. The level of trust and confidence in each other, once essential, becomes scarce. Deadlocks might arise and decision-making be impaired. Governance disputes, investment disputes and post-acquisition or partnership disputes can emerge. Where did that golden investment go? Anybody Seen My Baby? The need to intervene arises. Enter the lawyer.

Almost Hear You Sigh: the need for speed vs. careful drafting

The first step towards preventing disputes is careful drafting. So many misunderstandings about why parties do business with each other could be prevented with good contracts and articles of association. “Obviously,” I can already hear the reader sigh. But this is not so much about creating a legally strong position, although that of course also plays a role. Especially in international relationships where boilerplate language in one country might have a completely different impact in the Netherlands. Especially where the same language is already established through case law to have a different meaning (for example: the term “good faith”). But perhaps more than creating a strong legal position, it is about clarifying what the parties expect and want from each other. A Dutch court will always consider what the parties intended, not only in the context of an agreement, but also in the context of the workings of the Dutch legal entity itself. For example, in the case of a joint venture company, its interests are determined by the nature and content of the cooperation agreed between the shareholders. Determining the parties’ intentions is therefore of huge importance if litigation ensues in the Netherlands. Besides the above, clarifying expectations and preferences also plays a huge role in avoiding litigation altogether, because the parties are more aware of what they should and should not expect from each other.

This means looking beyond the sometimes urgent need or desire to get the deal done. Parties that trust each other – and want to avoid giving any impression to the contrary – are inclined to skip this part or to do it with a minimum of documentation. Like a couple who are engaged to be married, the parties might not want to stipulate terms that could imply that the possibility of the relationship going pear-shaped is even a serious consideration: why would you embark upon the relationship assuming that it will strand? Sometimes a shareholder thinks they can sort matters out if and when a problem arises. This is unfortunately often a misconception. Shareholders need to talk with and to each other and the board about their business principles, basic assumptions and expectations. The concern that this might come across as distrustful is misplaced. A professional and business-like approach is proper for making a business investment, and generally only inspires confidence. It is perhaps one of the greatest frustrations of lawyers: to see that a dispute that costs parties so much time and money and sleep could have been avoided quite easily.

As an aside: the quickest and cheapest route to a forced breakup of shareholders is by enforcing contractual obligations, for instance to offer shares in certain clearly specified circumstances, or shoot-out provisions. When reviewing dispute resolution clauses, keep in mind that shareholder disputes often arise when the need for action is pressing, for example when additional financing is urgently required. A good dispute clause includes the possibility for expedient action when the circumstances demand.

You Can't Always Get What You Want: negotiations

Sometimes a dispute simply cannot be avoided – no matter how carefully the agreements have been drafted. In that situation, it is important to make the most efficient use of the instruments that are available to the shareholder in those agreements, the articles of association, whatever internal rules and regulations are in place and possibly also sector-specific codes and the law. At the same time, for the purposes of risk management it is also important to keep an eye on building a sufficient paper trail. Shareholders should consider what the achievable and desirable goals are (including in the long term) and so determine a desired strategy. Do not simply pursue the short-term goals and think that the rest will be taken care of later. "The rest" might turn out to be a major obstacle in settlement efforts and litigation.

Good negotiations can ensure that shareholders achieve the desired solution without facing protracted and costly litigation. Negotiation is not about horse-trading or playing games. It is about understanding the conditions under which the other party will have an interest in reaching a particular agreement. This might be because you are in a stronger position from a legal perspective, but also because there are commercial interests at stake. What is important for one shareholder is not necessarily important for the other, and vice versa. If the other party is aggressive and/or litigious, it is important to anticipate their steps and take the necessary measures or carry out pre-emptive strikes. Of course, you will often need to compromise when finally settling. You can't always get what you want – no matter how much a shareholder is willing to invest in litigation.

Incidentally, all this does not mean that negotiating has to be a long process. Sometimes it can be very quick. It is possible to identify a quick route to a specific outcome, provided that you can make a good assessment of the other party, financially and psychologically. Take the Texas and Mexican shootout,

for example, or the fairest bid and Russian Roulette in the context of share transfers or deadlocks. Of course, more nuanced negotiation methods might also be appropriate – this is about breaking impasses, increasing control, enabling decision-making or investment financing opportunities, restoring relations, reaching an agreement on compensation or a definitive separation by means of an exit, demerger or transfer of shares. Like in any jurisdiction, a carefully thought-out strategy and realistic final objectives can take you a long way in negotiations. The fact that Dutch lawyers are generally more than happy to ”put the boot in” can – at appropriate times – work very well to get matters moving.

Start Me Up: enforcing the law

If there is no room or time to negotiate, or if a purely legal question is at stake, it might be time to start legal proceedings. Here, there are a multitude of routes and possibilities for shareholders, both as a corporate body and as individual shareholders (with both majority or minority interests): for example enforcing obligations to offer shares or expel shareholders, enforcing or blocking or setting aside decision-making, denouncing mismanagement, enforcing financing (including court-mandated financial injections) and dilution, forcing a demerger or simply holding shareholders

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liable. Disputes about the scope of information rights of individual shareholders (in particular minority shareholders) are also quite common, especially when other shareholders are represented on the board of directors or possess more or other information through other means. There are different routes for realizing those possibilities too, including the Enterprise Chamber, the regular courts, arbitration and the Netherlands Commercial Court. Before initiating any proceedings, however, it is a good idea to consider what best suits you and your situation and what steps should be taken to best prepare the ground for litigation.

Play With Fire: Immediate governance interventions, forced share transfers and denunciation of mismanagement

Using the Enterprise Chamber for shareholder disputes in an international context is a common phenomenon. The Enterprise Chamber is ideally suited for all types of governance disputes. The judges possess a thorough understanding of the legal practice and are highly versed in corporate law and related areas. The company's interests are leading for any dispute before the Enterprise Chamber, whereas in the regular courts the litigating parties' interests are. The proceedings focus on mismanagement and establishing who is responsible for it, but they are perhaps more frequently used – with the help of independent officers – to swiftly put matters to order. Once this is achieved, an investigation into mismanagement will then perhaps no longer be required. The Enterprise Chamber has a very wide range of immediate measures at its disposal. The Enterprise Chamber can intervene extensively, quickly, practically and effectively. One consideration, perhaps, is that the proceedings might in fact work against you as well: if you are not properly prepared, you could be playing with fire.

Although the Enterprise Chamber cannot directly obligate a shareholder to transfer their shares to another party, it is still the most effective route for achieving this. The Enterprise Chamber can be quite creative in this respect. The immediate relief granted by the court could ultimately result in a finalized transfer of shares. For example, the court might appoint an independent director with the authority to commence a bidding process or initiate a forced demerger. Alternatively, court-mandated financing might result in a significant dilution of a shareholder's stake, even in spite of contractual anti-dilution clauses. It might be that the shareholders have made arrangements about when shares must be transferred and who will transfer them. Discussions about the price for those

shares can become heated. The Enterprise Chamber may also be asked to determine the price of the shares. An expert is then usually appointed. The parties can request the court to give instructions on the valuation standard to be observed, the date by which the valuation must be made and other factors. If the parties are in disagreement about this as well, the court will decide on these subjects in fairness.

Time Is On My Side: commercial disputes (national and international) and compensation claims

The regular courts are a ideally suited for more commercial disputes, investment disputes and post-takeover disputes. It is possible to claim damages in the regular courts – unlike before the Enterprise Chamber. Courts can also be used to attach assets such as shares, bank accounts and evidence. Swift action is possible via summary relief proceedings. It is generally possible to obtain a judgment within a matter of weeks, depending on the true urgency of the matter, and that judgment might be far-reaching: examples exist of shareholders being ejected or compulsory purchases of shares being ordered in summary proceedings. If the case is not suitable for summary proceedings, e.g. if a declaratory judgment is sought, ordinary proceedings will need to be brought. Ordinary proceedings can take years, especially given the possibilities for appeal up to and including the Dutch Supreme Court. Anyone willing to commence litigation might need to be prepared for the long haul.

If an international dispute is involved and all parties prefer to litigate in English, they may choose proceedings before the relatively new Netherlands Commercial Court (NCC). The NCC also has a policy of handling business disputes more swiftly. One advantage of the NCC is that the parties may make procedural arrangements, there are clear English procedural rules and there is a somewhat closer alignment with international practices. However, all the parties involved must accept the NCC as the forum of choice.

Beast Of Burden: confidentiality and full cost recovery (arbitration)

International investors often prefer arbitration, though for some companies this is more out of habit than as a deliberate choice. A major advantage of arbitration (if successful) is that a full award of costs can be made, which is not the case in corporate law litigation. Another advantage is that the appointed arbitrators are often experts in the relevant area of the law. The greatest advantage of arbitration for investors is generally that the proceedings are confidential. That confidentiality is only relative, however, because

the names and the dispute could as yet come to light if a party tries to annul the arbitral award in court. Although the grounds for doing so are limited, the case law is public. Another disadvantage is that arbitration has its limitations. For example, decisions cannot be set aside in arbitration. An arbitration clause also does not rule out the possibility of litigating before the Enterprise Chamber, which has exclusive jurisdiction for certain corporate matters. Also, the degree of professionalism and the costs at the various arbitration institutes vary widely. An unconsidered choice for arbitration could in the end turn out not to be suitable.

If you do choose arbitration, then the Netherlands Arbitration Institute (NAI) might be a good choice. The NAI is professional, has a relatively large list of experienced arbitrators and is significantly less expensive than ICC arbitration, for example, and is therefore always a relatively safe choice. It also allows for expedient summary relief proceedings. A sufficiently detailed arbitration clause is essential in order to avoid unnecessary costs and uncertainty about jurisdiction.

It's All Over Now: conclusion

If a dispute arises or threatens to arise in the context of a Dutch legal entity, the shareholder is not left without recourse. Shareholders have a multitude of instruments at their disposal – both judicial and extrajudicial. However experienced the shareholder is, dealing with a dispute in the most efficient and effective manner requires specialist local knowledge. We possess that knowledge in plenty, and we are happy to share our expertise with you – with musical accompaniment, if you want.

If you have any questions about shareholder disputes and how to avoid them, about the role and position of shareholders' meetings and individual shareholders in the Netherlands, or about corporate dispute resolution in general, please contact *Marjon Lok*.

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You can also visit our website to find out more about the Corporate Litigation & Dispute Resolution team at DVDW.