Reinforcement of Minority Shareholders' Position in the Right of Inquiry

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On 6 January 2005, the Enterprise Section of the Court of Appeal of Amsterdam ordered an inquiry to be held into possible mismanagement at Koninklijke Ahold NV ('Ahold') over the period from January 1998 through December 2003. The Dutch Association of Stockholders (*Vereniging van Effectenbezitters*, VEB) and the American pension fund the Public Retirement Association of Colorado ('Copera') had requested such an inquiry. Copera was represented in the proceedings before the Enterprise Section by the authors of this contribution. This case is one of the largest of its kind the Netherlands has ever seen. An interesting aspect of the case is the important role a minority shareholder may play as an interested party, even though he personally does not meet the requirements allowing him to request an inquiry.

The Dutch right of inquiry

Although other jurisdictions also have the option of an inquiry into the conduct of business in an enterprise, the right of inquiry existing in the Netherlands has unique features. After the right of inquiry was introduced in its current form into Dutch company law in 1971, the number of cases has boomed, especially during the last ten years. One of the causes of this boom was that following an amendment of the law in 1994, the Enterprise Section could impose an unlimited number of preliminary injunctions pending the inquiry. Furthermore, the inquiry proceedings provide for a swift and flexible course of justice and the judges of the Enterprise Section – three professional and two lay judges – have great expertise. Because of these features, the inquiry procedure has proved to be an effective means for the resolution of company disputes. Some well-known examples of cases that were presented to the Enterprise Section over the past years are the takeover struggle around Gucci NV, the struggle for the takeover of Rodamco North America NV by Westfield Ltd, the British Corus that attempted unsuccessfully to force the Dutch subsidiary Hoogovens to agree to the sale of aluminium activities, and the conduct of business at the supermarket enterprise Laurus NV.

The Enterprise Section is a division of the Court of Appeal of Amsterdam. Since this is the only Enterprise Section in the Netherlands, all inquiry proceedings are dealt with by the same court of justice, which enhances the unity of law. Another consequence of the fact that the Enterprise Section is part of the Court of Appeal is that appeal from such proceedings only lies with the Supreme Court. This has a positive effect on the speed of the proceedings.

The rules applicable to the inquiry proceedings are set out in particular in section 2:344 ff of the Dutch Civil Code. Inquiry proceedings are not commenced by a writ of summons, but by a petition.

The inquiry proceedings consist of two phases. The objective of the first phase is to have the Enterprise Chamber order an inquiry into the conduct of business of an enterprise. After the inquiry is completed by a report, the petitioner may request the Enterprise Chamber in the second phase to rule that there is or has been misconduct on the part of the relevant enterprise and to impose one or more measures – restrictively enumerated in the Act – in order to restore relations within the enterprise.

A petition for an inquiry can be directed against a Dutch NV (public limited company) or BV (private company), even if the company is bankrupt. The petition may solely be made by:

(1) holders of shares or depositary receipts issued for shares of the company representing at least ten per cent of the issued capital or who are entitled to an amount in shares or depositary receipts issued for shares with a nominal value of €225,000;
(2) persons who are authorised to do so pursuant to the articles of association or under an agreement with the company;
(3) the trade union that has members employed by the company and defends the interests of employees in the sector of industry or the company; and
(4) the advocate general of the Court of Appeal in Amsterdam in cases of public interest.

Other parties, such as the company itself, cannot request an inquiry.

A petition for an inquiry may only be made if the investigators believe that there are well-founded reasons to doubt the correctness of the company's policy. It will depend on the facts and circumstances whether a well-founded reason to doubt the correctness of the policy exists. Such reasons may include that:

- losses are suffered;
- dividends are wrongfully not distributed;
- persons act contrary to the articles of association;
- a company has no works council;
- the company provides insufficiently information to shareholders;
- the interests of minority shareholders are not sufficiently taken into account;
- directors act with conflicting interests;
- the supervisory board does not properly exercise supervision; and
- conflicts between several bodies of the company render it unmanageable.

First, a petitioner has to state his or her objections against the policy of the company in writing to the board of directors and also to the supervisory board, if there is one. The company has to have sufficient opportunity to investigate the objections and take steps to accommodate them. Incidentally, the Enterprise Section usually takes a lenient attitude on the requirement of announcing the objections in writing.

After a petition is filed, a hearing is scheduled for the oral procedure. In general, this is done after six weeks following the filing of the petition. However, if preliminary injunctions are also requested, an oral procedure can take place within a few days. The court registrar summons the company against which the petition is directed and the interested parties, if any. The company and interested parties may file a defence before the hearing. Parties who consider themselves to be interested parties, but have not been summoned, may join the proceedings of their own accord by filing a defence in support or in rejection of the petition. After the oral procedure, a decision is usually rendered within six weeks. Decisions regarding preliminary injunctions can be given even faster, sometimes at the very hearing.

If the Enterprise Section believes that there are indeed well-founded reasons to doubt the correctness of a policy, it may order an inquiry. It will appoint one or more investigators. The inquiry may take up to one year. The investigators have far-reaching powers and may examine the books and records of the company. Directors, supervisory directors and employees of the company are obliged to provide information. At their request, the investigators may be authorised to examine records of enterprises closely connected with the company and may hear witnesses under oath. The report of the inquiry is filed with the Enterprise Section and can only be inspected by the parties involved, unless the Enterprise Section rules that other parties also have the right to inspect it.

If misconduct is established by the report, the Enterprise Section may impose measures. These measures must be requested by the original petitioner or other entitled parties. This is the second phase of the inquiry proceedings. Other than the preliminary injunctions in the first phase of the proceedings, the possible measures in the second phase are enumerated restrictively in the Act:

(1) suspension or annulment of resolutions;
(2) suspension or dismissal of directors or supervisory directors;
(3) temporary appointment of directors or supervisory directors;
(4) temporary derogation from the articles of association;
(5) temporary transfer of shares to a nominee; and
(6) winding-up of the company.

The Enterprise Chamber may also decide not to impose any measures, but to rule that there is misconduct.

The decision establishing misconduct and the investigators' report may be used by the petitioner and other interested parties as a ground substantiating a possible separate claim for damages against the company, directors and supervisory directors.

The Ahold case

The accounting scandal at Ahold and the proceedings before the Enterprise Section were covered in great detail by the financial media. Ahold made public in February 2003 that it had to make a downward adjustment of its financial results over 2002 and previous years due to the improper full consolidation of a number of joint ventures and proved fraud at US Foodservice, a subsidiary of Ahold in the United States. Ahold also reported suspicious transactions at its Argentinean joint venture Disco. In the course of 2003, the scandal at Ahold grew further as new disclosures appeared in the media. The consolidation of the joint ventures turned out to be based on control letters in

which, in derogation of the joint venture agreements, Ahold was proclaimed to have substantial control over the relevant joint venture. However, these control letters were contradicted by secret side letters. Both the control and side letters had been signed by members of the board of directors of Ahold.

Because of these facts, the VEB requested an inquiry in early 2004. Copera supported this request by joining the action as an interested party on the side of the VEB. Ahold opposed the request by stating that Ahold itself and government institutions in the Netherlands and the United States had already carried out sufficient inquiries and that the VEB and Copera had no interest in yet another one. The Enterprise Section has rejected these arguments. According to the Enterprise Section, a considerable amount of information was unavailable for shareholders, many questions remain unanswered, and the harm Ahold suffered from the inquiry does not outweigh the shareholders' interest in such an investigation, especially in view of the social unrest the scandal has caused.

Three investigators appointed by the Enterprise Section will have to investigate:

(1) the incorrect consolidation of the joint ventures;
(2) the due diligence investigation Ahold made when it took over US Foodservice and Ahold's supervision of the improvement of the internal control systems at US Foodservice; and
(3) Ahold's supervision of its operating companies.

This last area of attention of the investigators is remarkable, because it indirectly involves the entire Ahold Corporation in the inquiry. It is not yet clear how long the investigation will take. The Enterprise Section has determined that it may cost up to €250,000, which is the highest amount ever awarded for such an inquiry.

As observed above, each party that thinks it has an interest in the petition for an inquiry may join the proceedings, also on its own initiative, as Copera did. There is not much case law regarding the question of who will qualify as an interested party in the inquiry proceedings. The Enterprise Section assesses the facts on a case-to-case basis, as to whether a party can be regarded an interested party. In making this assessment, the Enterprise Section tends to pursue a generous admissions policy. In the past, associations such as the VEB, which hold some stock and, according to their objects, are representing the interests of investors, and former managing directors of the company against which a petition was filed, have been admitted as interested parties in inquiry proceedings. The issue of whether a party may participate as an interested party is important because the interested party can influence the proceedings considerably. The interested party may add to the ground for the petition, and request further scope of the inquiry. If the petitioner has requested preliminary injunctions, the interested party may also do so.

It has been argued that a shareholder who does not comply with the criteria for initiating an inquiry of its own accord cannot be considered to be an interested party, because this would allow small and very small shareholders to influence an inquiry. By admitting Copera as an interested party, the Enterprise Section has also now determined, in line with the flexible policy, that a shareholder who cannot independently file an inquiry petition may indeed participate as an interested party on the sole ground that it is a shareholder. It also appears from the decision that the Enterprise Section has duly involved the arguments made on behalf of Copera in its assessment of the case. Among other things, the Enterprise Section has considered, with reference to Copera's arguments, that it must be investigated whether the so-called 'control letters', on the basis of which Ahold has consolidated the joint ventures, indeed constitute sufficient ground for consolidation, irrespective of the secret side letters. A joint venture to which the request of the VEB did not relate, but with regard to which Copera has put forward additional objections, must also be included in the inquiry.

Conclusion

For shareholders of a Dutch company against which a petition for an inquiry is filed, the decision in the *Ahold* case means that they may join the proceedings independently and can influence the proceedings, although they cannot file a petition for an inquiry themselves. This offers minority shareholders the possibility to take, together with the petitioner and the company, a position of their own and to introduce their own arguments in favour of or against an inquiry.

CORRECTION

In the last issue of the Negligence and Damages Committee Newsletter (Vol 3 No 2, July 2004), in David Body's article 'The Creutzfeldt-Jakob Disease Litigation', the following sentence,

> 'Secondly, this letter should be put to paediatric endocrinologists who had been members of the Clinical Committee overseeing the UK treatment programme so that they could give evidence examination of expert evidence as to the warnings that would have been given in 1977, if they had been properly warned of the nature of the risk by those with oversight of the hormone production.'

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The IBA apologises for this error and regrets any inconvenience caused.