# Private equity in The Netherlands: market and regulatory overview

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A Q&A guide to private equity law in The Netherlands.

The Q&A gives a high-level overview of the key practical issues including the level of activity and recent trends in the market; investment incentives for institutional and private investors; the mechanics involved in establishing a private equity fund; equity and debt finance issues in a private equity transaction; issues surrounding buyouts and the relationship between the portfolio company's managers and the private equity funds; management incentives; and exit routes from investments. Details on national private equity and venture capital associations are also included.

## Market overview

1. What are the current major trends and what is the recent level of activity in the private equity market?

### Market trends

From 2007 to 2019, private equity firms (including VC funds) invested in about 4,800 Dutch companies for a total invested value of EUR43.9 billion, according to the statistics kept by the Dutch Private Equity and Venture Capital Association (*Nederlandse Vereniging van Participatiemaatschappijen*) (NVP). In The Netherlands, most PE and VC deals are private M&A deals. There are, however, also portfolio companies that are engaged in IPOs and dual-track exits.

In the first half of 2020 PE and VC activities in The Netherlands were (relatively briefly) interrupted by the insecurities caused by the global 2019 novel coronavirus disease (COVID-19) pandemic, with lenders focusing on offering relief rather than acquisition lending, and with investors focusing on portfolio management rather than making new investments.

As the Dutch PE & VC market was briefly paused, PE portfolio companies too started cutting on expenses and focusing on decreased cash-outs, for example by trying to renegotiate rental obligations (Hunkemoller & GrandVision) or commercial terms with for example suppliers (Action). Some PE firms attempted to renegotiate deal terms or cancel deals altogether (NIBC & J-Club) leading to litigation, according to Dutch news sources (for example, the newspaper *Het Financieele Dagblad* (FD)).

By the end of the summer in 2020, the PE & VC market recovered at a fast pace. Market developments initiated before the Dutch Government's lockdowns, among others, a continuing increased usage of warranty and indemnity insurance in private M&A deals, were still on track. Exit periods for portfolio companies seemed to follow a trend of becoming shorter compared to previous years.

## Fundraising

The relatively fast recovery of Dutch PE and VC firms in 2020 can be partially attributed to these firms having plenty of cash available (”dry powder”). In 2020 this would have been about EUR10 billion in the Netherlands alone (*source: FD*).

Fundraising for VC firms (early stage, late stage (until Series D financing in the growth phase) and general ventures) amounted to EUR706 million in 2019, which was less than the EUR1,47 billion in 2018, but more than EUR473 million in 2017.

Fundraising for PE firms (for buy-outs) in 2019 amounted to EUR2.6 billion in aggregate, a significant increase compared to 2018 (EUR265 million), but below the peak of 2017 (EUR3.8 billion) (*source: NVP*).

Among others, Dutch PE firms Gilde, Egeria and Waterland raised record-high funds in recent years (*source: FD*):

- Gilde raised EUR1.5 billion at the beginning of 2019.
- Nordian Capital raised a EUR320 million fund in 2019 (and indicated that funds were quickly raised).
- Egeria raised EUR800 million in 2017.
- Waterland raised EUR2 billion in 2017 (and in 2020 EUR2.5 billion with its eighth fund).
- Avedon raised EUR300 million in 2017.

Different routes are also open: for example, AAC Capital decided not to set up a new fund, stating that it considers that companies in today’s market have become too expensive and that it will go to providers of funds on a transaction-by-transaction basis (*source: FD*).

## Investment

The total value of PE investments (as of Series D financing for the growth phase) increased from EUR4.2 billion in 2017 to EUR5.9 billion in 2018, with a new peak of EUR6.2 billion in 2019. The total value of VC investments (up to Series D financing for the growth phase) increased as of EUR389.6 million in 2017, up to EUR458.7 million in 2018 and EUR569.5 million in 2019. The total value of VC investments in the first part of 2020 amounted to EUR243.3 million (*source: NVP*).

PE investments in 2019 mainly concerned companies in the information and communications technology (ICT), healthcare and biotechnology sectors, and the business products and services and consumer goods and services industries, which is generally comparable to previous years.

A majority of the VC investments in 2019 concerned either healthcare and biotechnology sectors or ICT (*source: NVP*). In the complicated year that was 2020, in general, the M&A-tech sector managed to increase its presence compared to previous years: about 20% of all deals on the Dutch M&A market in 2020 involved M&A-tech deals, according to research from KPMG.

## Transactions

In 2019, 75% of the total number of buyouts and other divestments were conducted by Dutch PE firms; in 2018 this was slightly higher (78%).

In growth capital deals, these percentages were greater: 90% in 2019 and 82% in 2018. Previous years show similar numbers.

For VC investments specifically, Dutch venture capitalists conducted an even higher number of total VC investments: 93% in

 

2019 (compared to slightly lower numbers in 2018 (85%) and in 2017 (87%)).

The deal value of transactions by foreign PE firms is typically higher. Therefore, the total value of foreign buyouts and other PE deals in recent years was slightly higher than the total value of Dutch buyouts and other PE deals. For growth capital deals the total value of Dutch deals versus foreign deals show a similar trend. For VC investments, in terms of deal value, Dutch venture capitalists conducted 80% of the total investments in 2019, which is slightly more compared to 2018 (72%) and 2017 (76%) (*source: NVP*).

### Exits

The exits realised by PE funds in 2019 consisted primarily (in terms of value) of secondary buyouts by other PE funds (49%), and sales to third parties (36%). In terms of deal numbers, sales to third parties (35%), secondary buyouts by other PE funds (30%) were also the main drivers, but management buy-backs (19%) also made up a relevant share. This is line with past years: since 2007, these two categories have constituted the main exit methods, followed by IPOs (sale of listed instruments) and other exits. The exits realised by VC funds in 2019 consisted primarily (in terms of value) of sales to third parties (50%). This category increased compared to 2018 (39%) and 2017 (21%). In 2017 (in terms of value) secondary buyouts by other funds was the largest category (27%) for exits realised by VC funds (*source: NVP*).

2.What are the key differences between private equity and venture capital?

PE and VC firms in The Netherlands typically have similar sources of funding (*see Question 3*), fund structures (*see Question 5*), sector focus (*see Question 1*), disclosure requirements (*see Question 17*) and tax treatment (*see Question 4 and further*).

For the difference in focus on the investment stages between PE and VC funds, please see *Question 8*.

## Funding sources

3. How do private equity funds typically obtain their funding?

NVP research shows (in the figures that concern fundraising for PE firms domiciled in The Netherlands) that the fundraising for buyouts in The Netherlands for 2019 was primarily provided by:

- Funds of funds (23%).
- Pension funds (22%).
- Private persons (13%).

Other less significant sources for fundraising in buyouts included:

- Family offices.

- Governmental institutions.
- Banks.
- Insurance companies.
- Other asset management companies.

Fundraising for PE firms in The Netherlands during 2019 for growth capital was mostly provided by:

- Funds of funds (23%).
- Governmental institutions (19%).
- Banks (19%).
- Pension funds (14%).

Fundraising for VC firms in The Netherlands during 2019 was mostly provided by:

- Private persons (25%).
- Family offices (24%).
- Pension funds (23%).
- Governmental institutions (13%).

Fundraising for both buyouts and growth capital was primarily domestic in 2019 (39% and 59% respectively), followed by funds provided from other European countries (38% and 26% respectively) and funds from North America (both 15%). Previous years (growth capital) show a different pattern, in particular with relatively more funds coming from other European countries compared to domestic fundraising.

In 2019 fundraising for VC firms was primarily domestic (84%), followed by funds provided from other European countries (9%). In previous years, fundraising for VC firms was typically acquired from other European countries, while relatively less domestic fundraising was acquired.

## Tax incentive schemes

4. What tax incentive or other schemes exist to encourage investment in unlisted companies? At whom are the incentives or schemes directed? What conditions must be met?

### Incentive schemes

Dutch tax law provides for various schemes and arrangements that encourage investment in private companies.

Participation exemption. As a starting point, all income realised by Dutch resident companies is subject to regular corporate income taxation. However, dividends, currency results and capital gains can be exempted from corporate income tax if the participation exemption applies. To qualify for the participation exemption:

- The Dutch resident company must own at least 5% of the total nominal paid-up share capital of its subsidiary.
- That subsidiary must not be held as a low taxed portfolio investment subsidiary (unless it is considered a qualifying portfolio investment subsidiary).

A subsidiary is considered a “portfolio investment” if it is held with the aim of generating a return that can reasonably be expected from ordinary asset management. This is a factual test. The participation exemption should generally apply if either the:

- Shareholder is a top holding or intermediate holding company and the taxpayer can interfere in the policy-making, financial and/or strategic control of its subsidiary.
- Activities of the subsidiary are in line with the business enterprise carried out by its shareholder.

Moreover, a subsidiary qualifies for the participation exemption if either:

- The assets of the subsidiary consist (directly or indirectly) of less than 50% of low taxed portfolio investments.
- The subsidiary is subject to at least 10% corporate income tax on its profits on a Dutch basis.

Fiscal investment institution. If a Dutch resident company qualifies as fiscal investment institution (*fiscale beleggingsinstelling*) (FBI), the applicable corporate income tax rate is 0%. A FBI is subject to the ordinary 15% dividend withholding tax. However, a reduction of dividend withholding tax on profit distributions by the FBI may be granted where an applicable tax treaty applies.

To qualify for FBI status, several requirements must be met:

- The company must have the legal form of a public limited company (*naamloze vennootschap*) (NV), a private limited liability company (*besloten vennootschap*) (BV), a mutual fund (*fonds voor gemene rekening*) (FGR) or a similar qualifying entity which is established in accordance with the laws of Aruba, Curaçao, Sint-Maarten, BES islands, any EU member state or certain jurisdictions with which The Netherlands has concluded a tax treaty (containing an anti-discrimination clause).
- The activities of the company seeking to apply FBI status are limited to portfolio investment activities (although certain non-portfolio investment activities can be allowed).
- Debt funding is limited to 60% of the book value of the real estate held by the company and 20% of the book value of its other investments.
- Profits must mandatorily be distributed within eight months following the end of the financial year, unless a reinvestment reserve is formed, and certain other criteria are met.
- All share classes must share equally in the profits of the company.
- Finally (and most importantly), stringent requirements apply to the shareholders.

Exempt investment institution. The exempt investment institution (*vrijgestelde beleggingsinstelling*) (VBI) is another tax regime for portfolio investments that is commonly used. If the criteria for application of the VBI-regime are met, the company that applies the regime is exempt from corporate income tax. Furthermore, distributions by the company are exempt from dividend withholding tax. Various requirements apply in relation to the legal form and shareholder base of the company. Furthermore, the assets of the company seeking application of the VBI regime must consist exclusively of financial interests (real estate investments are excluded).

 

### At whom directed

The participation exemption is directed at investors that seek to own an interest of at least 5% in the respective subsidiary, and is typically used for more significant investments given its potential tax benefits. The FBI and VBI regime are usually applied by funds with a diversified investor base.

### Conditions

See above, *Incentive schemes*.

## Fund structuring

5. What legal structure(s) are most commonly used as a vehicle for private equity funds?

PE and VC funds in The Netherlands can be structured in both corporate entities (with legal personality) and contractual investment vehicles (without legal personality). The corporate entities (with legal personality) that can be used to structure PE and VC funds are the NV, the BV and the co-operative (*coöperatie*). Commonly used contractual investment vehicles (without legal personality) are the limited partnership (*commanditaire vennootschap*) (CV) or mutual fund (FGR). The choice of corporate entity or vehicle used is often based on tax considerations.

PE and VC funds are, irrespective of their legal structure, regulated entities, and as such PE and VC funds qualify as alternative investment funds (AIFs) within the meaning of Directive 2011/61/EU on alternative investment fund managers (AIFM Directive). The AIFM Directive has been implemented in the Dutch Financial Markets Supervision Act (*Wet op het financieel toezicht* (FMSA)) and delegated decrees and regulations.

In the event that a PE or VC fund which is subject to the full AIFM Directive regime (*see Question 9*) is structured as a contractual investment vehicle (and not as a corporate entity), Dutch law stipulates that the legal ownership of the AIF's assets must be held by a separate entity which has the holding of such assets as its sole statutory object. The AIF's assets form a separate capital for the purpose of both:

- Debts relating to the management, custody and legal ownership of the assets of that AIF.
- Participation rights (*rechten van deelneming*).

Usually, a Dutch foundation (as a special purpose vehicle (SPV)) is incorporated to hold the AIF's assets. Contractual arrangements are made to ensure that the SPV has the legal title of the AIF's assets, which it holds for the risk and account of the AIF. The alternative investment fund manager (AIFM) of the AIF will typically be granted a power of attorney by the SPV to act on behalf of the SPV with respect to the assets the SPV holds on behalf of the AIF.

6. Are these structures subject to entity level taxation, tax exempt or tax transparent (flow through structures) for domestic and foreign investors?

Most legal forms for fund structures are non-transparent for Dutch tax purposes. Entities incorporated under Dutch law are subject to corporate income tax by virtue of their incorporation. Accordingly, taxation in principle takes place with the respective entity. However, due to application of the participation exemption (*see Question 4, Incentive schemes*), income received by domestic entities from their participations (including capital gains and dividends) is often exempt from Dutch taxation, allowing for a tax-friendly exit of the subsidiary or receipt of dividends by the shareholders.

Alternatively, fund structures use a closed-CV or closed-FGR as main fund entity. If set up properly, such CV or FGR is deemed transparent for Dutch tax purposes, as a result of which income received by the CV or FGR is deemed to be received by its respective participants. However, to maintain the closed character of a CV or FGR, stringent restrictions apply to the transferability of interests in the CV or FGR.

7. What foreign private equity structures are tax-inefficient in your jurisdiction? What alternative structures are typically used in these circumstances?

From a Dutch tax perspective, foreign partnerships (for example, a Cayman Islands limited partnership) are usually considered non-transparent, as opposed to their foreign classification as tax transparent. Direct investments by such vehicles are typically less attractive for Dutch tax purposes. Often, these types of investments are structured through legal entities that are tax residents of a tax treaty jurisdiction. The Netherlands has strict rules to combat tax-abusive structures.

## Fund duration and investment objectives

8. What is the average duration of a private equity fund? What are the most common investment objectives of private equity funds?

### Duration

The average life of PE funds in The Netherlands differs based on several factors, which include, among other things, the size, the investments and the rates of return of such funds. A majority of funds follow global trends, having a life cycle of approximately ten to 12 years, generally with the possibility to extend that life cycle (with appropriate consents).

### Investment objectives

In general, PE funds have a main objective of investing in target companies in order to maximise their return on investment in the event of an exit (typically occurring between five to seven years after acquisition of a target company).

Similarly to other jurisdictions, PE funds typically measure their returns on investment based on their internal rate of return for investments and/or divestments over the period of their life cycle.

Based on the nature of VC and PE investments, investment stages differ. VC investments pertaining to start-up and scale-up companies usually allow investors to invest in several phases/financing rounds (seed capital, Series A (early stage), Series B (growth) and Series C (later growth)) resulting into an IPO or sale. By contrast, mid- to long-term investments of PE firms usually occur in the growth phase (as of Series D financing/investment) and forward (*source: NVP*).

For VC investments in the seed capital phase, the Dutch government has a Seed capital scheme in place. This scheme aims to support technical and creative start-ups. The government provides an interest-free loan to an investment fund for minimum investments between EUR100,000 and EUR3.5 million with a maximum term of 12 years, provided that at least three shareholders invest at least the same amount in the start-up and certain other criteria are met (*source: Netherlands Enterprise Agency (RVO)*).

## Fund regulation and licensing

9. Do a private equity fund's promoter, principals and manager require authorisation or other licences?

In general, EU AIFMs must be authorised by the competent authorities of their home member state. In The Netherlands, the competent authority that grants licences to Dutch AIFMs is The Netherlands Authority on the Financial Markets (AFM). Under this licence, these AIFMs can manage and market AIFs in the EU by completing a notification procedure and successfully obtaining an "EU passport".

However, Dutch AIFMs are exempt from the obligation to obtain this licence where the assets under their management do not exceed a total threshold of either:

- EUR100 million.
- EUR500 million (in the case of unleveraged AIFs that have no redemption rights exercisable during a period of five years from the date of the initial investment in the AIF).

If one of the above two thresholds is met, in addition the AIFM must offer participations exclusively in one of the following ways in order to benefit from the licensing exemption:

- To professional advisors within the meaning of the AIFM Directive.
- To less than 150 persons.
- In denominations of EUR100,000 or more.

AIFMs meeting these criteria are exempt from the requirement to obtain a licence, but must be registered and are subject to certain information requirements and anti-money laundering/counter terrorist financing requirements. This regime is often referred to as the "light regime" or the "registration regime". No EU passport is available for AIFMs making use of this light/registration regime. A large number of Dutch PE fund management companies are subject to this light/registration regime.

For AIFMs not incorporated in an EU member state (that is, "third country" AIFMs), a different regime (the Dutch National Private Placement Regime (NPPR)) is available, provided that the relevant conditions are met.

For VC funds (and as of 1 March 2018 also for a wider range of AIFMs), the European Venture Capital Fund (EuVECA

 

(Regulation) (EU) 345/2013, as amended by Regulation (EU) 2017/1991) allows venture capital managers to raise funds across Europe with an EU-wide marketing passport, without having to follow the NPPR, if certain requirements are met. The EuVECA regulation is addressed to AIFs that focus on portfolio companies which are start-ups or other early-stage companies.

10. Are private equity funds regulated as investment companies or otherwise and, if so, what are the consequences? Are there any exemptions?

## Regulation

See *Question 9* for details of the regulation of AIFMs of PE and VC funds.

No separate licence is required for the PE or VC fund itself, although each PE and VC fund must be registered under the licence of the relevant AIFM. However, in the event of internally managed AIFs (structured as a corporate entity), the AIF itself must be licensed (as there is no separate AIFM).

AIFMs must be duly authorised to market/offer the relevant AIF in The Netherlands (including the use of marketing materials to do so). AIFs are subject to the rules for marketing/offering materials as set out in the Dutch Financial Markets Supervision Act (*Wet op het financieel toezicht* (FMSA)). Marketing materials must not contradict obligatory information provided to such investors, most importantly information included in the prospectus.

Additional rules apply in relation to AIFs marketed to non-professional investors under the Decree on Conduct Supervision FMSA (*Besluit Gedragstoezicht financiële ondernemingen Wft*) and the Further Regulations on Conduct Supervision FMSA (*Nadere Regeling Gedragstoezicht financiële ondernemingen Wft*). Moreover, Regulation (EU) 1286/2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs Regulation) and the Unfair Commercial Practices Act (*Wet oneerlijke handelspraktijken*) also apply.

Finally, all marketing materials addressed to (potential) clients (both professional and non-professional) must be fair, clear and not misleading.

## Exemptions

See *Question 9*.

11. Are there any restrictions on investors in private equity funds?

See *Question 9*. Otherwise, the applicable regulations governing the AIFM/AIF do not contain any such specific restrictions.

Based on the legal form of the investors in PE funds, there are typically specific restrictions that apply to the PE fund's investors from a corporate law perspective (for example, a BV must have a minimum of one shareholder).

Furthermore, the PE fund's articles of association, terms and conditions, fund regulations and/or equivalent documents may include specific requirements that apply to the PE fund's investors.

12. Are there any statutory or other maximum or minimum investment periods, amounts or transfers of investments in private equity funds?

PE funds in The Netherlands are not subject to any laws or regulations that prescribe maximum or minimum investment periods, amounts or transfers of investments in PE funds. However, these matters may be governed by the PE fund's articles of association, terms and conditions, fund regulations and/or equivalent documents.

13. How is the relationship between the investor and the fund governed? What protections do investors in the fund typically seek?

As mentioned in *Question 11* and *Question 12*, the relationship between PE funds and investors is typically regulated by the PE fund's articles of association, terms and conditions, fund regulations and/or equivalent documents. No specific "best practices" for PE funds and their relationship with their investors apply in The Netherlands. However, the Dutch private equity and venture capital association (*Nederlandse Vereniging van Participatiemaatschappijen*) (NVP) and the Dutch Fund and Asset Management Association (DUFAS) regularly provide information that may be relevant for PE funds. The same applies for VC funds.

Key investor protections include arrangements relating to:

- Key person events.
- Removal of the manager (with cause and without cause (no-fault divorce)).
- Change of control provisions.
- Indemnification.
- Conflicts.
- The role/operation of the Investor Advisory Committee or similar body.
- Reporting provisions.
- The application of the "most favoured nation" treatment.

## Interests in portfolio companies

 

14. What forms of equity and debt interest are commonly taken by a private equity fund in a portfolio company? Are there any restrictions on the issue or transfer of shares by law? Do any withholding taxes or capital gains taxes apply?

## Most common form

Both Dutch and non-Dutch PE funds' investments in Dutch portfolio companies are commonly structured by using a bid vehicle which acquires the shares in a target company. The PE fund will typically invest indirectly by obtaining ordinary shares and fixed return cumulative preference shares in the capital of the bid vehicle. In general, the bid vehicle maintains both debt and equity instruments, typically determined on a case-by-case basis. Levels of debt/equity held by a fund may be determined by external factors, such as bank lending criteria for third party financing.

Dutch and non-Dutch VC funds' investments in Dutch portfolio companies are typically also structured by using a bid vehicle or vehicles for the VC investors to (indirectly) hold (depositary receipts of) shares in the capital of the portfolio company. There is a larger focus on equity instruments compared to PE funds' investments.

## Other forms

PE funds sometimes opt to provide convertible or non-convertible shareholder loans or bonds. Less common are priority shares or shares of certain classes (which may be shares with specific voting rights or veto rights). By contrast, for VC funds it is not uncommon to work with shares of certain classes to differentiate between the several rounds of investments (seed round and several rounds of financing resulting into the issuance of (different classes of) shares in the capital of the portfolio company).

## Restrictions

Transfer restrictions for shares are typically included in the bid vehicle's or portfolio company's articles of association (for example, pre-emptive rights for other shareholders, or general meeting consent). However, Dutch corporate law does not require such restrictions to apply.

Other specific provisions regarding transfers, (the exclusion of) pre-emptive rights and rights of first refusal are customarily laid down in the articles of association or contractual arrangements between shareholders (for example, a shareholders' agreement) on the bid vehicle level (or portfolio company level, if no bid vehicle is incorporated).

## Taxes

In addition to commercial drivers, tax considerations also play an important role for PE (and VC) investments when determining the desired level of debt/equity. Unlike dividends, interest incurred on loans is in principle deductible for Dutch corporate income tax purposes, thereby reducing the taxable basis. The Netherlands has detailed legislation that may restrict interest deductibility. For example, if certain conditions are met, a loan can be deemed equity for Dutch tax purposes, preventing interest deductibility.

Dutch tax law further provides for interest non-deductibility provisions that are aimed at "tainted transactions", as well as a generic earning stripping provision that seeks to mitigate the effects of base erosion by limiting interest deductibility to the highest amount of either:

- 30% of the taxpayer's EBITDA.

- EUR1 million.

Conditions apply to back-to-back financing companies and to be eligible to obtain a tax ruling from the Dutch tax authorities on the acquisition (and funding) structure.

The Netherlands levies a 15% withholding tax on dividend payments (although a reduction or exemption typically applies under domestic law or an applicable tax treaty). No withholding tax on arm's length interest payments is levied, making debt funding relatively attractive as compared to equity funding. Interest paid to related parties that is not considered at arm's length (that is, interest that is excessive) can be treated as a (deemed) dividend and accordingly become subject to withholding tax.

Further, as from 2021, a conditional withholding tax of 25% in respect of interest payments to related parties in certain designated low-tax or non-cooperative jurisdictions (including payments made as part of abusive arrangements) applies. Special attention is required when transparent entities are used in the investment structure. The foregoing may require certain PE and VC funds to revisit their acquisition and financing structure for investments in The Netherlands.

Finally, Dutch tax law contains specific provisions targeting abusive situations. Such abusive situation may be present if an individual directly or indirectly owns an interest of 5% or more in a Dutch company and artificially interposes one or more non-Dutch entities between himself/herself and the Dutch company to avoid Dutch taxation (for example, by invoking EU law or tax treaty benefits). If applicable, Dutch corporate income tax is due on income derived by the non-Dutch resident from its shareholding in the Dutch company. The criteria for these provisions are detailed and often change and should be monitored closely. Under certain conditions, taxpayers can discuss the tax aspects of their investments in advance with the Dutch tax authorities and seek certainty through a tax ruling.

# Buyouts

15. Is it common for buyouts of private companies to take place by auction? Which legislation and rules apply?

Although no specific data is available, it is common for buyouts of private companies to be concluded through an auction process. The most relevant applicable regulations are those on the prohibition on offering equity instruments to the general public.

A typical auction process for buyouts of private companies is further set out in *Question 17*.

16. Are buyouts of listed companies (public-to-private transactions) common? Which legislation and rules apply?

Buyouts of listed companies are less common than buyouts for private companies (the number of private companies far exceeds the number of public companies), but the number of PE funds showing an interest in Dutch public companies does appear to be on the rise. In addition, there seems to be an appetite to list Dutch and non-Dutch companies (such as Universal

 

Media Group and Coolblue) to the Amsterdam stock exchange (*source: FD*).

For public bids, the FMSA and the Dutch Civil Code apply. Furthermore, specific rules regarding the timetable, the offer memorandum and announcements are included in the Public Bid Decree (*Besluit openbare biedingen*). For securities subject to a public bid on regulated markets in The Netherlands the AFM is the regulatory authority. The authority of the AFM as regulator is based on the jurisdiction in which the target company is incorporated; other regulators in the EEA could have authority instead of the AFM. The Enterprise Chamber (*Ondernemingskamer*), not the AFM, has the power to rule on whether a mandatory bid is applicable. Specific laws and regulations may also apply to certain sectors (for example, the financial sector, the energy sector and/or other vital sectors).

## Principal documentation

17. What are the principal documents produced in a buyout?

## Acquisition of a private company

For buyouts of private companies in The Netherlands the principal documents are usually similar to the types of documents used in private M&A deals in other jurisdictions. In auction processes, following the "teaser" phase, bidders are commonly required to sign a non-disclosure agreement (NDA) (NDAs are also normally used in one-on-one transactions).

More often than not, in one-on-one transactions, the parties enter into a letter of intent or "heads of agreement" type agreement (setting out principal envisaged terms, and, where relevant, exclusivity arrangements) before the negotiation and conclusion of a share and/or asset purchase agreement, and (where relevant) a shareholders' agreement.

Depending on the specifics of the transaction, ancillary documents may be needed (for example, management or employment agreements, IP assignment agreements, service level agreements/disentanglements for carve-outs, escrow arrangements, and so on). For a transfer of shares in a Dutch BV, a notarial deed of transfer must be executed.

The documents set out above are typically confidential and not required to be made publicly available.

## Acquisition of a listed company

For buyouts of listed companies in The Netherlands strict bid rules apply. Generally, the parties will first enter into a merger protocol, which typically sets out the provisions governing the process of the bid, which also prescribes for certain documents to be made publicly available as part of the process.

## Buyer protection

18. What forms of contractual buyer protection do private equity funds commonly request from sellers and/or management? Are these contractual protections different for buyouts of listed companies (public-to-private transactions)?

 

PE funds typically request seller's warranties regarding the target group's business and may also request specific indemnities to be included in the transaction documents (a tax covenant/tax indemnity is fairly standard). Warranty and indemnity insurance is often used to offer protection for the buying party while allowing the selling party to achieve a clean exit.

It is not necessarily uncommon to base part of the purchase price on earn-out provisions, but experience is that parties tend not to favour this type of arrangement.

For roll-over situations, where a seller re-invests part of the transaction proceeds, it is not uncommon to see ratchets based on money multiples or on the internal rate of return.

Shareholders' agreements typically arrange for contractual anti-dilution protection for shareholders (not specific to the investor's rights). PE funds usually arrange for specific provisions in shareholders' agreements on information rights, the right to force a future exit and provisions typically relating to a majority shareholder's position (for example, consent rights for material decisions taken within the group).

In the context of venture capital transactions, anti-dilution rights for investors are more common; full ratchet protection is not standard as most venture capital investors tend to be willing to accept (broad based) weighted average protection.

19.What non-contractual duties do the portfolio company managers owe and to whom?

Managing directors must at all times act in the interests of the company and its stakeholders as a whole, which includes the company's shareholders and also, for example, its employees, suppliers and customers. Managing directors are not required to follow the instructions of the general meeting, let alone individual shareholders, if doing so would not be in the interests of the company and its stakeholders as a whole. Managing directors are fairly autonomous in this respect.

Managing directors are required to exercise their duties with at least such level of expertise and care as may be expected from any suitable, skilled and diligent managing director. In general, it is very common to include the manager's duties to the company within the relevant contractual agreements (*see Question 20*).

In relation to a management buyout, it is not uncommon to include the relevant (confidentiality) obligations of the managing directors that are intending to participate in a buyout in a letter of intent and/or term sheet for the management buyout. These documents could also set out the procedures of conduct for such managing directors towards potential investors.

20. What terms of employment are typically imposed on management by the private equity investor in an MBO?

 

The employment of managers is typically arranged for at a bid vehicle or portfolio company level. Managers can either be engaged based on a management agreement or an employment agreement, which will typically contain details including salary, function description, restrictive covenants (non-competition and non-solicitation), confidentiality provisions, and a tax indemnity for any social security premiums and fines (in the event of a management/service agreement).

Arrangements regarding managers' (indirect) co-investment are customarily arranged for in a separate management participation scheme or incentive plan, which will usually include good leaver/bad leaver (and sometimes early leaver) provisions, vesting schemes and/or other performance-related arrangements. They are, for tax purposes, not intended to be part of the employment terms.

21. What measures are commonly used to give a private equity fund a level of management control over the activities of the portfolio company? Are such protections more likely to be given in the shareholders' agreement or company governance documents?

In general PE funds could ensure that a (supervisory) director's seat in the portfolio company's (supervisory) board will always be filled by a person appointed by the PE fund. Further, PE funds tend to implement reserved matter lists (consent rights on certain material commercial matters), with consent rights resting directly with the PE fund, or with certain or a majority of non-executive or supervisory directors. This is often laid down in management regulations but can also be placed in the articles of association of a company; as an amendment of the latter involves a notarial deed and is therefore more costly, the former option is normally preferred. The company's articles of association are publicly available but that is, for this purpose, normally not an objection.

## Debt financing

22. What percentage of finance is typically provided by debt and what form does that debt financing usually take?

Financing by debt can typically be obtained from both third parties (such as banks) and investors. Debt finance in Dutch PE deals is primarily made available in the form of senior debt provided by Dutch banks, but foreign banks are also present and active in the region. Next to senior debt, and perhaps to a somewhat lesser extent, debt finance is made available in the form of mezzanine finance provided by mezzanine-debt funds or banks.

Acquisition financing in The Netherlands is, in general, arranged for by the buyer, and not pre-arranged by the seller (stapled financing).

If funding requirements cannot be met by attracting senior debt and/or mezzanine finance, then vendor loans can be (and are regularly) used to meet the funding gap.

Leverage ratios depend on the investor, the industry and the relevant tax aspects.

### Lender protection

 

23. What forms of protection do debt providers typically use to protect their investments?

## Security

Depending on the debt finance provided by a third party, security rights are vested to securitise the PE fund's payment obligations under such debt finance. In The Netherlands, banks typically request security in the form of rights of pledge over shares (with the condition subsequent that voting rights on such shares may be exercised by such bank in the event of a default). Other security will depend on the type of business but can include a pledge over assets such as intra-group receivables, IT and IP rights, bank accounts, stocks and/or insurances, or rights of mortgage over real estate and/or other fixed assets. If there are multiple obligors, it is common that cross guarantees are put in place. Ringfencing typically excludes the PE fund and occurs on a lower level.

## Contractual and structural mechanisms

Financing packages can include senior, mezzanine or junior financing with lenders entering into intercreditor arrangements regulating how to enforce their rights and/or security against the borrower. Structural subordination is also common with financing being provided at different levels of the structure.

## Financial assistance

24. Are there rules preventing a company from giving financial assistance for the purpose of assisting a purchase of shares in the company? If so, how does this affect the ability of a target company in a buyout to give security to lenders? Are there any exemptions?

## Rules

For BVs, the financial assistance restrictions set out under Dutch law were abolished from 1 October 2012.

For public companies (NVs) the financial assistance rules remain in force, stipulating that NVs and their subsidiaries:

- Are not allowed to provide securities and/or guarantees for financing used to acquire shares in an NV.
- May not provide loans to third parties to acquire such shares in an NV.

The practical impact of the financial assistance rules for PE deals in The Netherlands is limited, as the number of BVs used in The Netherlands is relatively far higher than NVs.

General Dutch corporate law principles (for example, corporate benefit and board duties) also come into play in assessing whether a company can enter into a transaction involving financial assistance (a detailed review (including liquidity forecasts) is required, to show the continued ability of a company to pay its debts as they fall due).

## Exemptions

There are a few exemptions to address the financial assistance rules for NVs, which are not further discussed here as, in practice, such exemptions hardly ever apply in a PE deal structure.

## Insolvent liquidation

25. What is the order of priority on insolvent liquidation?

Insolvency procedures in The Netherlands are primarily governed by the Bankruptcy Act. In general, in the event a company is declared bankrupt, by law, the ranking of the company's stakeholders (including the company's creditors) is determined in accordance with Dutch law, as follows:

- Creditors with a right of pledge, mortgage or retention right are typically secured creditors and can exercise their rights as if the company has not been declared bankrupt.
- The Dutch Tax Authority has a preferential right relating to certain assets (movable properties).
- The Dutch Tax Authority, the Employee Insurance Agency (*Uitvoeringsinstituut Werknemersverzekeringen*) (UWV) and the company's employees with a claim for loan payments (where that right of claim existed prior to the bankruptcy), who are typically preferential creditors.
- Unsecured creditors.
- Estate creditors.

In general, payments to creditors with a preferential right are ranked above payments to unsecured creditors. Unsecured creditors should typically be treated on equal terms. For financial instruments, more specific Dutch law regulations have been concluded in the Decree on Conduct Supervision FMSA (*Besluit Gedragstoezicht financiële ondernemingen Wft*).

As of 1 January 2021, a new law on the confirmation of private restructuring plans entered into force. This law, which sets up a Dutch pre-insolvency procedure (*Wet homologatie onderhands akkoord*) was inspired by the scheme of arrangement under the UK's Companies Act 2006 and Chapter 11 of Title 11 of the US Bankruptcy Code. The new law allows for the provision of a plan offering to prevent a debtor's insolvency. It intends to combine a fast and flexible framework for the conclusion of pre-insolvency schemes with a high degree of deal certainty.

## Equity appreciation

26. Can a debt holder achieve equity appreciation through conversion features such as rights,

 

warrants or options?

Yes: debt finance arrangements can include convertible debt instruments, warrants or options, (convertible) bond loans and/or financial instruments (for example, debt/equity swaps) to achieve equity appreciation through the conversion of debt into equity.

The upside to these arrangements is mainly only achieved upon conversion, based on which the debt instrument follows the valuation of the shares (or other equity instruments) it is converted into.

## Portfolio company management

27. What management incentives are most commonly used to encourage portfolio company management to produce healthy income returns and facilitate a successful exit from a private equity transaction?

Most commonly, PE funds structure management's participation through a trust office foundation (*Stichting Administratiekantoor*) (STAK), which holds the equity interests in the company and issues depositary receipts of shares to participating managers. A VC fund typically uses the same structure for its investors and managers. The STAK is the legal owner of the relevant shares and is entitled to exercise the voting rights on such shares, and to co-operate in a sale of the shares (the exit). The STAK board tends to be controlled, or at least co-directed, by the PE or VC fund.

In the event managers hold shares directly in the bid vehicle, this may be structured using shares without voting rights (but with the right to participate in the company's shareholders meetings).

Management incentives are typically structured by giving managers the chance to invest in the institutional strip based on similar terms as the PE fund's institutional strip, with sweet equity being made available or a ratchet arrangement applying. VC funds also provide managers with (option rights to) shares and/or the possibility to invest in future funding/financing rounds.

28. Are any tax reliefs or incentives available to portfolio company managers investing in their company?

There are no specific tax reliefs or incentives available to portfolio company managers investing in their company. However, the Dutch personal income tax system is organised in such way that, if properly structured, the beneficial "Box III" regime applies to investments by portfolio managers. If this Box III regime applies, income tax is levied on the net asset value of the assets on 1 January of the relevant fiscal year, with an effective tax rate varying between 0.59% and 1.76% (in 2021). As opposed to this tax-friendly treatment, Box I taxes the actual income from employment at progressive rates of up to 49.5%. Finally, Box II taxes income derived from a substantial interest (generally a shareholding of at least 5%) in a Dutch (holding) company at a flat rate of 26.9%.

Based on the foregoing, from a Dutch income tax perspective, it is most efficient for a portfolio manager to hold an equity investment that is taxed in Box III (portfolio investment) due to the relatively low effective tax rate as compared to Box I or Box II. For this reason, the Dutch legislator introduced specific rules relating to carried interest investment schemes for management, advisors or other individuals performing activities for an underlying Dutch business. If a carried interest investment scheme falls within the scope of these specific rules, income derived from such investment is subject to income tax in Box 1 at a maximum rate of 49.5%. These carried-interest rules, however, do not apply if the income derived from a carried interest is both:

- Held through a qualifying management holding company of the individual owning a direct or indirect substantial interest (that is, 5% or more) in the relevant Dutch entity.
- This income or capital gain is, upon realisation, immediately (that is, within the same calendar year) and fully (that is, 95% or more) distributed by the holding company to the manager.

In principle, this structure enables a Dutch manager to effectively realise a Box II income tax treatment at a flat rate of 26.9%.

Finally, Dutch tax law provides for a specific treatment of stock options granted to a manager who qualifies as a Dutch-based employee. These options are generally not subject to Dutch wage tax/income tax upon grant. Instead, the amount of taxable income is determined when a stock option is exercised. Any profit received by a Dutch employee in this respect qualifies as income in Box I and is subject to income tax, levied at a maximum rate of 49.5%.

29. Are there any restrictions on dividends, interest payments and other payments by a portfolio company to its investors?

The restrictions are similar as for other EEA states. As mentioned in the AIFM Directive, these restrictions apply to both private and public companies in The Netherlands and prohibit asset stripping in the first two years that the PE fund owns a portfolio company. See *Question 28* for the tax considerations.

30. What anti-corruption/anti-bribery protections are typically included in investment documents? What local law penalties apply to fund executives who are directors if the portfolio company or its agents are found guilty under applicable anti-corruption or anti-bribery laws?

## Protections

Investment documents typically contain anti-corruption/anti-bribery warranties. In The Netherlands the provisions concerning instances of bribery and corruption are codified in the Dutch Criminal Code. Distinctions are made between bribing public officials and private commercial bribery, and between active and passive bribery. Both a legal entity, and the persons, directing or ordering corruption or bribery can be prosecuted for the criminal offence.

### Penalties

Based on the specifics of a case, the penalties can vary, and are as follows:

- For individuals, penalties can include fines, imprisonment, or both.
- For legal entities, penalties can include fixed fines or fines of up to 10% of the entity's turnover for the prior fiscal year.

In addition, the Dutch Anti-Money Laundering and Anti-Terrorist Financing Act (*Wet ter voorkoming van witwassen en financieren van terrorisme*) (WWFT) regulates financial record-keeping and contains the prohibitions on money laundering.

## Exit strategies

31.What forms of exit are typically used to realise a private equity fund's investment in a successful company? What are the relative advantages and disadvantages of each?

### Forms of exit

There is no general rule for PE and VC funds realising an exit for a successful portfolio company. In general, secondary buyouts and trade sales are the most common. In recent years, The Netherlands seem to also be open to new opportunities, such as dual-track exits. With the Amsterdam stock exchange recently overtaking London as Europe's most popular share trading exchange, IPO's have become a more popular way of providing for exits, with a number of new special purpose acquisition companies being listed in Amsterdam recently, which is also expected to provide a boost for IPO's.

In general, PE and VC sellers have a strong preference for "clean exits", and with most buyers willing to accept that, warranty and indemnity insurance continues to be on the rise.

### Advantages and disadvantages

The specific advantages and disadvantages of any exit strategy are highly dependent on the portfolio company and should be assessed on a case-by-case basis.

32. What forms of exit are typically used to end the private equity fund's investment in an unsuccessful/distressed company? What are the relative advantages and disadvantages of each?

### Forms of exit

Exit strategies primarily depend on the level of distress. If the company is still viable, it may be sold to another (turnaround) PE/VC fund or management; there are also examples of "pre-packs" being used by PE funds to re-acquire a business from a bankrupt portfolio company.

### Advantages and disadvantages

A fire sale will generally generate low returns but it can typically be used to achieve a swift and relatively clean exit.

The "pre-pack" route gives a PE fund another run at the business case, but there are both legal and public relations considerations to take into account (*see also* Question 25, on the introduction of a Dutch pre-insolvency procedure). In all events, bankruptcies tend to be complicated, and generate negative PR.

## Reform

33. What recent reforms or proposals for reform affect private equity?

The Dutch government's response to the COVID-19 crisis has included measures which may (indirectly) affect PE/VC firms and underlying portfolio companies.

In addition, several recent legislative reforms and pending proposals that may affect private equity are the following:

- The legislative proposal introducing a statutory waiting period of 250 calendar days for public Dutch companies in the event of, among others, an unsolicited public bid is envisaged to be in full force and effect as of 1 March 2021.
- The Regulation (EU) 2019/452 establishing a framework for the screening of foreign direct investments into the EU applies in The Netherlands, for example, with respect to the screening of foreign direct investments.
- As of 1 January 2021, Dutch pre-insolvency procedure (*Wet homologatie onderhands akkoord*) entered into force (*see* Question 25) which will likely also affect PE funds with Dutch portfolio companies, or which are interested in turnaround cases in the jurisdiction.
- The UBO register has been in full force and effect as of 2020 for entities incorporated under Dutch law (with the exception of FGRs that will be subject to a trust register instead).
- A legislative proposal is pending to extend the rules to strive for the supervisory and managing boards of large companies to comprise at least 30% women.
- A legislative proposal is pending for employees of larger companies to have a right to consent for important resolutions pertaining to the course of business and to expand the rights of the works council.

In general, environmental, social and governance (ESG) and corporate social responsibility (CSR) are rapidly gaining attention in the PE and VC sectors. This resulted into the implementation of the Dutch Child Labour Due Diligence Law which stipulates that each company that supplies goods or services to end users in The Netherlands has an obligation to conduct due diligence on whether such goods and services have been produced or delivered involving child labour.

On an EU level, as a result of the EU Action Plan, among others, the Sustainable Finance Disclosure Regulation (SFDR) (*Regulation (EU) 2019/2088*) must be implemented by EU member states by 10 March 2021. The SFDR requires asset managers, financial advisors and other market participants to classify financial products into three categories of sustainability level(s): dark green (sustainable objectives), light green (promoting environmental or social characteristics) or grey (ESG-risks or non-sustainable).

On 10 March 2021, the SFDR enters into full force and effect and, therefore, from that date on, financial institutions and market participants must comply with the SFDR (disclosure) requirements. Dutch guidelines are being provided by the AFM.

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