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Re Takeovers of businesses

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Dear Madam President,

In recent months, there has been a visible increase in takeover activities, both in the Netherlands and the rest of Europe. The most striking examples of which are PPG Industries' bid to take over AkzoNobel and Kraft Heinz's bid to acquire Unilever in February. This increase in activity is, in part, the result of monetary easing and companies' increasing profitability, which has resulted in a great deal of liquidity in circulation. In addition, the euro at present is relatively low against the US dollar.

This letter is to inform the House regarding the way the government views and considers these developments. I should also like to take this opportunity to respond to the request submitted by the MP Omtzigt from the Order of Business of 12 April 2017 (reference 2017Z04925). I would also like to point the House to the answers to the sets of questions submitted by the MPs Hijink and Van Kent (both of the SP) (2017Z04066 and 2017Z04997), by the MPs Leijten and Hijink (both of the SP) (2017Z04274), by the MP Hijink (of the SP) (2017Z04688) and by the MPs Paternotte (of D66) and Bruins (of the ChristenUnie) (2017Z04996), which will be submitted to the House parallel to this letter.

Takeovers by foreign companies are part and parcel of the economic process. They provide opportunities for our business community, but they also pose a potential risk to the economy of the Netherlands, particularly if such takeovers are hostile in nature. On the one hand, they serve to keep corporate governance on its toes and can lead to additional investment, synergy benefits and opportunities to realise economies of scale. On the other hand, they may lead to the loss of R&D activities, head offices, and the ability to provide solutions to the challenges in society. They can also serve to weaken the Dutch innovation ecosystem or even lead to risks to national security.

The government is committed to an open stance regarding takeovers, given their importance to the business establishment and investment climate of the Netherlands. In addition, the government appreciates the responsibility taken by key companies (companies with a significant amount of R&D, offering high-quality employment and playing a central role on a national or regional level) in the search for solutions to the challenges in society. In some takeovers, there is a risk

that any focus on the long term falls by the wayside in favour of short-term profits.

It should be noted that company boards are under tremendous pressure to respond in a timely fashion when faced with a hostile takeover bid and it is in the interest of all stakeholders the board should have an adequate amount of time to go through a careful and diligent process. This goes primarily toward benefiting long-term value creation and the interests of all the stakeholders involved.

Another key point of consideration is that investors from outside the EU in many cases will have more freedom to invest in the EU than is the case vice versa. A number of other EU Member States have increasingly begun to experience discomfort regarding this issue and have brought it to the attention of the European Commission.

Rhineland model of corporate governance

First and foremost, it is primarily the responsibility of the businesses themselves to distinguish themselves from the competition and strengthen their position by way of a good strategy. This fits within the Rhineland model of corporate governance adhered to by Dutch companies. The model is centred on long-term value creation, with due consideration of the interests of all stakeholders involved. This is exemplified by the Corporate Governance Code, which is a product of self-regulation by the supporting parties.

In addition to their strategy, companies have a number of other options to support long-term value creation:

- i. Dutch corporate law affords companies the opportunity to issue differentiated shares, which allows shareholders with a long-term perspective to be given certain advantages;
- ii. Based on the Dutch Corporate Governance Code, the board may invoke a response time of up to 180 days in the event that a shareholder puts an item on the agenda that may lead to a change in the company's strategy;
- iii. Companies do have the option to (temporarily) defend themselves against an imminent hostile takeover by way of anti-takeover measures;
- iv. Companies may submit a request for an inquiry at the Enterprise Division if they deem the actions of the shareholders to be running contrary to the interests of the company.

More assertive use of these options should be considered. A review should also be undertaken to ascertain whether sufficient use is made of the Enterprise Division within the current legal framework.

Within the Dutch model of corporate governance, employees fulfil a clear role in the ins and outs of the company. This is shaped by, among other things, the right of consultation held by the Works Council in respect of strategy, periodic consultations with the executive director and the Supervisory Board, the right to set the agenda, and, for example in the case of a statutory two-tier company, to

provide a (weighted) recommendation regarding the appointment of some of the members of the Supervisory Board.

Shift in balance advisable

Taking into account the opportunities businesses themselves have, the government notes that a shift in the balance of responsibilities between the various stakeholders would be advisable (also see Memorandum on progress of corporate law modernisation¹). The objective of which is to build in additional safeguards for long-term value creation and due consideration of the interests of all stakeholders.

Because such a shift is liable to affect the business and investment climate, it is crucial that this be shaped as proportionally as possible. To that end, consultations will be held with the relevant stakeholders and due consideration will be given to achieving a level playing field with the countries that are relevant to us.

Action lines

The government will be taking action along four key lines:

1. The government wishes to provide corporate governance with more space and time to assess the effects on all stakeholders of a takeover or a significant strategy change proposed by the shareholders.
2. The government shall enter into a dialogue with Dutch institutional investors in order to ascertain whether they experience obstacles when investing in Dutch companies, and, if so, if and how those obstacles can be removed.
3. Priority will be given to finalise the ex-ante analyses of the crucial sectors that are being carried out by the NCTV and the relevant Ministries. If necessary, additional measures shall be proposed to safeguard national security.
4. The Netherlands supports the undertaking of a debate in Europe regarding reciprocity with third countries outside the EU.

Additional time and space for fair and proper assessment of the effects for stakeholders

In cases where an announced takeover bid or other circumstances should threaten the continuity, independence, identity or development of the company, the government believes that corporate governance should have an adequate amount of time to prepare a considered response, taking into account the interests of all stakeholders involved. Consideration of these interests by corporate governance in its decision making process is part and parcel of the Rhineland model of corporate governance, as evidenced by the – recently revised – Dutch Corporate Governance Code.

¹ Parliamentary Papers II 2016/2017, 29 752, no. 9. Minister of Security and Justice

In practice, however, not all companies are afforded that consideration time. Anti-takeover measures can provide that option, however not all companies have adequate protection. The interim implementation (following initial public offering) or extension of an anti-takeover measure may even meet opposition from incumbent shareholders. In addition, anti-takeover measures cannot always provide sufficient protection against pressure from activist shareholders.

It is paramount that corporate governance should have adequate time to reflect on and consider the potential consequences for all stakeholders and, if necessary, modify its strategy. After all, an informed decision is in the interest of the company and goes towards fostering long-term value creation. For that reason, four options were considered to ensure a way in which each and every company could be afforded that time. These options took into account the proposals made publicly by various executives, scientists, and interest groups.

Three key criteria were considered in the assessment of the options: expected effectiveness, including the impact on the business and investment climate, the duration of the measure and the scope of its effects. All three options, however, take into account the relevant EU regulatory framework, including the European directives concerning shareholder's rights in listed companies (Directive 2007/36/EC), concerning takeover bids (Directive 2004/25/EC) and the revised Second Company Law Directive (Directive 2012/30/EU).

Option A: statutory reflection period

Firstly, a statutory reflection period could be introduced for a period of up to one year, which would provide the board of directors of a company with time and space to act in the event of a hostile takeover bid. In addition, this option would ensure that the decision-making process at the general meeting of shareholders concerning the appointment and dismissal of directors and the strategy of the company could be suspended.

This option does not prevent a hostile takeover outright, but rather has a preventive effect that forces the acquiring party to wait before moving forward.

Option B: increase of minimum settlement percentage

Secondly, the bidding rules could be amended by implementing a substantial increase in the minimum settlement percentage. This would make it more difficult to effect a hostile takeover of a Dutch company, as bidders would have to offer a higher price or reach an agreement with the board of directors.

Simultaneously providing corporate governance with the option of lowering that threshold also goes to avoiding obstruction of friendly takeovers.

Option C: simplification of issuance of protective preference shares

Thirdly, companies should be better enabled to implement anti-takeover measures. More specifically, the rules regarding the decision-making process at

the general meeting of shareholders on the issuance of protective preference shares should be amended.

In the event of an imminent hostile takeover, the Supervisory Board will then be able to propose the issuance of preference shares, with the general meeting of shareholders only being able to reject that proposal with a two-thirds majority of the votes cast. Essentially, the general meeting of shareholders is only given right of veto by qualified majority. This would meet the needs of companies currently experiencing difficulties with implementing or extending an anti-takeover measure.

Option D: amendment of Public Bids Decree of the Financial Supervision Act
Fourthly, a minimum reflection period could be introduced in the Public Bids Decree of the Financial Supervision Act. At present, the decree only provides for a maximum period of 12 weeks for the submission of an offer document. The rationale in this case is that the bidder would only be able to submit the offer document after he had given the board the opportunity to respond. The minimum reflection period for corporate governance to respond would then be granted as a supplement to this maximum period.

In any case, careful and diligent design will be required to avoid clashes with the foregoing European directives. In addition, attention should be paid to the proportionality of the measure, the effects on the investment and business climate and the level playing field with countries relevant to us. The government currently favours the creation of a statutory reflection period of one year (option A), as, in addition to (hostile) takeovers, it also applies to shareholder activism and provides the opportunity of a wider scope of application than merely in listed companies. On this basis, consultations will be held with stakeholders and experts.

Role of institutional investors

Dutch institutional investors are major players on the international capital market, being committed to realise a good return for their customers and members at a manageable level of risk. In doing so, they frequently maintain a long-term horizon, which offers companies a wider berth to follow a long-term strategy. In the long term, this is expected to lead to better results and greater returns.

The government shall enter into a dialogue with Dutch institutional investors in order to ascertain whether they experience obstacles when investing in Dutch companies, and, if so, if and how those obstacles can be removed. Even a small part of their capital would allow them to take up substantial holdings in Dutch companies, which would give companies a lot more space to follow their long-term strategy. In this case, a minority share may already be sufficient. Additionally, institutional investors and other wealthy parties would have a key role to play at the time the company in question was about to be taken over, for example, by carefully considering the interests of all relevant stakeholders and by emphasising the importance of long-term value creation.

Ex-ante analyses of vital sectors

As communicated to the House in the letters of June 2014² and January 2016³, the government has been conducting ex-ante analyses in sectors with a vital process. These ex-ante analyses served to map potential risks to national security in takeovers by foreign parties in a timely fashion and, moreover, to determine whether the existing instruments of the government could provide adequate safeguards. Based on the results of such an analysis, decisions can be made regarding the desirability of additional measures.

Following the results of the ex-ante analysis in the telecommunications sector, I moved the Telecommunications Sector (Undesirable Control) Bill to the public consultation stage. The bill introduces the authority for the Minister of Economic to prohibit the retaining or acquisition of a controlling interest in a telecommunications player, if that controlling interest should lead to such an influential position in the telecommunications sector so as to endanger national security or public order. The responses obtained from the public consultation are currently being assessed. I shall be informing the House separately regarding the progress thereof.

At present, multiple ex-ante analyses of sectors with vital processes are either in preparation or underway, including in the fields of drinking water (Infrastructure and the Environment), chemical industry (Infrastructure and the Environment and Economic Affairs), nuclear (Infrastructure and the Environment), payment transactions (Finance), flight and aircraft department (Infrastructure and the Environment), handling of shipping (Infrastructure and the Environment), defence capability (Defence), police effort (Security and Justice). These analyses shall be prepared or completed with priority status. The House shall be informed of the results in a subsequent Economic Security progress letter.

Importance of an international level playing field (reciprocity)

The final line of action concerns the issue of investors from third countries (not in the EU or within the European Economic Area), who wish to acquire an equity stake in an EU company or wish to take over an EU company in its entirety, being entitled to the same treatment within the EU as EU investors, under European Union law (free movement of capital). Contrary to this openness to foreign investment from third countries, European companies often encounter a more closed system in those very countries, such as China and the United States. A similar observation can be made regarding foreign companies that are State owned or receive State aid. Such companies occupy a better position than private EU companies and, as such, are better able to take over companies within the EU and protect themselves against foreign takeovers. A number of Member States

² Parliamentary Papers II 2013/14, 30 821, no. 22.

³ Parliamentary Papers II 2016/17, 30 821, no. 27.

have already signalled their increasing discomfort on the matter to the European Commission.

In relation to trade agreements, the EU is committed to realising the broadest possible market access for European companies in third countries. In addition the EU is committed to far-reaching agreements on the manner in which State-owned enterprises are allowed to operate. The Netherlands actively supports this commitment. The government furthermore supports the intention to initiate a debate within Europe regarding reciprocity with third countries outside the EU.

Conclusion

The government considers this to be a balanced package of measures. Companies will be facilitated to take action themselves. The government considers additional regulatory measures to be desirable in order to allow for more careful consideration of the interests of all relevant stakeholders in takeovers, in any case. In matters that require public action, such as in the case of national security and reciprocity, the government will act on its own initiative.

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