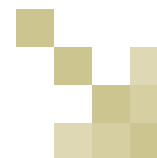


# The Netherlands



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## MARKET AND INCENTIVES

1. Please describe briefly the private equity market in your jurisdiction, in particular:

- The sources from which funds established to invest in private equity transactions (private equity funds) obtain their funding, such as institutional investors (for example, pension funds, insurance companies and banks), companies, individuals and government agencies.
- Market trends (for example, the role of hedge funds in private equity).

The information in *Question 1* has been derived from *De Nederlandse private equity-markt in 2006* (a report about the Dutch private equity market in 2006) by Nederlandse Vereniging van Participatiemaatschappijen (NVP) (see box, *Private equity/venture capital associations*) and PricewaterhouseCoopers.

### Sources of funding

In 2006, Dutch private equity funds obtained their funding mainly from:

- Banks (EUR818 million (about US\$1.2 billion) or 36% of total private equity investments).
- Pension funds (EUR432 million (about US\$624 million) or 19%).
- Insurance companies (EUR198 million (about US\$286 million) or 9%).
- Non-financial institutions (EUR113 million (about US\$163 million) or 5%).
- Fund of funds (EUR455 million (about US\$657 million) or 20%).
- The public sector (EUR76 million (about US\$110 million) or 3%).
- Individuals (EUR130 million (about US\$189 million) or 6%).

### Market trends

In 2006 the market for private equity continued to be strong in terms of the number and size of transactions.

2. Please summarise the level of activity in recent years in relation to:

- Fundraising by private equity funds and hedge funds.
- Private equity investment in established, early stage and start-up businesses.
- Private equity financed transactions (for example, management buyouts (MBOs), management buy-ins (MBIs) and public to private transactions).
- Exits from private equity funds (that is, the realisations of the investments).

The information in *Question 2* has been derived from *De Nederlandse private equity-markt in 2006* by NVP and PricewaterhouseCoopers.

### Fundraising

In 2006, private equity funds obtained EUR2.3 billion (about US\$3.3 billion) of new funds, mainly from banks and pension funds (see *Question 1*).

### Investment

In 2006, private equity funds mainly invested their funds in established businesses (93.3% of the invested capital), especially through buyouts. Investments in early stage businesses (0.6%) and start-up businesses (2.9%) were limited.

### Transactions

In 2006 and consistent with previous years, more than 100 private equity financed buyout transactions took place in The Netherlands for a total amount of EUR2.4 billion (about US\$3.5 billion). Most of these transactions concerned mid-cap companies.

### Exits

Divestments by private equity funds totalled EUR1.7 billion (about US\$2.5 billion) (cost price) in 2006. This amount was attributable to the following exit methods:

- Sale to third parties (mostly strategic buyers): EUR447 million (about US\$646 million) or 26%.
- Sale to other investors (secondary buyouts): EUR422 million (about US\$610 million) or 25%.

- Capital markets (flotation and trading of securities on secondary market): EUR134 million (about US\$196 million) or 8%.
- Sale to shareholders: EUR581 million (about US\$839 million) or 34%.
- Liquidations: EUR97 million (about US\$140 million) or 6%.

### 3. What tax incentive schemes exist to encourage investment in unlisted companies? At whom are the schemes directed? What conditions must be met?

For individual investors, certain subordinated-debt investments in start-ups can be exempt from income tax.

While not specifically targeted towards investments in unlisted companies, the participation exemption benefits equity participations in Dutch and non-Dutch resident companies, which include unlisted companies (see *Question 5*).

## FUND FORMATION

### 4. What legal structure(s) (domestic or foreign) are most commonly used as a vehicle for private equity funds in your jurisdiction?

The following legal vehicles are used for private equity funds in the Netherlands:

- Private companies (*besloten vennootschap met beperkte aansprakelijkheid*) (BV).
- Public companies (*naamloze vennootschap*) (NV).
- Limited partnerships (*commanditaire vennootschap*).
- Funds for joint account (*fonds voor gemene rekening*).

Only the BV and the NV have legal personality at present. A limited partnership can opt for legal personality under the new law on partnerships (*personenvennootschappen*) which is expected to come into force at the beginning of 2008.

### 5. For each structure identified in *Question 4*, identify whether it is taxed, tax exempt or fiscally transparent (that is, tax is levied on the individual investors rather than the fund itself):

- So far as domestic investors are concerned.
- So far as foreign investors are concerned.

A private equity fund can be structured for corporate income tax purposes as any of the following:

- Non-transparent and subject to the regular corporate income tax regime.

- Non-transparent and subject to tax at the rate of 0% under the special corporate income tax regime for fiscal investment institutions (FII).
- Transparent and not subject to corporate income tax.

### Corporate income tax regime

Under the regular corporate income tax regime, the worldwide profits (income and gains) of a Dutch resident company are subject to corporate tax at the rate of 25.5% in 2007.

**Participation exemption.** For private equity funds, benefits (both income and gains) derived from qualifying subsidiaries are exempt under the participation exemption. Investments by Dutch resident funds of at least 5% of the share capital of Dutch and non-Dutch portfolio companies qualify for the exemption (*for reductions in this 5% threshold, see below*), provided that the subsidiary both:

- Has its capital divided into shares.
- Meets one of the following requirements:
  - qualifies as a real estate investment company; that is, the company's assets on a consolidated basis consist of at least 90% real estate;
  - does not constitute a low-taxed portfolio investment; a subsidiary qualifies as a low-taxed portfolio investment if both:
    - at least 50% of its assets consist of portfolio investments (Asset Test);
    - it is not subject to an effective tax rate on its profits of at least 10% (Effective Tax Rate Test).

For purposes of the Asset Test, portfolio investments are defined as investments that are not reasonably required for the business operations of the entity holding the assets. The Asset Test is also determined on the basis of the fair market value of assets held directly by the subsidiary, or indirectly through any entity in which the subsidiary holds at least 5% of the share capital. There is no full consolidation in the sense that all inter-company loans are taken into account.

Whether or not a subsidiary meets the Effective Tax Rate Test is, in principle, determined at the level of the subsidiary only. The actual profit tax due by the subsidiary must be compared with the subsidiary's hypothetical liability to Dutch corporate income tax if it were a tax resident in The Netherlands.

A shareholding of less than 5% does not qualify, unless one of the following exceptions applies:

- The parent company previously held a shareholding of 5% or more for an uninterrupted period of at least 12 months, and, following the decrease of the shareholding below the 5% threshold, not more than three years have passed.
- A related party holds a shareholding in the subsidiary that meets the requirements for the participation exemption.

**Non-transparent vehicles.** A withholding tax of 15% is levied on dividend distributions made by non-transparent companies to its shareholder(s) or partners. This rate is reduced, or even completely eliminated, if the shareholder or partner is a Dutch resident or an EU resident meeting certain requirements mentioned in Directive 90/435/EEC on the taxation of parent companies and subsidiaries (provided that this shareholder holds at least 5% of the nominal issued share capital of the Dutch subsidiary).

If the shareholder resides in a country that concluded a tax treaty with The Netherlands, the statutory withholding tax of 15% is generally reduced to 5% or completely eliminated in case of substantial participations, generally 25% or more, in the Dutch company. With the exception of certain long term participating loans, no withholding tax is levied on interest payments.

**Transparent vehicles.** If the private equity fund vehicle is transparent, the fund is not subject to corporate income tax.

### Companies

Private and public companies are always non-transparent and subject to either the:

- Regular corporate income tax regime.
- Special FII regime.

Under the FII regime, a company is taxed at the rate of 0%. It is, however, obliged to distribute its profits annually. Currently a legislative proposal is pending which introduces a tax-exempt regime for investment funds that invest in publicly traded financial instruments. The proposal is expected to take effect in the course of the second half of 2007.

### Limited partnership

A limited partnership can either be transparent or non-transparent:

- A limited partnership is non-transparent and subject to the regular corporate income tax regime if accession and/or replacement of limited partners can take place without the prior consent of all partners.
- A limited partnership is transparent for tax purposes and therefore not subject to corporate income tax if accession and or replacement of limited partners can only take place with the prior consent of all partners.

A limited partnership, transparent or not, cannot elect the FII regime.

### Fund for joint account

A fund for joint account can either be transparent or non-transparent:

- A fund for joint account is non-transparent and subject to regular corporate income tax regime or the special FII regime, if the participations are tradeable. The participations in the fund are deemed tradeable if they can be transferred without the consent of all participants. The participations are not tradeable if they can only be transferred to the fund for joint account itself or to certain direct relatives of a participant.

- The fund for joint account is transparent for tax purposes if the participations in the fund are not tradeable.

### 6. What (if any) structures commonly used for private equity funds in other jurisdictions are regarded in your jurisdiction as not being tax transparent (in so far as they invest in companies in your jurisdiction)? What parallel domestic structures are typically used in these circumstances?

Tax transparency of a foreign entity is determined by, among other things, its governing law and regulations, and the deed of incorporation or the partnership agreement. In this regard the following questions need to be addressed:

- A. Is the entity the legal owner of the assets and liabilities used to carry out its activities?
- B. Has at least one participant unlimited liability for debts and other obligations of the entity?
- C. Has the entity a capital divided into shares?
- D. Is accession and/or replacement of the participants possible without the prior consent of all other participants?

The entity is non-transparent if the answer to question (A) is "yes" and to question (B) is "no". If the answer to question (A) is "yes" or "no" and to (B) is "yes", the questions as stated under (C) and (D) must be answered. The entity is non-transparent if both question (C) and (D) are answered with "yes". The entity is transparent if the answer to either question (C) or (D) is "no".

If a foreign limited partnership is comparable to a Dutch limited partnership, the rules for a Dutch limited partnership apply to determine whether the foreign limited partnership is tax transparent (see *Question 5, Limited partnership*). An entity is comparable to a Dutch limited partnership if all of the following apply:

- A business is carried on in the name of the entity.
- The entity has at least one general partner and one limited partner.
- The general partner has unlimited liability or has proportional liability towards third parties.
- The limited partner is only liable to the extent of his investment.
- The limited partner does not perform any external acts of management and administration.

### 7. Are a private equity fund's promoter, principals and manager required to be licensed?

Under the new Dutch Financial Markets Supervision Act (*Wet op het financieel toezicht*) (FMSA) which came into force on 1 January 2007, it is prohibited to offer units in a private equity fund in The Netherlands, unless the fund's management company (*beheerder*) or, in certain circumstances, the private equity fund itself, has ob-

tained a licence from the Netherlands Authority for the Financial Markets (*Stichting Autoriteit Financiële Markten*) (AFM).

Marketing and advertising a possible offering of units in a private equity fund may already qualify as offering units in the private equity fund.

It takes at least 13 weeks to obtain the licence from the AFM. A licence, however, is not required if one (or more) exemptions or exceptions apply(ies) (*see Question 8*).

Any person other than the management company who offers interests in the fund for sale (including a fund manager retained by the management company), such as an intermediary or an asset manager offering the units, must generally obtain a licence from the AFM to act as an investment firm (*beleggingsonderneming*).

Exceptions apply for, among others, foreign investment firms which provide their services using a European passport in respect of the provision of services as an investment firm.

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**8. Are private equity funds regulated as investment companies or otherwise and, if so, what are the consequences? Are there any exemptions? Include, in the answer, any restrictions on how a private equity fund can be marketed or advertised (for example, under private placement or prospectus rules).**

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The fund's management company (*beheerder*) or, in certain circumstances, the private equity fund itself, is subject to a licence requirement under the FMSA if units in the fund are offered in The Netherlands, unless an exemption or exception applies (*see Question 7*).

A licence is not required if any of the following (either separate or in combination) exemptions or exceptions apply:

- The units are offered solely to qualified investors (*gekwalificeerde beleggers*) (such as banks, brokers and institutional investors).
- The units are offered to fewer than 100 persons not being qualified investors.
- The units offered have an individual denomination of at least EUR50,000 (about US\$72,235) (or its foreign currency equivalent).
- The units offered can only be acquired for a total consideration of at least EUR50,000 (or its foreign currency equivalent) per investor.

The AFM holds the position that the above-mentioned amounts of EUR50,000 must be actually contributed to the private equity fund, as committed capital is considered by the AFM not to be sufficient for the relevant exemption or exception to apply.

Under the FMSA, an offer of units in a private equity fund under an exception or exemption as described above must be accompanied by a "warning statement" to the effect and depending on who is offering the units and on whether the fund is closed-end or open-end that, in summary:

- The fund and its manager (to the extent it acts for the fund) do not require a licence under the FMSA.

- The fund and its manager are not supervised by the AFM.
- The person who offers units in the fund does not require a licence under the FMSA with respect to that offering and is not supervised by the AFM in relation to that offering.

An important exception to the licence requirement under the FMSA for investment institutions applies to offerings of units in funds from countries that have been accredited by the Dutch Minister of Finance as countries having "adequate supervision for collective investment schemes". Currently, Luxembourg, Guernsey, the US, Ireland, Jersey and Malta have been accredited by the Dutch Minister of Finance to have such adequate supervision. This adequate supervision exception has been quite popular in 2006 and 2007, as it was used by KKR, Apollo, Carlyle Capital, Marshall Wace Tops and Boussard Gavaudan and other major private equity and real estate houses and hedge funds in close consultation with tax advisers to list funds formed in Guernsey on the Amsterdam Stock Exchange in 2006 and 2007.

The Minister of Finance may add more countries to the adequate supervision list in the future.

It is important to note that a closed-end private equity fund a private equity fund the units of which are not redeemable by the fund on the participant's request is not only subject to the licence requirement under the FMSA (*see above*). They also need to prepare a prospectus that meets the requirements of Directive 2003/71/EC on the prospectus to be published where securities are to be offered to the public or admitted to trading (Prospectus Directive) (as implemented by the FMSA) when its units are offered to the public or admitted to trading on a regulated market. The prospectus also requires approval by the AFM (or by another supervisory authority in another EU or European Economic Area member state). However, similar exceptions and exemptions or exceptions as mentioned above exist for the prospectus requirement for a closed-end private equity fund.

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**9. Are there any restrictions (for example, nationality, age and number) on investors in private equity funds?**

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There are no restrictions on investors in private equity funds, other than those on how a private equity fund can be marketed or advertised (*see Questions 7 and 8*).

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

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The relationship between investors and the fund is typically governed by the:

- Partnership agreement, for partnerships.
- Articles of association and a shareholders' agreement, for companies.

In companies, protection is often sought against dilution resulting in an investor holding less than 5% of the company, in which case the participation exemption, generally, will not apply (*see Question 5*). Some pension funds want to avoid holding a sub-

stantial interest in a fund (for example more than 20%), as they expect future tax legislation to make such holdings taxable.

In partnerships, investors usually seek protection by negotiating in the partnership agreement:

- Investment restrictions.
- Limitations of liability.
- Veto and/or majority rights.
- The installation of an investment advisory board or committee, the approval of which is required to make certain management decisions.

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

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There are no statutory or other limits, other than those on how a private equity fund can be marketed or advertised (see Questions 7 and 8), and those relating to the possible tax transparency of the fund (see Question 5).

## INVESTMENTS

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**12. What are the most common investment objectives of private equity funds (for example, what is the average life of a fund and what are the typical average rates of return sought)?**

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Capital gain is the most common investment objective of private equity funds. The typical average life of a private equity fund is between seven and ten years. The typical average rate of return sought depends on the product invested in by the fund. The average rates of return sought with:

- Real estate funds is between 9% and 12%.
- Venture capital funds is between 10% and 20%.

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**13. What forms of equity and debt interest are commonly taken by a private equity fund in a portfolio company? What are the relative advantages and disadvantages of each? Are there any restrictions on the issue or transfer of shares by law?**

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Private equity funds can take various equity interests in portfolio companies, such as:

- Ordinary and preference shares.
- Compulsorily redeemable and convertible shares.
- Warrants and loans (subordinate and senior).

There are no specific trends and the nature of the interest taken largely depends on the type of transaction and the fund's intentions.

For example, convertible preference shares can provide protection against dilution if further shares are issued. Loan debt ranks ahead of shareholder debt in the proceeds of a company's liquidation.

The advantage of equity for Dutch-resident funds is that benefits from the equity interest in the portfolio company (both dividends and capital gains) are generally exempt from corporate income tax under the participation exemption (see Question 5). The benefit of participating in a Dutch portfolio company using debt is that interest payments are generally tax deductible by the portfolio company. However, interest income received by the fund is generally not tax exempt under the participation exemption.

The offering of transferable units (through issue or transfer) in closed-end funds requires a prospectus under the FMSA unless an exemption (or an exception) applies (see Question 8).

In addition, a private company must include provisions in its articles of association restricting the transfer of its shares to third parties. In particular, the transfers must be subject to either (section 195, Book 2, Civil Code):

- Approval by a corporate body of the company, such as the general meeting of shareholders (general meeting) or the management board.
- A right of first refusal in favour of the other shareholders.

## BUYOUTS

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**14. Is it common for buyouts of private companies to take place by auction? If so, which legislation and rules apply?**

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Buyouts by auction are very common, especially for non-listed entities. Apart from the individual procedure and rules dictated by the seller and his financial adviser, buyouts of portfolio companies, whether by auction or not, are governed by the following legislation and rules:

- Books 2 and 6 of the Civil Code.
- The FMSA.
- The Works Council Act and the Social and Economic Council Merger Code of Conduct 2000.
- Regulation (EC) No. 139/2004 on the control of concentrations between undertakings (Merger Regulation) or, depending on the size of the concentration, the Dutch Competition Act 1997.

In relation to listed companies, additional legislation and rules apply (see Question 15).

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**15. Are buyouts of listed companies common (public to private transactions)? If so, which legislation and rules apply?**

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Public to private transactions (and attempts at these) are increasingly common. In 2006, VNU was acquired by a private equity group consisting of AlInvest Partners, The Blackstone Group, The Carlyle Group, Hellman & Friedman, Kohlberg Kravis Rob-

erts & Co and Thomas H Lee Partners and subsequently de-listed from Euronext Amsterdam. A recent example is Stork.

In addition to the legislation mentioned in *Question 14*, the FMSA contains rules applicable to public to private transactions, such as:

- Requirements (for example, timescales and content of public announcements and offers) for public offers (firm, partial or tender offers) (these rules are currently still contained in the Securities Act, but will in the near future be contained in the FMSA).
- Insider trading rules.

The AFM is the regulatory authority that enforces compliance with these rules.

#### 16. What are the principal documents produced in a buyout?

The principal documents produced in a buyout (not being a public to private transaction) are:

- A share (or asset) purchase agreement.
- A shareholders' agreement.
- Corporate documentation for the incorporation of an acquisition vehicle (if any).
- Financing documents (including security documents).
- Management agreements.

#### 17. What forms of contractual buyer protection are commonly requested by private equity funds from sellers and/or management?

The most common covenants for buyer protection in private equity transactions that may not exist in other acquisitions are:

- A financing condition.
- A material adverse change condition.
- A provision that the company assists in preparing finance documents.
- A condition that if the company has set up a works council under the Works Council Act, the works council must advise on the security to be given by the company for financing the transaction.

The scope and extent of buyer protection covenants largely depend on the negotiating strengths of the parties and differ by transaction. Representations, warranties and indemnities are not unique to private equity transactions. However, it is customary in private equity transactions for management to give covenants in favour of funds about their lack of knowledge of breaches of warranties. Managers often forfeit all or part of the equity interest they take during the transaction if these covenants are breached.

In addition, private equity transactions typically require agreements with the management involved in the transaction. These agreements may include, in addition to base salary, variable remuneration components for managers, for example, bonus and long-term incentive plans typically linked to personal or company targets being met.

#### 18. What non-contractual duties (for example, of confidentiality and employment) do the portfolio company managers owe and to whom (for example, when approaching possible investors in relation to an MBO)?

As non-contractual duties are more common in public to private transactions, the following relates to the non-contractual duties of managing and supervisory directors in public to private transactions.

Companies can have a two-tiered board structure with a management and supervisory board. Listed companies usually have a two-tiered board structure.

##### Supervisory board

The supervisory board:

- Supervises the management board and the general affairs of the company.
- Advises the management board.
- Must consider the interests of the company in fulfilling its duties.

In case of an MBO, the supervisory board of the target is the only independent party involved in a public to private transaction and plays a key role. It only recommends the bid to the target's shareholders if it is convinced that the bid represents the best strategic option for the target and fair value for its shareholders.

##### Management board

The target's management board is responsible for the day-to-day management of the target. It has a fiduciary duty to act in the best interests of the company and its business.

In case of an MBO, the fiduciary duties of the MBO team members are likely to conflict with their own personal interest in the bid. Despite this, they do not need to resign from the management board, provided that:

- The entire board is aware of the situation.
- They comply with the provisions of the target's articles of association about management directors' conflicts of interest and the Corporate Governance Code (which applies to listed companies and other companies who voluntarily apply it).

In addition, the management board must ensure that the target continues to be run effectively throughout the bid process. The MBO team members have a duty to disclose all relevant information, including information about competing offers and other opportunities, to the rest of the management board.

The supervisory board and the management board jointly determine whether to make a favourable recommendation. In making this decision, the interests of all stakeholders must be taken into account.

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

In addition to contractual buyer protections for funds (see *Question 17*), management in an MBO must usually enter into restrictive covenants (including non-compete and confidentiality obligations).

If the target is acquired by a venture capital fund, management are also often asked to participate in the target's capital by acquiring shares, either directly or through a trust office (*administratiekantoor*). This participation (which requires the managers to invest their own private funds) creates a stronger commitment than options, grants and stock appreciation rights, although these instruments are also available.

### 20. What measures are commonly used to give a private equity fund a level of management control over the activities of the portfolio company (for example, representation at board level)? Are such protections more likely to be given in the shareholders' agreement or company bye-laws?

Private equity funds can use a variety of measures to obtain more management control over the activities of a portfolio company, for example:

- Representation on the management board or supervisory board (if any).
- Making certain management board resolutions subject to the approval of the general meeting or supervisory board (if any). These approval rights can be either specific or general.

These measures can be included in a shareholders' agreement and/or the articles of association.

### 21. What percentage of the finance will typically be provided by debt and what form does that debt financing usually take (for example, term loans, working capital facilities, convertible loans and bonds)?

Thin capitalisation regulations generally allow for a maximum debt-to-equity ratio of 3:1 for tax purposes, taking into account the taxpayer's equity for corporate income tax purposes. However, if the portfolio company is part of a group for accounting purposes that has a higher debt-to-equity ratio on a group basis, this higher ratio can be used instead, taking into account the taxpayer's equity for commercial purposes. If and to the extent the net total debt (the loans receivable minus the loans payable) exceeds three times the total equity, a proportionate part of the interest is not deductible. However, this restriction is limited to the net amount of interest due to and from all affiliates of the tax payer.

Term loans, working capital and mezzanine facilities are all forms of debt commonly used in private equity transactions (sometimes combined with a potential equity interest).

As a general rule, the interest expenses incurred on a loan are deductible in computing taxable profits for Dutch corporate income tax purposes. However, a deduction is disallowed for the interest

incurred on a debt obligation issued directly or indirectly to a related entity in connection with any of the following:

- Distribution of profits or a return of capital to a related entity.
- Capital contribution, or other use of equity funds, to a related entity.
- The acquisition of shares in an entity that is considered to be related after this acquisition.

The interest deduction limitations are not applicable if either:

- The transactions are entered into mainly for valid business reasons.
- The interest paid on the debt is subject to tax on income or profits which is considered reasonable by Dutch standards (10% is deemed to be a reasonable level of taxation).

### 22. What forms of protection do debt providers typically use to protect their investments, in particular through what types of:

- Security?
- Contractual and structural mechanisms such as subordination?

#### Security

Debt providers often, subject to certain financial assistance restrictions (see *Question 23*), take security.

#### Contractual and structural mechanisms

Debt providers often allocate a ranking at different levels of seniority.

Inter-creditor arrangements provide additional mechanisms to establish the priority of payments among all stakeholders.

### 23. 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 impact on the ability of a target company in a buyout to give security to lenders? Are there exemptions and, if so, which are most commonly used in the context of private equity transactions?

Under financial assistance rules contained in the Civil Code, a Dutch target cannot grant guarantees or security or otherwise accept liability with a view to the acquisition by the buyer of target shares, either in a domestic or cross-border transaction. This prohibition also applies to the target's subsidiaries including, probably, its foreign subsidiaries.

These limits can often be mitigated by a debt push down under which, simultaneously with or as soon as possible after the acquisition, the target distributes all of its distributable reserves to the buyer. Distributable reserves include the target's net assets, less the amount of its issued share capital and any mandatory reserves. The distribution is financed by additional external fi-

nancing, therefore increasing the target's debt. This is secured by guarantees by, and security over, the target group's assets. The buyer uses the proceeds of the distribution to repay part of the acquisition financing, therefore reducing the buyer's debt.

For private company targets, a debt push down can also be structured as a loan (instead of a capital distribution) by the target to the acquirer, up to the amount of the distributable reserves, provided that the loans are allowed under its articles of association.

Other structures may be available, such as merging the target and the acquirer. However, Dutch law does not provide for whitewash procedures setting aside financial assistance rules if certain procedural steps are taken.

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**24. What is the order of priority on insolvent liquidation? Are debt providers given priority over equity holders by law or is priority purely a matter of contract and company constitution?**

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Creditors of a company generally take priority over shareholders. Distributions on an insolvent liquidation are usually made in the following order of priority:

- Secured creditors (to the extent that recourse can be taken against the assets subject to the security rights).
- Costs and expenses (*faillissementskosten*) incurred by the trustee in winding up the company.
- Preferential creditors.
- Ordinary unsecured creditors.
- Shareholders of the company.

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**25. Is it possible for a debt holder to achieve equity appreciation through conversion features such as rights, warrants or options?**

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A debt holder can achieve equity appreciation through warrants and options, including contractual special rates of return on advances of debt.

## PORTFOLIO COMPANY MANAGEMENT

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**26. What management incentives are most commonly used (for example, shares, options and ratchets) to encourage portfolio company management to produce healthy income returns and facilitate a successful exit from a private equity transaction?**

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Management incentives are often included in the context of contractual protection for buyers (see *Question 17*) and management employment in an MBO (see *Question 19*). Shares and options are commonly used as incentives for portfolio company management. Share grants to employees are taxed when the right to the shares becomes unconditional, but tax on option grants is usually deferred until the exercise or disposal of the options.

## PRIVATE EQUITY/VENTURE CAPITAL ASSOCIATIONS

Dutch private equity and venture capital association (*Nederlandse Vereniging van Participatiemaatschappijen*) (NVP)

**Contact.** Tjarda Molenaar (Director)

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1070 AC Amsterdam  
The Netherlands  
**T** +31 20 5712270  
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**E** [info@nvp.nl](mailto:info@nvp.nl)  
**W** [www.nvp.nl](http://www.nvp.nl)

**Status.** The NVP is a non-governmental organisation.

**Membership.** The NVP has about 60 full members and also has associated members.

**Principal activities.** The NVP represents the interests of its private equity fund members and provides information on the private equity market in The Netherlands.

**Information sources.** See website address above.

In addition, management is also frequently offered incentives by good leaver and bad leaver arrangements.

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

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No specific tax reliefs or incentives are available for portfolio company managers investing in their company.

With respect to a Dutch resident sponsor of a private equity fund, a distinction is made between the taxation of carried interest and management fees:

- Carried interest is, in principle, subject to taxation in the hands of the sponsor, but may, under certain circumstances, be exempt under the participation exemption (see *Question 5*).
- Management fees are, under all circumstances, subject to taxation in the hands of a Dutch resident sponsor (or a sponsor who has a permanent establishment in The Netherlands to which the management fees are attributable).

Carried interest paid by a Dutch resident non-transparent fund is considered a profit distribution and, as such, is not deductible from the taxable profits.

There is uncertainty as to the tax treatment of carried interest. Tax authorities take the position that the carried interest is considered to be service income for the main portion and only the percentage of capital contributed can be considered dividend income. If this position holds up in court, it will lead to higher taxation.



## EXIT

**28. What forms of exit are typically used to realise a private equity fund's investment in a successful company (for example, trade sale, initial public offering (IPO) and secondary buyout)? What are the relative advantages and disadvantages of each?**

The most commonly used exits regarding successful portfolio companies are:

- Sales to third parties (usually strategic).
- IPOs.
- Sales of shares in a listed company on the secondary market.
- Sales of participations to other investors (secondary buyouts).

IPOs have the disadvantage of lock-up periods and strict regulatory legislation, which can often make IPOs time consuming. However, IPOs have the advantage of providing in general, and depending on the share prices in the relevant industry sector, a high return on investment. In 2006, the Dutch Ministry of Finance has granted a licence for the launch by Euronext Amsterdam of Alternext Amsterdam, an exchange regulated-market, intended to offer small and medium-sized companies a simplified access to the capital markets. Until now, the number of listings on this exchange has been very limited.

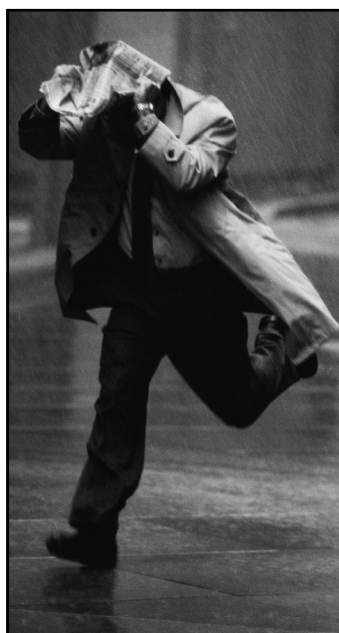
Sales to third parties may often be made more quickly than an IPO but with lower returns on investment (although the sale may be slowed down by competition in a controlled auction process).

For tax purposes, no exit strategy is particularly advantageous for a successful company because capital gains are generally exempt under the participation exemption.

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

Fire sales and voluntary liquidations are typically used to end the investment in an unsuccessful company. A fire sale usually has the advantage for the seller of being able to sell all the company's assets, but the disadvantage of a low purchase price. Voluntary liquidations may achieve a higher purchase price, but have the disadvantage of a long process, due to the statutory procedure required (such as publication requirements and rights for obstructive creditors).

Losses on unsuccessful portfolio company investments are generally not tax deductible under the participation exemption. However, in some circumstances, losses on the liquidation of an unsuccessful company can be tax deductible. Therefore, it may be preferable from a tax perspective for a fund to liquidate an unsuccessful company rather than sell it.



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