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The Reform of Dutch Private Company Law: New Rules for the Protection of Creditors

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Abstract

A Bill to amend Dutch private company law is currently pending before the Dutch Parliament. In our paper, we discuss the proposed rules for the protection of creditors of Dutch private limited companies (BVs). In order to give an insight in the background of the proposals, we first summarise our study on alternatives for capital protection, which served as a basis for the legislative proposals. Next, we point out what criticisms were made during the consultation following the publication of the draft Bill in April 2006 and how the legislature responded to these criticisms. We show that certain controversial provisions have been amended as a result of the outcome of the consultation process. Our paper ends with a few remarks on the rather limited amendments made to the Second Company Law Directive. We conclude that after the implementation of the Bill, the rules on creditor protection applicable to Dutch BVs and Dutch NVs (public companies) will differ considerably. In our view, there is no reason to fear that the new creditor protection rules applicable to the BV will lead to increased popularity of the NV, as has been suggested by some. Time will tell whether the fundamental reform of the law applicable to the Dutch BV renders it well-equipped to contend with foreign competition.

Keywords: Dutch private limited company law reform, creditor protection, capital maintenance.

1. INTRODUCTION

On 31 May 2007, a Bill to amend Dutch private company law[1] was sent to the Dutch Parliament. The Bill to amend Dutch private company law is the result of a project that was launched by the Dutch Ministry of Economic Affairs and the Dutch Ministry of Justice in 2003. The aim of this project is to make Dutch law on private companies more flexible and simple so that it better reflects entrepreneurial reality. Private companies need to be made more appealing to those who use them, bearing in mind the interests of other stakeholders. It is widely seen as a problem that the Dutch private limited liability company (BV) does not really have a distinct character: it is to a large extent subject to the same (strict) rules as

[1] There are two types of stock companies in the Netherlands: the BV (*besloten vennootschap*) and the NV (*naamloze vennootschap*). Currently, the law applicable to the BV differs from the law applicable to the NV in the following respects: the transferability of shares is restricted, issuance of bearer shares and share certificates is prohibited (issuance of registered shares only) and the BV requires a minimum capital of only €18,000 instead of €45,000 for the NV.

the Dutch public limited company (NV).[2] The legislature was also motivated by regulatory competition within the European Union, which was sparked off by a number of decisions of the European Court of Justice on the freedom of establishment, in particular the *Inspire Art* case.[3] The BV has to be well equipped in order to contend with foreign competition. An added benefit of the reform may be that administrative burdens and legal costs will be reduced.

An important part of the project to make Dutch private company law more flexible and simple concerns capital protection law. The criticism is that the existing system of capital protection does not provide adequate protection for creditors and places unnecessary obstacles in the way of private companies running their businesses.[4]

In May 2004, the Expert Group that had been commissioned to advise the Dutch government published its report containing proposals for the review of Dutch private company law.[5] These proposals included changes to the capital protection rules applicable to Dutch BVs.[6] After the publication of the Expert Group's report, a study on alternatives for the capital protection regime was carried out by the authors of this article, at the request of the Scientific Research and Documentation Centre (*Wetenschappelijk Onderzoek- en Documentatiecentrum*, WODC) of the Dutch Ministry of Justice. The final report was published on 18 August 2005.[7]

[2] See H.J. De Kluiver and S.F.G. Rammeloo, 'Capital and Capital Protection in the Netherlands: A Doctrine in Flux', in M. Lutter, ed., *Legal Capital in Europe*, ECFR Special Vol. 1 (Berlin, Walter de Gruyter 2006) pp. 559-560.

[3] ECJ, Case C-167/01 *Inspire Art* [2003] *ECR* I-10155.

[4] See De Kluiver and Rammeloo, loc. cit. n. 2, at p. 561.

[5] Eindrapport Expertgroep, *Vereenvoudiging en Flexibilisering van het Nederlandse BV-recht*, 6 mei 2004 [Final Report of the Expert Group, *Simplification and Flexibilisation of Dutch Private Company Law*, 6 May 2004]. This report is available on the website of the Ministry of Justice, at: <http://www.justitie.nl/images/eindrapport_tcm34-18395.pdf>. A summary of the Final Report of the Expert Group in the English language is available on the website of the Ministry of Economic Affairs, at: <http://www.ez.nl/content.jsp?objectid=150534&rid=150535>.

[6] The Expert Group's proposals for changes to the capital protection rules are to a large extent based on the conclusions of a comparative study carried out in 2004 by M.L. Lennarts and J.N. Schutte-Veenstra on behalf of the Dutch Ministry of Economic Affairs: *Versoepeling van het BV-kapitaalbeschermingsrecht* [Relaxation of the capital protection law applicable to private limited companies], Final Report dated 31 March 2004, IVO series, Part 47 (Deventer, Kluwer 2004).

[7] The report in the Dutch language is available on the website of the WODC, at: <http://www.wodc.nl/onderzoeken/onderzoek_1190.asp?soort=publicatie&tab=pub>. For an English translation of the report, see Hanny Schutte-Veenstra, Hylda Boschma and Marie-Louise Lennarts, *Alternative systems for capital protection*, Final Report dated 18 August 2005, IVO series, Part 50 (Deventer, Kluwer 2005) (hereinafter referred to as 'the Report').

The main purpose of our study was to establish whether other legal systems provide alternative systems for capital protection and, if so, whether these systems or elements of these systems could be incorporated into Dutch private company law without reducing the level of protection of creditors and shareholders.

In Part 2 of this article, we will first describe the Dutch capital protection regime currently applicable to private companies and the criticism thereof (section 2.1). Then, the content of our study (section 2.2) as well as our main findings and recommendations to the Dutch legislature (section 2.3) will be discussed.

In Part 3 of this article, attention will be paid to the current state of affairs with respect to the reform of Dutch private company law. During the course of 2005 and 2006, a draft Bill to amend Dutch private company law was published in three parts. The third part of the draft Bill, which concerned a revision of the capital protection rules, was made available for consultation in April 2006. Written reactions to the third part of the draft Bill were published on the website of the Ministry of Justice by the end of June 2006.[8] On 3 November 2006, the consolidated Bill to amend Dutch private company law was approved by the Council of Ministers and sent to the Council of State. The text of the Bill was, however, not available to the public until the Bill was sent to Parliament on 31 May 2007.

Because of the ongoing discussion in respect of the importance of formal rules on capital protection, we have chosen to show what points of discussion the draft Bill gave rise to and how the legislature has reacted to them. For this reason, we will first discuss the changes to the capital protection rules that were proposed in the draft Bill (sections 3.1 to 3.3). Then, we will identify certain controversial issues by discussing the outcome of the consultation process (section 3.4). Finally, we will indicate in which respects the creditor protection provisions in the Bill that was sent to Parliament differ from the draft Bill. We will show that certain controversial provisions have been amended as a result of the outcome of the consultation process. (section 3.5).

Part 4 of this article is dedicated to recent developments at EU level regarding the Second Company Law Directive, which contains capital protection rules for public companies. Pursuant to the implementation of the Second Company Law Directive in national law, the capital protection regime for Dutch public companies is even stricter than that for private companies. Here, too, there is a need for change, although in this case the initiative has to be taken by the European legislature (amendment of the Second Company Law Directive). Part 4 of this article contains a discussion of the amendments recently made to the provisions of the Second Company Law Directive by Directive 2006/68/EC.

In Part 5 of this article, some final remarks will be made.

[8] See: <http://www.justitie.nl/onderwerpen/wetgeving/bv%5Frecht/Consultatie%5Fderde%5Ftranche/>.

2. A DUTCH STUDY ON ALTERNATIVE SYSTEMS FOR CAPITAL PROTECTION

2.1 The Dutch capital protection regime on private companies in a nutshell and criticism thereof

Dutch law on private companies has a strict capital protection regime.[9] The main pillar of this regime is the capital of the company, which is divided into shares with a nominal value. In principle, this nominal value corresponds to the payment requirement for shareholders. The payment requirement for shares is the subject of the first category of the provisions of capital protection law. They include:

- the minimum capital requirement: the minimum issued and paid-up share capital for the BV is set at €18,000;[10]
- the requirement of a payment of at least 25 per cent of the nominal value of the acquired shares;[11]
- the requirement that a consideration in kind must have an economic value that can be established;[12]
- the prohibition on the contribution of an undertaking to perform work or provide services;[13]
- the provisions regarding the control of considerations in cash, which have to be accompanied by a statement of the bank that a cash consideration has been paid;[14]
- the provisions regarding the check on considerations in kind, which must be described by the incorporators/board of directors and accompanied by a valuation by an independent expert;[15] and
- the *Nachgründung* (post-incorporation) provision: if the BV acquires assets from an incorporator or shareholder within two years of the company's incorporation, both a description of the assets by the board of directors accompanied by a valuation by an independent expert and the approval of the general meeting of shareholders are required.[16]

[9] The capital protection regime that applies to the BV is almost similar to that which applies to the Dutch public company (NV). For the historical background of this similarity, see Part 5 of this article.

[10] Art. 2:178, para. 2 BW.

[11] Art. 2:191, para. 1 BW.

[12] Art. 2:191b, para. 1 BW.

[13] Art. 2:191b, para. 1 BW.

[14] Art. 2:203a, para. 2 BW.

[15] Arts. 2:204a and 2:204b BW.

[16] Art. 2:204c BW.

Besides provisions regarding the raising of capital, Dutch capital protection law also contains provisions relating to the maintenance of capital. For this second category of capital protection provisions, not only the capital itself but also the reserves stipulated by law and the articles of association are relevant. These reserves, together with the paid-up and called-up capital, are known as the tied-up assets. These assets may not be reduced by distributions to shareholders, regardless of the method used: (interim) dividend, purchase of own shares or repayments resulting from a capital reduction. The reason is that the tied-up assets should be maintained so that they can provide recourse for creditors. Book 2 of the Dutch Civil Code (*Burgerlijk Wetboek*, BW) therefore contains strict rules preventing erosion of the tied-up assets through distributions to shareholders. Distributions of dividend, the purchase of own shares and repayments with capital reduction are subject to an *enhanced balance sheet test* and are therefore only allowed if, and insofar as, the net assets exceed the sum of the tied-up assets.[17] Distributions of dividend, share buy-backs and repayments on shares that were effectuated in spite of the fact that there were no distributable reserves available are void, which means that the shareholder must pay back any sums he has received.

It should be noted that the purchase of own shares by the BV against consideration is not only subject to an enhanced balance sheet test but also to several other conditions: a BV may only repurchase shares up to a maximum of 50 per cent of the issued capital, the articles of association must permit the purchase of own shares and the general meeting of shareholders (GMS) must have authorised the repurchase.[18]

Dutch law also contains strict provisions regarding the giving of financial assistance to third parties for the acquisition of the company's own shares. A BV may not provide collateral, give a price guarantee, otherwise act as surety or bind itself jointly or severally with a view to the acquisition of the company's own shares.[19] The provision of loans by the BV to a third party in connection with the acquisition of the company's own shares is only allowed up to the extent of the distributable reserves.[20]

With regard to capital reduction, we note that Dutch law provides company creditors with a right to object to a capital reduction and ask for additional securities for the payment of their claims.[21]

[17] For distributions of dividend and the purchase of own shares, this follows from the statutory provisions (Art. 2:216, para. 2 BW and Art. 2:207, para. 2 BW). According to the prevailing opinion in literature, a capital reduction that involves a repayment on shares is also subject to the enhanced balance sheet test.

[18] Art. 2:207, para. 2 BW.

[19] Art. 2:207c, para. 1 BW.

[20] Art. 2:207c, para. 2 BW.

[21] Art. 2:209 BW.

There has been much criticism of the current Dutch capital protection regime,[22] both of specific provisions of capital protection law and of the system of capital protection as a whole. The capital protection provisions are not always easy to interpret, sometimes they are too strict (the legislation contains a lot of imperatives and little in the way of regulation), sometimes they are self-contradictory and some provisions are easy to evade. From a more principled point of view, the criticism is that the system of capital protection does not provide adequate protection to creditors and places unnecessary obstacles in the way of public and private companies running their businesses.

The minimum capital requirement, for example, provides only very limited protection to creditors. First, the amount of €18,000 of minimum capital is arbitrary. This amount of starting capital would not be sufficient for many business operations. Second, a minimum capital requirement only has meaning if the amount paid up for the shares is still actually available in the assets of the private company at the time that the creditor wishes to be paid for the goods or services supplied. There is no guarantee whatsoever that this will in fact be the case. The creditor requires settlement of his claim. In other words, the liquidity of the private company in the short and long term needs to be sufficient to settle the claims of its creditors. The minimum capital requirement falls short in this respect and only gives creditors the appearance of security.

Not only the provisions regarding the raising of capital but also the provisions relating to the maintenance of capital are not adequate from the point of view of creditor protection. Pursuant to the statutory provisions, the making of distributions to shareholders is bound up with having sufficient free distributable equity. Whether this condition is met has to be determined on the basis of the most recently adopted annual accounts. The data in these annual accounts is necessarily outdated by the time resolutions regarding distributions to shareholders are adopted. The financial position of the company may have changed drastically in the meantime. The Dutch Companies Act, however, does not provide for an additional liquidity test.

Already in 1991, the Dutch Supreme Court recognised the shortcomings of the statutory provisions on dividend distributions.[23] In the so-called *Nimox* case, the Court decided that the adoption of a GMS resolution for dividend distribution, which takes into consideration all the provisions of capital protection, does not indemnify the shareholders and directors against liability claims by third parties. If the dividend distribution could reasonably have been expected to lead to a

[22] See, *inter alia*, the special issue of the *Tijdschrift voor Insolventierecht*: *Curator en kapitaalbescherming* [Journal of Insolvency Law: The liquidator and capital protection] of November 2003 and the contributions of H.P.J. Ophof and J.W. Winter in *Knelpunten in de vennootschapswetgeving* [Problems in company law], IVO series, Part 24 (Deventer, Kluwer 1995).

[23] See HR 8 November 1991, *NJ* 1992 No. 174 (*Nimox*).

situation in which the claims of the company’s creditors can no longer be met, both the shareholders and the directors have acted unlawfully in the sense of Article 6:162 BW (tort law), if they voted for or implemented the resolution to distribute dividend in these circumstances. In doing so, they have disadvantaged the company’s creditors, who remain unpaid. They can thus be held liable for the damages suffered by the company’s creditors.

2.2 Content of study: legal systems of Australia, Delaware and the RMBCA

As we pointed out above, there is a need for a fundamental reform of the Dutch capital protection law. The means by which we can come to a simplification of the current Dutch system of capital protection and offer alternative solutions is to carry out a comparative legal study. There are legal systems that contain other mechanisms to protect creditors either instead of or alongside capital protection provisions. These regulations vary between two extremes. The greatest deviation from the current Dutch capital regime occurs in countries where shares with no nominal value are issued. In these countries, creditors are protected against non-payment of their claims by their debtor companies through measures such as publication requirements and liability provisions (e.g., in cases of wrongful trading). The systems of other countries, which do use the concept of par value shares as a basic principle, may contain provisions that are significantly more flexible in certain respects.

The study describes the creditor protection rules of three legal systems of non-EU countries. The reason why none of the Member States was included in the study is that the aim of the study is not limited to serving as a basis for the reform of the capital protection rules applicable to the private company. The aim of the study is broader: it should also play a role in the discussion on a fundamental review of the Second Company Law Directive.[24] The study seeks to find alternatives to the capital protection rules that are directly or indirectly derived from this Directive. It is hard to find such alternatives within the European Union: first, because the legislation of all Member States on public limited liability companies must be in accordance with the provisions of the Second Company Law Directive; second, because it cannot be denied that this Directive has had a considerable impact on the capital protection law applicable to private companies, in spite of the fact that there was no obligation for Member States to implement the Directive in the laws applicable to private companies. In some Member States, we see the phenomenon of imitation, in the sense that the capital protection regime for private companies has in many respects been amended in line with the implementation of the Second Company Law Directive in respect of public

[24] See section 4.5 of this article.

companies. This has occurred, for instance, in the Netherlands, Belgium, Denmark and Italy. In other Member States, this was not the case, but the Second Company Law Directive has nevertheless had an impact on legislation on private companies. For example, in the United Kingdom, there is no minimum capital requirement for private companies, but the provisions regarding distributions to shareholders and associated legal transactions are heavily influenced by the provisions of the Second Company Law Directive.

We have chosen to study the legal system of Australia and that of the US state of Delaware. The Revised Model Business Corporation Act (RMBCA), a model act drawn up by the American Bar Association, was also studied.

Australia was chosen because the nominal value of shares was abolished fairly recently there (1998). The reasons for this and the amendments necessary in company legislation as a result of the abolition can therefore be clearly identified. Company law in the state of Delaware is considered to be a leading model and therefore could not be omitted. It is also an interesting point that under Delaware law a company can issue shares both with and without nominal value.[25] Finally, the RMBCA was studied because of the extensive influence this model act has had on the company law of many other US states.

With this choice of legal systems, an attempt has also been made to give a representative picture of the possibilities offered by foreign legal systems for alternative regulation for the protection of corporate creditors. Such alternative regulation can be found both in systems where shares have a nominal value and in systems where nominal value has been abolished. For this reason, we decided to describe:

- a legal system that only permits real no par value shares in combination with provisions for capital protection (Australia);
- a legal system that is based on the issue of real no par value shares but in which the issue of par value shares is not prohibited (RMBCA); and
- a legal system that allows the company to issue shares with or without nominal value or a combination of the two (Delaware).

We have made a comparative legal study of the three above-mentioned legal systems, using a number of questions[26] grouped around three themes: creditor protection, shareholder protection and the introduction of NPV shares.

The themes and questions were arrived at on the basis of a number of focal points in the study. First, it is important to establish which provisions in the legal system concerned contribute to the protection of the interests of creditors. This

[25] See § 151 DGCL (Delaware General Corporation Law).

[26] These questions are enumerated on pp. 11 and 12 of the Report.

concerns provisions relating to the payment for shares and the making of distributions to shareholders, but also publication requirements and liability provisions.

We have included aspects of shareholder protection as well as creditor protection for two reasons. Some of the capital protection provisions are part of the protection of the interests of shareholders, such as the prohibition of share issues below par and pre-emptive rights in a share issue. The second reason is that part of the study concerns the advantages and disadvantages of introducing NPV shares. The term nominal value is important for the position of the shareholders. In principle, the nominal value is the determining factor for the voting rights and rights to profits attached to a share. Furthermore, the nominal value is the starting point when establishing the issue price of a share. The nominal value of a share also affects the setting of thresholds for decision making at the GMS, such as requirements relating to a majority of votes and a quorum. Finally, the nominal value of a share is used as a criterion for determining whether one or more shareholders can establish claims or make certain requests. Any abolition of the nominal value would mean that another criterion would have to be established for all these issues. Ideas for this can be obtained from the legal systems studied.

A third theme concerns the introduction of NPV shares. Consideration needs to be given to whether there were specific problems involved in the introduction of NPV shares in the respective foreign legal systems, so that they can be avoided in the event of such an introduction in the Netherlands. The question whether a company may simultaneously issue shares with and without nominal value, and under what conditions a conversion of both types of share would be possible, is also considered.

We have made a country report for each of the legal systems studied. In each country report, the main features of the legal system and the answers to the questions mentioned above are discussed.[27] The report itself contains an integrated treatment of the results of the study and the conclusions and recommendations derived from them. The report also contains a matrix[28] showing the results of the study in diagram form.

For our study, we consulted the following sources: legislation, literature and case law. Certain experts from the legal systems investigated were also consulted (in Australia, officials of the Australian Treasury, in cooperation with employees of ASIC,[29] the regulator; in the United States, lawyers active in insolvency practice). They answered many of our questions, which mainly concerned clarifications and additions to the study of legislation, literature and case law in the legal system concerned. However, little or no information was available on

[27] These country reports are enclosed as attachments to the original report in the Dutch language (see n. 7).

[28] See pp. 66-73 of the Report.

[29] ASIC is the government body that registers companies. ASIC also provides publicly available information on all Australian companies through its ASCOT database.

the practical application of alternative systems for capital protection. A much more extensive study would have to be set up for this, for example, through surveys of company directors and insolvency specialists.

2.3 Main findings and recommendations

2.3.1 *Introduction*

In this section, we will present the main findings of our study, as well as our recommendations to the Dutch legislature, regarding the raising of capital (section 2.3.2), distributions to shareholders (section 2.3.3) and the introduction of NPV shares (section 2.3.4).

2.3.2 *Raising capital*

2.3.2.1 Main findings

The study shows that the legal systems of Australia, Delaware and the RMBCA offer much more freedom for companies in the area of raising capital than is the case in the Netherlands.

First of all, there is *no minimum requirement* for the amount of issued and paid-up share capital upon incorporation of a company. In the legal systems studied, it is for the founders and subsequently the directors of the company to assess how the company's operations should be financed and to what degree the amounts paid or assets contributed for the shares should contribute to this. If it turns out that the company is inadequately financed, repressive measures can be taken. Directors who authorise distributions when the company is in a precarious financial position incur liability risks.[30]

With regard to the *contribution of assets*, we note that in principle the laws of Delaware and the RMBCA place no limitations on the form of considerations in kind.[31] In Australia, a contribution should represent money's worth. The contribution of an undertaking to perform work or supply services meets this requirement.[32]

The *valuation of the consideration* for shares is also left to the founders or directors; they do not have to engage independent experts for this. It is the duty of the company's directors to determine that the value of the consideration is

[30] See further section 2.1.2 of the Report.

[31] See § 6.21 (b) RMBCA and § 152 DGCL. Under the RMBCA, a choice for the contribution of an undertaking to perform of work or supply services can have consequences for the transferability of the shares concerned and the dividend received thereon.

[32] See further section 2.1.4.1 of the Report. See also *Re White Star Line Ltd* [1938] 1 *All ER* 607.

adequate. It is notable that in Delaware and under the RMBCA the value attributed by the directors to a non-cash consideration is decisive unless there is a situation of fraud,[33] while in Australia the directors can be guilty of a breach of their fiduciary duties if they overvalue a consideration and can be held liable.[34] At first sight, it would appear that directors in Australia are more likely to be held liable. However, the case law on this point shows that directors have a large degree of freedom in the valuation of the consideration. Only in cases where a company issues shares to its director against a consideration in kind and this director has overvalued the consideration is there a situation of a breach of his fiduciary duties (duty to avoid conflicts of interests).[35]

2.3.2.2 Recommendations

On the basis of our study, we concluded that there are good grounds for abolishing the Dutch provisions regarding the raising of capital for private companies.[36] The provisions go further than necessary for the purpose of giving protection to creditors and also involve unnecessary costs for businesses. This means that the following provisions of Dutch company law could be abolished: the minimum capital requirement, the provisions regarding the payment obligation on shares (statement of the bank that a cash consideration has been paid and the valuation of a consideration in kind by an independent expert) and the *Nachgründung* (post-incorporation) provision (which applies to a company acquiring assets belonging to the founders of the company). The legal systems studied do not have such provisions either.

We also recommended repealing the prohibition on the contribution of an undertaking to perform work or supply services. It is clear that the abolition of this prohibition would make Dutch company law more flexible. The study shows that, in principle, no limitations apply to the form of a consideration in kind under the RMBCA or in Delaware. In Australia, a consideration should represent money's worth; a contribution of work or services to be performed meets this requirement.

[33] See, respectively, R. Franklin Balotti and Jesse A. Finkelstein, *Delaware Law of Corporations and Business Organizations*, 3rd edn., Vol. 1 (New York, Aspen 1997) pp. 5-25/5-26; and B. Manning and J.J. Hanks, *Legal Capital*, 3rd edn. (Westbury, NY, The Foundation Press 1990) p. 181.

[34] See the CSLRC (Companies and Securities Law Review Committee) Report: *Issue of Shares for Non-Cash Consideration and Treatment of Share Premiums* (September 1986).

[35] See further sections 2.1.4.2 and 2.1.4.3 of the Report. See also *Re Baglan Hall Colliery Company* (1870) LR 5 Ch App 346; *Re Wragg Ltd* [1897] 1 Ch 796; [1895-99] *All ER Rep* 398; *Re White Star Line Ltd* [1938] 1 *All ER* 607; and the CSLRC Report, op. cit. n. 34.

[36] See Lennarts and Schutte-Veenstra, op. cit. n. 6, at pp. 11-33.

The basic principle is that a contribution must have a value in economic terms. In this context, it is unclear why a distinction is made between the contribution of a right to one's own or another's work or services, on the one hand, and a contribution of goodwill and know-how, on the other. All these contributions can be valued in economic terms. However, the former cannot form a contribution, while the latter can. Furthermore, it can be difficult in practice to distinguish between the contribution of know-how and the contribution of a right to future work.

It is obvious that certain risks, relating to the valuation of such a contribution, are involved in a contribution of future work or services. Take a situation in which the work or service is not carried out because the contributor is no longer in a position to do so, having fallen sick or died. If the work or service is of a personal nature and cannot be carried out by another, this means in reality that the agreed contribution for the shares has not and will not be paid. This will necessitate reverting to a cash payment for the shares. The problem is usually that there is no cash available, as people will have chosen to make a contribution in the form of future work or service for a reason. However, the existence of these risks does not necessarily mean that such contributions should be prohibited. They should be included in the calculation of the economic value of the work or services to be contributed. The company may require a bank guarantee from the shareholder or that the shareholder takes out insurance to cover these risks, with the company as the beneficiary. If this is done, the risks attached to a contribution of future work or services no longer play a part. In all other situations, however, this remains the case.

2.3.3 *Distributions to shareholders*

2.3.3.1 Main findings

Distribution of dividend. In all three legal systems studied, the board of directors is the entity authorised to make distributions.[37] The criteria to be considered for making a distribution of dividend, however, differ in each legal system under review.

The accepted tests in the legal systems studied are the liquidity test and the balance sheet test. In the *liquidity test*, the criterion is whether the company, assuming that its operations continue, has sufficient cash available after making the distribution to be able to meet the debts that fall due in the following period as a result of its ordinary business operations. In the *balance sheet test*, the criterion is whether after making a distribution the assets of the company are at least equal to its debts and provisions. Only the surplus may be distributed.

[37] In Australia, the company's constitution may deviate from this general rule.

Under § 6.40 (c) RMBCA, distributions have to pass a double test consisting of a combination of a liquidity test and a variant of the balance sheet test.

With regard to the liquidity test, it should be noted that, according to the official commentary on § 6.40 RMBCA, generally available information will, in most cases in which a business is operating normally as a going concern, make it clear that there are no grounds for an investigation as to whether the company can meet the requirements of the liquidity test. The existence of significant shareholders' equity and normal operating conditions in themselves form a strong indication that the liquidity test will not cause problems. When, then, are there grounds for an investigation into a company's liquidity position? The official commentary on the RMBCA says the following on this point:

> It is only when circumstances indicate that the corporation is encountering difficulties or is in an uncertain position concerning its liquidity and operations that the board of directors or, more commonly, the officers or others upon whom they may place reliance under section 8.30 (b), may need to address the issue.

The variant of the balance sheet test means that the company should maintain a certain capital cushion. This cushion, however, only concerns the amount that would be needed, if the company were to be dissolved at the time of the distribution, to satisfy the holders of shares with a preferential right with regard to the liquidation surplus. This capital cushion, however, has nothing to do with creditor protection.

The RMBCA is very liberal with respect to the question of the valuation of assets and liabilities associated with the balance sheet test. Directors may use accounting practices and principles that are reasonable in the circumstances or a fair valuation or other method that is reasonable in the circumstances. This means that, in principle, directors are free to deviate from the GAAP principle that assets must be reported in the balance sheet at historical cost. There is criticism of this to the extent that it can lead to the distribution of pure holding gains, which are based on the revaluation of assets. In this respect, however, it should be noted that the RMBCA does not permit selective revaluation.

When forming their opinion, according to § 8.30 RMBCA, directors may in principle use information, opinions, reports and statements originating from other expert persons. It cannot normally be expected of directors that they should go into the details of the various analyses and market and economic forecasts that may be relevant in depth. However, § 8.30 RMBCA does state that directors may not adopt the opinion of an expert if they themselves possess information that makes reliance on that opinion unwarranted.

One important question is what is the relevant date should be for determining whether a distribution meets the double test of § 6.40 RMBCA. For dividend distributions, the answer can be found in § 6.40 (e) (3) RMBCA. The date of the decision by the board of directors applies as the standard date for the assessment of the lawfulness of the dividend distribution if the payment occurs within 120 days after the date of authorisation by the board of directors.[38] If payment occurs more than 120 days after the date of authorisation, the standard date is the date the payment is made. The extent of the validity of a positive result from the liquidity and balance sheet tests is therefore not more than 120 days.

In Delaware, dividend distributions are subject to a balance sheet test.[39] The basic principle is that the board of directors is only authorised to make dividend distributions if and to the extent that there is a surplus. If a company has issued NPV shares, there is a surplus if the company's equity is positive (bare net assets test). If the company has issued PV shares, then the company's equity should be greater than its capital (enhanced assets test). This also applies if the company has issued NPV shares and the board of directors has designated part of the consideration for shares as capital. The amount of the capital is the buffer that may not be touched by the making of dividend distributions. There is one exception to this basic principle that a company may only make distributions if and to the extent that there is a surplus: the nimble dividends provision.[40] This means that, in the absence of a surplus, the company may nevertheless distribute dividend to the extent that it has realised net profits in the financial year in which the dividend is set or in the previous financial year. This implies that losses sustained in a previous financial year do not first have to be made good before the company may distribute dividend. From the point of view of creditor protection, such a regulation is not to be preferred. The financial years should be considered as a whole, so that losses previously sustained have to be made good before dividend distributions can be made. A temporary improvement in a company's financial position should not lead to a distribution being made to the shareholders at a time when this would be at the expense of the company's creditors. Indeed, this would mean that the shareholders would receive a benefit when their position is subordinate to that of the company's creditors.

In Australia, the statutory criterion for the payment of dividend is that there must be sufficient profits to do so.[41] The regulation is unclear, since there is no statutory definition of the term profits and the case law[42] does not offer a solution

[38] In cases of distribution by purchase, redemption or other acquisition of the company's shares, the standard date is the date on which money or other property is transferred or a debt is incurred by the company in connection with the distribution. If, however, the shareholder ceases to be a shareholder with respect to the acquired shares, the date the shareholder ceases to be a shareholder is the standard date. In the case of a distribution of indebtedness, the date the indebtedness is distributed is the standard date.

[39] § 170 (a) DGCL.

[40] ON this provision, see M.A. Eisenberg, *Corporations and Other Business Organizations*, 8th edn. (New York, Foundation Press 2000) p. 1257.

[41] See § 254T CA2001.

[42] See *Re Spanish Prospecting Co Ltd* [1911] 1 Ch 92; *Foster New Trinidad Lake Asphalte Co Ltd* [1901] 1 Ch 208; *Ammonia Soda Co Ltd* v. *Chamberlain* [1918] 1 Ch 266; *Quick* v. *Stoland* [1998] 29 ACSR 130.

in all cases. A second disadvantage is that a distribution of nimble dividends is permitted.[43] Moreover, in practice, because of the additional effect of the insolvent trading provisions,[44] a liquidity or solvency test applies. It would be better if this test were to be included in the statutory provision on the payment of dividend.[45]

In all three legal systems, acting in contravention of the above-mentioned criteria for the distribution of dividend can lead to the liability of the directors towards the company. It is important how this remedy relates to any liability of the shareholders to repay the unlawful dividend distribution they have received. For example, are the directors only liable for the amount that cannot be reclaimed from the shareholders? It is also relevant whether the shareholders are only obliged to repay the distribution if they have acted in bad faith. Under the RMBCA and in Delaware, a director held liable has recourse to shareholders who acted in bad faith.[46] The fraudulent transfer rules can also be used to compel shareholders who acted in good faith to repay the unlawfully distributed amount they received.[47]

Under Australian law, directors and shareholders acting in bad faith may be equally subject to a claim by ASIC to pay damages to the company, among other things.[48] In practice, it is more important that the directors incur liability risks under the insolvent trading provisions.[49] This procedure is normally initiated by the liquidator. If a director is guilty of insolvent trading, either the liquidator or ASIC, but also – in certain circumstances – an individual creditor, can make a claim for payment of damages. In the first two cases, the director has to pay damages to the company in question; in the third case, the individual creditor is reimbursed for the damages sustained.[50]

Purchase of own shares. The study shows that, under the RMBCA, the same criterion applies for a purchase of a company's own shares as for making a dividend distribution: a liquidity test and a variant of the balance sheet test.[51] In Delaware, too, the same general rule applies: the company may only repurchase

[43] See *Ammonia Soda Co Ltd* v. *Chamberlain* [1918] 1 Ch 266. See also AARF, *Payment of Dividends under the Corporations Act 2001*, April 2002, p. 1, available at: <http://www.aarf.asn.au/docs/Dividends.pdf>.

[44] See § 588G CA2001.

[45] See section 2.2.1.2 of the Report.

[46] § 8.33 (a) RMBCA and § 174 (c) DGCL.

[47] Rules in respect of fraudulent transfers can be found, for example, in the Uniform Fraudulent Transfer Act (UFTA) and in § 548 Bankruptcy Code.

[48] See §§ 256D (3) and 1317E CA2001.

[49] See § 588G (1a) CA2001.

[50] See section 2.2.1.3 of the Report.

[51] See §§ 6.40 and 6.31 RMBCA.

its own shares if and to the extent that there is a surplus.[52] Preference shares, however, may be repurchased at any time. The reason for this is not clear. Another exception concerns a situation in which the company has not issued preference shares and the repurchased shares are withdrawn and the company's capital is reduced simultaneously. The question is, what meaning does this exception to the surplus rule have, given the statutory provision that the company should have enough assets available to be able to meet its liabilities after such a capital reduction? In Australia, on the other hand, different criteria apply for a dividend distribution and a share buy-back – at least on paper. The condition for a payment of dividend is that the company should have sufficient profits at its disposal, whereas a liquidity or solvency condition applies for a share buy-back.[53] In practice, however, due to the additional effect of the insolvent trading provisions, a liquidity or solvency test also applies to the making of dividend distributions.[54]

In two of the three legal systems, the purchase provision is limited to the prescription of a criterion for payment of the acquisition price of the company's own shares. Only in Australia do further requirements apply. It is notable that here, too – in a somewhat different form – the limit of 10 per cent known in Dutch public company law applies.[55] The division of powers between the board of directors and the GMS is also regulated to prevent shareholders being treated inequitably.[56]

Financial assistance. Only Australia has a special statutory regulation for financial assistance.[57] Under the RMBCA and in Delaware, the authority of the board of directors includes an assessment of whether or not the company should enter into such transactions. Important elements in Australian regulation are that the approval of the GMS is required and that a liquidity or solvency test must be taken into consideration.[58]

Capital reduction. For a capital reduction, a liquidity test applies in both Delaware – 'no reduction of capital shall be made or effected unless the assets of the corporation remaining after such reduction shall be sufficient to pay any debts of the corporation for which payment has not been otherwise provided'[59] – and

[52] See § 160 DGCL. See also Michael P. Dooley and Michael D. Goldman, 'Some Comparisons between the Model Business Corporation Act and the Delaware General Corporation Law', 56 *Business Lawyer* (2001) p. 741 and footnote 22.

[53] See § 257A CA2001.

[54] See section 2.2.2.2 of the Report.

[55] See § 257B (1) CA2001.

[56] See section 2.2.2.2 of the Report.

[57] See § 260A CA2001.

[58] See section 2.2.4.1 of the Report.

[59] See § 244 (b) DGCL.

Australia – 'the reduction: … does not materially prejudice the company's ability to pay its creditors'.[60] Since the RMBCA does not acknowledge legal capital, it has no provisions regarding capital reduction. The board of directors is authorised to reduce a company's capital in Delaware.[61] In Australia, a capital reduction must be approved by the GMS.[62,63]

2.3.3.2 Recommendations

On the basis of our study, we made several recommendations to the Dutch legislature regarding distributions to shareholders. Some of these recommendations are discussed below.

Specific creditor protection when making distributions. We have taken as a starting point that specific provisions are necessary if the company makes distributions to shareholders and engages in associated transactions. In comparison to normal commercial transactions, these transactions involve extraordinary risks for creditors. Assets disappear from the company without anything being received in exchange. Creditors have an interest in a company having sufficient cash available after making distributions to pay debts as they fall due (in the following period) in its ordinary course of business.

Balancing interests of creditors, shareholders and directors. When implementing a new regime for distributions to shareholders, the interests of creditors as well as the interests of shareholders and directors have to be taken into account. If the company makes a profit, the shareholders justifiably wish to share in this as a reward for their investment. Directors have a special responsibility regarding the making of distributions, since financial policy is part of their duties. It is in their interest that the conditions under which distributions can be made are clear. An additional benefit of this is that, if these conditions are not observed, there will also be clarity regarding the personal liability of directors.

Directors' statement. If we take the special responsibility of directors for the making of distributions to shareholders as the basic principle, it should also be a requirement that they make an explicit statement that the distribution will not negatively affect creditors. This could be in the form of a published statement, in which the directors declare that, in their assessment, the distribution complies with the applicable requirements. The directors may only implement a resolution

[60] See §§ 256D (1) and 256B (1) CA2001.
[61] See § 244 DGCL.
[62] See §§ 256B (1) and 256C CA2001.
[63] See sections 2.2.3.1 and 2.2.3.2 of the Report.

by the GMS – or another body indicated in the articles of association – to make a distribution on the condition that they submit a positive statement of this type. The board of directors' statement will also clarify the relationship between the GMS and the board of directors (see below). Making a board of directors' statement on the making of distributions mandatory will have a negligible effect on administrative costs. We are not suggesting that the statement has to be certified by an auditor. A solvency declaration was made mandatory in New Zealand a decade ago and works quite satisfactorily.[64] In the United Kingdom, the Companies Act 2006 introduces a solvency statement to be submitted by the directors if private companies reduce their capital.[65]

Implementation of a simple balance sheet test combined with a liquidity test. Retaining the enhanced balance sheet test mentioned in Article 2:216, paragraph 2 BW means that the current problems will continue. This test does not provide creditors with the desired reasonable prospect that, after making a distribution, a company will be able to pay its debts as they fall due. And, in the interests of the directors, there is not the desired clarity of the conditions under which distributions may take place.

One simplification could consist of replacing the enhanced balance sheet test with a simple balance sheet test. A buffer is built into the current enhanced balance sheet test: after a distribution is made, the amount of the company's assets must be no less than the sum of its debts and provisions, plus the amount of the paid-up and called-up capital, plus the reserves that must be maintained under the law and the articles of association. Since the possible abolition of the minimum capital requirement for private companies is envisaged, the buffer in many cases could end up as a very small amount. It is questionable what extra protection the prescription of a buffer gives to creditors and whether such a prescription is justified. The prescription of an enhanced balance sheet test appears to be unnecessary from the point of view of creditor protection and also forms a burden for companies. We therefore recommend the *introduction of a simple balance sheet test*.

The condition imposed by a simple balance sheet test is that a company's equity may not be negative as a result of a distribution to shareholders. Whether this condition is met should be assessed on the basis of the information in the

[64] This is apparent from a comparative legal report prepared under the responsibility of J. Rickford, ed., 'Reforming Capital: Report of the Interdisciplinary Group on Capital Maintenance', The Company Law Centre, British Institute of International and Comparative Law, published in 15 *European Business Law Review* (2004) p. 972.

[65] See sections 642 and 643 of the Companies Act 2006. The Companies Act 2006 received Royal Assent on 8 November 2006. It is expected that all provisions of the Act will be implemented by October 2008. The full text of the Companies Act 2006 is available at: <http://www.opsi.gov.uk/acts/acts2006a.htm>.

annual accounts, with all the uncertainties this involves. So many factors affect the size of a company's equity, such as what is meant by assets and liabilities. The discussion of the position of preference shares under the International Financial Reporting Standards (IFRS) is a good example.[66] Furthermore, the result depends on the accounting principles applied – for example, historical cost price or market value – for the valuation of assets and liabilities. Another significant factor is whether or not the valuation is made on a going concern basis. In short, the result depends on the criteria and accounting principles underlying the calculation, for which rules are laid down in legislation and financial reporting standards.

We propose that the legislation and standards in force at the time of the decision should be decisive, as should the choices made by companies in this area. The consequence of this is that different standards may apply to both different and similar types of company, depending on the choice made by the company in question. Listed companies have to prepare their consolidated annual accounts in accordance with the IFRS from financial year 2005. Unlisted Dutch companies can voluntarily apply the IFRS from financial year 2005 for both their unconsolidated and consolidated annual accounts, but also have the option of applying the standards of Title 9, Book 2 of the Dutch Civil Code.[67]

The potential differences in the amount of the distribution arising from the application of different financial reporting standards have been taken into account in our proposal. International developments in the area of financial reporting standards law mean that the link between financial reporting standards law and capital protection law introduced by the Second and Fourth Company Law Directives is becoming more tenuous. The actual function of the annual accounts is therefore becoming more defined. They are mainly intended to provide information on the company's financial position to its capital providers and other stakeholders.[68]

The disadvantages of prescribing a simple balance sheet test, such as possible fair value valuations instead of valuations according to the principle of prudence[69]

[66] See J.M. van Dijk, 'Van prefs die vreemd vermogen zijn' [About preference shares that qualify as debt], 6 *Ondernemingsrecht* (2004) p. 211 et seq.; and C.J.A. van Geffen, 'De grens tussen eigen en vreemd vermogen' [The dividing line between equity and debt], 6 *Ondernemingsrecht* (2004) p. 207 et seq.

[67] Title 9, Book 2 of the Dutch Civil Code provides rules on the drawing up and publication of annual accounts. These provisions are the result of the implementation of the Fourth and Seventh Company Law Directives (Directive 78/660/EEC of 25 July 1978, *OJ* 1978 L 222, and Directive 83/349/EEC of 13 June 1983, *OJ* 1983 L 193) into Dutch company law.

[68] See C.J.A. van Geffen, 'De wijzigingen in het (Europese) jaarrekeningenrecht; invloed op het kapitaalbeschermingsrecht?' [Changes in (European) annual accounting law; what effect on capital protection law?], *TvI* (2003) p. 254 et seq.

[69] As specified in Art. 2:384, para. 2 BW: profits must be realised on the balance sheet date.

and the uncertainties involved in the use of several distinct financial reporting standards, are addressed by *prescribing a liquidity test alongside the balance sheet test*. The simple balance sheet test is an initial test to check whether the company's assets are at all greater than its debts and provisions, in other words, whether there is scope to make a distribution to shareholders. The liquidity test gives additional protection: the distributions will only be made if it is clear that the creditors can be paid thereafter. Application of the liquidity test should therefore prevent distributions to shareholders that have too great an effect on a company's liquidity, so that creditors are disadvantaged. The prescription of a liquidity test is, as it were, a codification of the *Nimox* case.[70] The drawback of making only a liquidity test mandatory is that the test only has to consider liabilities in the relatively short term, which is associated with the necessary uncertainties. This is the reason we are recommending a simple balance sheet test in combination with a liquidity test. This combination offers creditors a reasonable prospect that, after the distribution, the company will be able to pay its debts as they fall due.

When prescribing a liquidity test, the interests of the directors also have to be considered. The conditions whereby they can make a distribution to shareholders must be clear. For this reason, the requirements that a liquidity test must meet must be stated clearly. It is proposed that the directors prepare a liquidity estimate for the coming twelve-month period. The actual requirements this liquidity estimate must meet can be established in consultation with accounting organisations.

Same threshold for the various distributions. From the point of view of consistent legislation, the same threshold should be set for the making of distributions to shareholders regardless of how this is done. This basic principle means that a simple balance sheet test in combination with a liquidity test should apply for the distribution of (interim) dividend, a purchase of the company's own shares and distributions to shareholders as part of a capital reduction. If a separate regulation continues to exist for the provision of financial assistance for the acquisition of the company's own shares – this point is dealt with below – this threshold should also apply to these transactions.

Relaxation of the purchase regulation. The purchase regulation can be limited to prescribing the criterion for the payment of the acquisition price for the company's own shares: a simple balance sheet test in combination with a liquidity test. The 50 per cent threshold does not need to be retained from the point of view of creditor protection. From the point of view of protecting the interests of

[70] See HR 8 November 1991, *NJ* 1992 No. 174 (*Nimox*). See section 2.1 of this article for the meaning of this judgment.

shareholders, the division of powers between the board of directors and the GMS must remain the subject of regulation, contrary to the situation under the RMBCA and in Delaware.

Abolition of financial assistance provision. The study shows that, in two of the three legal systems studied, there is no separate regulation regarding the provision of financial assistance to third parties for the acquisition of the company’s own shares. Only in Australia is this otherwise. This raises the question whether a separate statutory regulation as laid down in Article 2:207c BW needs to be retained. Is it not the duty of the board of directors to assess whether or not such a transaction is in the company’s interest – risk analysis – and to check whether the company is still in a position to meet the claims of its creditors after providing the financial assistance? If the board of directors does not fulfil this duty adequately, it incurs liability risks. These financial assistance transactions do not differ from other commercial transactions, such as other types of loans to shareholders, directors or third parties, to the extent that a special statutory regulation is justified.

Abolition of the right to object to a capital reduction. If a company makes distributions to shareholders as part of a capital reduction, a simple balance sheet test in combination with a liquidity test applies. This provides sufficient protection for creditors. The right to object to a capital reduction – which is unknown in the three legal systems studied – can be abolished.

2.3.4 *Introduction of NPV shares*

2.3.4.1 Main findings

Connection of an alternative regime and NPV shares. The main purpose of our study was to establish whether other legal systems provide alternative systems for capital protection and, if so, whether (elements of) these systems could be incorporated into Dutch company law without reducing the level of protection of creditors and shareholders. It turns out that the legal systems of the RMBCA, Delaware and Australia do indeed offer alternative systems for capital protection. It also emerges that the implementation of these alternative systems is usually associated with abolition of the nominal value of shares in these legal systems. We wish to emphasise here that any implementation of an alternative system for capital protection in Dutch company law does not necessarily have to involve the introduction of shares without nominal value. However, the issue is worth consideration, all the more so since the study shows that NPV shares and alternative systems for capital protection act as communicating vessels. For the best possible assessment of whether NPV shares should be introduced in the Netherlands, we first considered what functions the nominal value of shares fulfils in current Dutch company law. We then looked at how these functions are fulfilled in the legal systems studied.

Replacement measures. The fact that a share has a nominal value is not a fundamental principle of Dutch company law. Abolition of the nominal value of shares, however, would have consequences for other areas besides capital protection provisions in (and outside) Book 2 of the Dutch Civil Code. Pursuant to current Dutch company law, the nominal value is a criterion for determining the voting rights and rights to profits of shareholders. It is also a criterion from which deviation is possible in many ways.[71] The nominal value of a share also plays a part in determining the thresholds for decision making in the GMS, namely in the requirements regarding a majority of votes and a quorum. Lastly, the nominal value of a share is used as a criterion for determining whether one or more shareholders can make certain claims or certain requests. If the nominal value is to be abolished, other measures would have to be found. The study shows that in each legal system there are various measures used for each of these issues. The three legal systems studied have in common that, for the determination of the voting rights on shares, the criterion is that one share has one vote. However, there is much freedom to deviate from this criterion in a company's articles of association. All this means, for instance, that a notion such as '10 per cent of the issued capital' – depending on the substance of the statutory provision – could be replaced by '10 per cent of the total issued shares' or '10 per cent of the total votes to be cast'. It is also possible to choose an absolute criterion, for example that a GMS could be convened at the request of at least 100 shareholders.

2.3.4.2 Recommendations

Various measures possible. The study shows that the criterion of the nominal value of shares can be fairly easily replaced by other measures. No particular criterion is recommended as a replacement. The best possible criterion must be chosen for each regulation. In share issues, the nominal value can be replaced by the issue price; in the case of voting rights, the 'one share one vote' idea can be the basic principle. For the determination of rights to profits, the basic principle can be that all shareholders share equally in the profits. Companies must be offered the scope to deviate from these basic principles in their articles of association. For issues such as voting majority and quorum requirements, a percentage of the total number of votes to be cast or a percentage of the total number of shares can be decisive. The same applies to the thresholds that must be

[71] See proposed Art. 2:228 BW in the official draft amendment to Book 2 of the Dutch Civil Code in connection with the rules for private limited liability companies. See: <http://www.justitie.nl/onderwerpen/wetgeving/bv%5Frecht/Consultatie%5Feerste%5Ftranche/>.

reached if shareholders wish to make an appeal to certain minority rights. One could also choose an absolute criterion, for example, a certain right may be invoked at the request of a certain minimum number of shareholders.

Introduction of NPV shares. The heart of the matter is whether the reasons for the abolition of the nominal value of shares are sufficiently convincing. The main argument for abolition, as appears from the explanations given by the legislatures that have introduced shares without nominal value, is that the false appearance generated by the nominal value, whereby shares appear to have a certain value that in most cases does not correspond to reality, is avoided. Legislation should be as simple and clear as possible. Terms that have no distinct meaning should be avoided. Retention of terms simply because of familiarity in practice ignores the fact that future generations of businessmen, investors, lawyers and others will have to become acquainted with them. For this reason, we recommend the introduction of NPV shares.

The Dutch legislature can realise this for private companies (BVs). However, the introduction of NPV shares for public companies (NVs) is only possible if the Second Company Law Directive is amended appropriately. It is conceivable that, following such an amendment, the two systems – PV shares and NPV shares – will continue to exist alongside each other. The fact that this is perfectly possible is shown by the company law of Delaware.

3. DRAFT BILL TO AMEND DUTCH PRIVATE COMPANY LAW

3.1 Introduction

A majority of the recommendations made in our report were adopted in the draft Bill, which was published in November 2006. And although the final Bill shows that some amendments have been made, the foundations of the new system, which were laid down in the draft Bill, remain unaltered.

The proposed system of creditor protection no longer relies on a certain amount of capital that may not be distributed to shareholders. Instead, it is based on a system in which the lawfulness of distributions will be judged by having regard to the solvency of the company.[72]

The concept of par value shares is retained in the draft Bill. The option to introduce no par value shares is discussed in a separate paper, which takes the form of an Appendix to the draft Bill.[73] In this article we will not discuss the

[72] Explanatory Memorandum, p. 6.

[73] Available at: <http://www.justitie.nl/images/NOTITIE%20AANDELEN%20ZONDER%20NOMINALE%20WAARDE_tcm34-2574.pdf>.

content of the Appendix for the reason that it is apparent from the report of the Company Law Commission, which preceded the final Bill that was sent to Parliament, that there would be too many complications involved in introducing no par value shares. A great number of provisions in Book 2 of the Dutch Civil Code rely on the concept of par value shares as a criterion to determine if and to what extent shareholders may benefit from certain rights. All these provisions would have to be amended in the case of introduction of no par value shares. Moreover, several provisions of tax law would also need to be revised. This means that the introduction of no par value shares would slow down the project to make Dutch private company law more flexible. We agree that this is not desirable.

3.2 **Raising capital**

Very little of the complex set of rules with respect to the raising of capital is left intact in the draft Bill. First of all, the minimum capital is abolished, as well as the sanction attached to it, namely the joint and several liability of directors for legal acts of the company that are committed before at least the minimum capital has been raised (see Art. 2:180 BW). Secondly, the draft Bill does away with most of the rules that aim to ensure that capital is actually raised. The following reason for this radical change is given in the Explanatory Memorandum:

> As a consequence of the abolition of the minimum capital, it is possible to form a BV with a very small capital, for example two shares with a par value of 0.01 eurocent each. This is an important fact, because in the proposed system the consideration for shares will probably lose its function as a safeguard for creditors. For this reason the draft Bill does not contain extensive formalities with respect to the raising of capital.[74]

The provisions requiring a bank statement in the case of a consideration in cash and a mandatory valuation by an independent expert of a consideration in kind are repealed. However, the draft Bill retains the requirement that the incorporators or, if consideration in kind is agreed upon after incorporation, the directors provide a description of consideration in kind. Currently, this description, which must contain the value of the assets that are contributed and the valuation methods used, is not made public. The draft Bill changes this by requiring that the description of the incorporators has to be attached to the deed of incorporation. The legislature has decided not to introduce a specific statutory provision that creates a liability for incorporators and directors who knowingly overvalue contributions

[74] Explanatory Memorandum, p. 6.

in kind.[75] Instead, the draft Bill provides that a shareholder who turns out to have contributed an asset that is worth less than the amount that he has undertaken to contribute must without undue delay pay the difference in cash. In the wake of the abolition of the mandatory valuation of considerations in kind, the so-called *Nachgründung* provision[76] is also repealed. Another liberalisation of the rules on considerations in kind is the abolition of the provision that prohibits the contribution of an undertaking to perform work or provide services.

Finally, it should be noted that the draft Bill retains the requirement of the payment of at least 25 per cent of the nominal value of the acquired shares.[77]

3.3 Distributions to shareholders

General remark. An important feature of the draft provisions on distributions is that different rules will no longer apply to transactions that have in common that they result in distributions to shareholders. Distributions of dividends and payments made as a result of repurchases of shares or capital reductions will all be subject to both a balance sheet test and a liquidity test, which must be executed by the board of directors. The existing bright-line distribution rules that lead to the nullity of transactions in the case of non-compliance are replaced with a duty of care for directors to which the *ex post* sanction of liability is attached.[78]

Payment of dividends. Currently, Dutch law is not clear about the responsibility of the board for payments of dividends, because in principle it is the GMS that has the power to decide on such payments. By assigning responsibility to the board, a gap in the Dutch system is filled. The draft legislation attaches the sanction of liability to the responsibility of directors for checking the lawfulness of distributions. Every director who knows, at the time of the distribution, that the company would fail the balance sheet test or the liquidity test is jointly and severally liable towards the company for the amount of the distribution. This liability also applies to shadow directors. Our recommendation to make distributions subject to a statement by the board concerning the company's solvency has not been adopted in the draft Bill. According to the legislature, the burden for companies created by an obligation to publish such a statement is too heavy.[79]

[75] This was suggested in the report of the Expert Group headed by De Kluiver, op. cit. n. 5. For an overview of the contents of the report, see H.J. de Kluiver, 'Towards a Simpler and More Flexible Law of Private Companies – A New Approach and the Dutch Experience', 3 *ECFR* (2006) pp. 45-68.

[76] See section 2.1 of this article.

[77] However, the legislature asks whether there are grounds to abolish this requirement. See draft Bill, footnote 1.

[78] Explanatory Memorandum, p. 6. The sanction of nullity will not be abolished completely. For example, the repurchase by the BV of all of its own shares remains invalid.

[79] Explanatory Memorandum, pp. 28-29.

The draft Bill requires the board of directors to subject proposed distributions to both a balance sheet test and a liquidity test. The balance sheet test proposed in the draft Bill differs from the simple balance sheet test we recommended in our report: the par value of the capital may be distributed but it remains prohibited to distribute those reserves that must be maintained because this is prescribed by statutory provisions or by the articles of association. As to the liquidity test, this is defined by the legislature in the following way: the directors must check whether, after the distribution has been made, the company will continue to be able to pay its debts as they fall due. This means that directors must not only take into account debts that are payable at the time of the distribution but also debts arising from current agreements of which they know that they will become payable in the near future.[80]

In the case of a distribution that has taken place within one year prior to the opening of bankruptcy proceedings, it is presumed that the board knew that the company failed the liquidity test. Directors can escape from being held liable by proving that they cannot be blamed for the unlawful distribution and that they were not negligent in taking measures to prevent the consequences of such a distribution.

The draft Bill introduces an obligation for shareholders to pay back any distribution that was made within one year prior to the opening of bankruptcy proceedings, regardless of whether the distribution was received in good faith. According to the legislature, the close involvement of shareholders in the decision-making process of a private company justifies legislative measures in order to prevent them from benefiting from distributions in cases where directors are punished with liability.[81]

Repurchase of shares. With respect to the responsibility and liability of directors, the rules applicable to payments of dividends will also apply to repurchases of shares. Where the position of the shareholder who received the distribution is concerned, however, there is a notable difference: the pay-back obligation in the case of a distribution made within one year prior to the opening of bankruptcy proceedings does not apply to share repurchases. The reason stated in the Explanatory Memorandum for this different treatment of share repurchases is that the mandatory resolution of the GMS in the case of share repurchases will be abolished. This means that there will be no (mandatory) involvement of shareholders in the decision-making process and that they should therefore not be subject to an obligation to pay back what they received.[82] In line with our recommendations,

[80] Explanatory Memorandum, pp. 27-28.
[81] Explanatory Memorandum, p. 30.
[82] Explanatory Memorandum, p. 21.

the draft Bill also repeals the restriction that BVs may only repurchase shares up to a maximum of 50 per cent of the issued capital.

Financial assistance. The provisions on financial assistance are repealed entirely. The Explanatory Memorandum states two reasons for this radical change. The first reason is that the provisions are very complex and give rise to a considerable amount of legal uncertainty. The second, more principled argument is that specific statutory provisions regulating financial assistance are not necessary for the protection of creditors or shareholders. The Explanatory Memorandum refers to the relevant conclusions drawn in our report.

Reduction of capital. In line with our recommendations, the creditors' right to object to a capital reduction will be abolished. Payments made to shareholders resulting from a capital reduction will be subject to the regime applicable to payments of dividends.

3.4 Reactions to the consultation document

3.4.1 *Raising capital*

The reactions to the proposed changes to the rules with respect to the raising of capital were generally positive.[83] The proposed abolition of the minimum capital, the bank statement in the case of considerations in cash and the expert valuation of considerations in kind can be characterised as uncontroversial. However, objections were raised against the proposed obligation to publish the description of contributions in kind. Opponents of this obligation pointed out that, when the current rules on contributions in kind were introduced, the legislature decided against the publication of the description because it contained sensitive information. It is indeed not clear why this reason should no longer be valid.

In view of the fact that the abolition of the expert valuation generally met with approval, it is not surprising that the abolition of the *Nachgründung* provisions – which aim to prevent the evasion of the formalities involved with contributions in kind – is equally uncontroversial. However, the abolition of these provisions does mean that it will become very easy to evade the controversial obligation to publish a description of contributions in kind. This can be done by opting for a contribution in cash when the company is formed and subsequently selling the assets that the shareholder originally wished to contribute to the company. It was noted that, in view of this fact (and taking into account the opposition against the

[83] The reactions to the consultation document can be found on the website of the Ministry of Justice, at: <http://www.justitie.nl/onderwerpen/wetgeving/bv%5Frecht/Consultatie%5Fderde%5Ftranche/>.

publication of sensitive information), the legislature should reconsider introducing an obligation to publish a description of contributions in kind.[84]

There was also some controversy with respect to the obligation of a shareholder to pay the difference in cash if he has contributed an asset that is worth less than the amount that he had undertaken to contribute. In the case of the sale of the shares by the shareholder who has contributed too little, this obligation may transfer to the new owner. This was seen as problematic.

The most controversial part of the proposed amendments to the rules on the raising of capital is the abolition of the prohibition on the contribution of an undertaking to perform work or provide services. This proposal met with considerable opposition. We list the most important objections:

- problems will arise when the work is not performed or the services are not provided;
- the economic valuation of an undertaking to perform work or provide services is not easy;
- an undertaking to perform work or provide services does not satisfy the definition of 'asset' applied by the International Accounting Standards Board (IASB): 'an asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow';[85] and last but not least
- in practice there is no need for the possibility to contribute an undertaking to perform work or provide services.

The answers to the question whether the requirement of the payment of at least 25 per cent of the nominal value of the acquired shares should be retained vary. Where some were in favour of the abolition of this requirement, others were in favour of abolishing the possibility of deferred payment.

3.4.2 *Distributions to shareholders*

As such, the introduction of the responsibility of the board for making distributions of dividends does not seem to be controversial. Many doubts were raised, however, with regard to the execution of the balance sheet and liquidity test and

[84] See M.L. Lennarts, 'Enige kanttekeningen bij de voorstellen tot wijziging van het kapitaalbeschermingsrecht bij de BV' [Some comments on the proposals to reform the capital protection law applicable to the BV], 72 *Onderneming & Financiering* (2006) p. 36.

[85] See P. van der Zanden, 'Het nieuwe kapitaalbeschermingsrecht vanuit accountancy perspectief' [The new capital protection law from an auditor's perspective], 6676 *WPNR* (2006) pp. 582-583.

the liability of board members attached to it. We briefly list the most important issues:[86]

1. Several respondents believed that the legislature should give more guidance on the proposed liquidity test. There are worries with respect to foreseeability. It was therefore suggested by some that the liquidity test should be restricted to the next twelve months.[87] Clarification also seems necessary with respect to the question whether contingent and prospective liabilities must be taken into account. It is also unclear whether prospective and contingent assets may be included in the test.[88]
2. The consultation also shows that the exact timing of the liquidity test is not clear in the case of a payment of dividends.[89] Given the fact that the GMS has the power to adopt a resolution on the distribution of dividends, it seems practical for the board to first make its assessment, which is then passed on to the GMS. If the latter votes for a distribution, it is consequently the board that must execute the resolution. Time may pass between the initial assessment by the board and the moment when the distribution is actually made. Must the board, in such a case, apply the test again when the distribution is made? This is implied by the draft provisions that attach liability to knowledge of illiquidity *at the time of the distribution*. We suggest that the law should provide that the board's approval remains valid for a maximum period of four months.
3. The most important remarks of respondents with respect to the envisaged director liability aim at limiting the risk that this liability will materialise. Some respondents took the view that the legislature should make it clear that directors can only be held liable in the case of a 'serious reproach'. Other

[86] For a more elaborate assessment of the reactions to the consultation document, the reader is referred to L. Lennarts, 'Directors' and Shareholders' Liability as a Means of Protecting Creditors of the BV', 8 *EBOR* (2007) pp. 138-144.

[87] De Kluiver proposes that directors should only be required to make a detailed assessment for the next twelve months. Events taking place after that period should be taken into account, however, if it is evident to the average capable director that these events threaten the solvency of the company. See H.J. de Kluiver, 'Vermogensbescherming bij de BV: modernisering in internationaal perspectief' [Capital maintenance in the BV: modernisation from an international perspective], 137 *WPNR* (2006) pp. 578-579. This approach appeals more to us than simply limiting the liquidity test to the next twelve months, as this seems rather arbitrary.

[88] See Rickford, loc. cit. n. 64, at p. 979.

[89] What is said here about the timing problem also applies to distributions made upon a decision to reduce capital, because a resolution of the GMS is also necessary in the case of a capital reduction. The timing problem will be less severe in the case of repurchases of shares, because it is proposed to give the exclusive power to decide upon share repurchases to the board, instead of to the GMS. In this case, there is only a timing problem if a long period lapses between the date of the board's resolution and the date the repurchase is executed. It should be noted, however, that a provision requiring the approval of the shareholders' meeting for share repurchases may be adopted in the articles of association.

> respondents stressed that directors should be able to rely on expert advice, except – of course – when they have committed fraud.
>
> Worries have further been expressed with respect to the one-year period during which the threat of liability will hang over the directors' heads like a sword of Damocles. A means of mitigating the liability risks for directors, which was suggested by most respondents, is to limit the extent of the liability to the amount of the debts that cannot be paid because the distribution was made. It was widely expressed that it is unfair to automatically make directors liable for the full amount of the distribution.

The consultation shows that opinions were divided with regard to the introduction of the automatic pay-back obligation for shareholders who have received a distribution in the suspect period. Some argued that this obligation is justified, because it is the shareholder who determines the dividend policy and who benefits from the distribution. Others, however, considered it unjust to confront an unwitting shareholder with a straightforward duty to return the distribution. Like directors, shareholders should be able to rebut a presumption of knowledge. It has also been pointed out that the introduction of an automatic pay-back obligation for shareholders of a BV might cause a shift to the Dutch NV[90] or to a foreign stock company.[91] Furthermore, it has been noted that a strict pay-back obligation only makes sense if it also applies in the case of hidden distributions. Otherwise, there is a risk that the hidden distribution will become a loophole in the new law.[92]

The proposed pay-back obligation does not apply in the case of a repurchase of shares that took place within one year prior to bankruptcy of the company. This exception was criticised by several respondents, who point out that the proposed abolition of the mandatory approval of the GMS does not justify this exception, because a shareholder whose shares are repurchased is *ipso facto* involved in the repurchase. The more lenient treatment of shareholders whose shares have been repurchased should also be reconsidered, because it may lead to strategic behaviour. If share repurchases are regulated less strictly than the other forms of distributions, shareholders will have an incentive to opt for a share repurchase. There is a risk that the share repurchase will become a loophole as far as the automatic pay-back obligation is concerned.[93]

[90] Under the regime of the NV, which will continue to apply, shareholders only have to pay back distributions that they received in bad faith.

[91] See De Kluiver, loc. cit. n. 87, at p. 578, who points to the competitive disadvantage created by the automatic pay-back obligation, because laws applicable to foreign private companies (he mentions German and English law) protect shareholders who received distributions in good faith.

[92] See Lennarts, loc. cit. n. 86, at p. 141.

[93] See Lennarts, loc. cit. n. 86, at p. 141.

Finally, an issue that needs clarification according to the consultation is the relationship between the liability of directors and the pay-back obligation of shareholders who have received an unlawful distribution.

3.5 **The final Bill**

The legislature has paid heed to many of the points of criticism raised in the consultation. Several draft provisions were removed or amended. With respect to the raising of capital, the following draft provisions were removed:

- the requirement that at least 25 per cent of the nominal value of the acquired shares must be paid up immediately;
- the obligation to publish a description of contributions in kind;
- the proposed obligation for a shareholder to pay the difference in cash if he has contributed an asset that is worth less than the amount which he had undertaken to contribute; and
- the abolition of the prohibition on contributing an undertaking to perform work or provide services.[94]

With respect to distributions to shareholders, the legislature has chosen to subject these distributions only to a liquidity test and to delete the balance sheet test. This means that directors will not have to check whether the company's assets exceed its liabilities before making distributions to shareholders. However, the prohibition on distributing reserves that must be maintained pursuant to the statutory provisions or the articles of association will be retained. This prohibition is only of relative importance. Statutory reserves can be transformed into capital that can be distributed. Reserves that must be maintained pursuant to the articles of association can be made freely distributable by an amendment of the articles of association.

The legislature has paid heed to the concerns expressed with respect to the liquidity test by giving more guidance on the execution of the test in the Explanatory Memorandum: not only liquidity is of importance, but other financial standards, like the solvency and the profitability of the company, should be taken into account as well. To reflect the fact that not only liquidity should be taken into account, the relevant provisions of the Bill no longer refer to a 'liquidity test' but to a 'distribution test'. According to the Explanatory Memorandum, the horizon of the distribution test can generally be restricted to the next twelve months. This may be different in specific cases, for example when the directors know that in eighteen months' time the company must pay a large amount due to tax debts.

[94] This provision was repealed mainly for tax law reasons. See Explanatory Memorandum, p. 35.

The issue of the exact timing of the distribution test, which arose in the consultation, has not been resolved by the legislature. The final Bill still attaches liability to knowledge of illiquidity *at the time of the distribution*, which leaves the question whether directors must apply the test again if time lapses between the initial test and the actual distribution.

The most important changes are those made to the provisions concerning directors' and shareholders' liability in the case of unlawful distributions. First, the Bill no longer contains a refutable presumption that the board knew or should have known that the company failed the liquidity test in the case of a distribution within one year prior to the opening of bankruptcy proceedings. Second, shareholders who received dividends in good faith will be protected. They will only have to repay the distributions made to them within the period of one year prior to the opening of bankruptcy proceedings if they knew or should have known that the company had failed the liquidity test. The Explanatory Memorandum does not clarify what the situation is when the distribution was made before the one-year period. We are of the opinion that in such cases the judgment in the *Nimox* case[95] will still be relevant. If the shareholder voted for the distribution when he could reasonably expect this to lead to a situation in which the claims of the company's creditors could no longer be met, the shareholder has acted unlawfully in the sense of Article 6:162 BW (tort law) and can be held liable for the damage suffered by creditors as a consequence of the distribution. We therefore wonder why the one-year period has been inserted.

An amendment that can only be applauded is the removal of the different treatment of shareholders who have sold their shares to the company. It is fortunate that the legislature has come to see that there is no justification for the milder treatment of the shareholder who has received a distribution as a consequence of a share repurchase.

The draft Bill contained a liability for the *amount* of the distribution. Article 2:216, paragraph 3 BW was amended to the effect that, with respect to the extent of the liability, it refers not only to the amount but also to the *value* of the distribution. According to the Explanatory Memorandum, the aim of this amendment is to make clear that distributions in kind also fall within the scope of Article 2:216, paragraph 3. There is no further explanation, which leaves the question whether this small amendment means that directors may be held liable on the basis of Article 2:216 in the case of a hidden distribution in the form, for example, of a transaction at an undervalue with a shareholder.

Where the draft Bill was not clear with respect to the relationship between the liability of directors and the pay-back obligation of shareholders, this has been clarified in the final Bill. The proposed Article 2:216 now provides that the

[95] HR 8 November 1991, *NJ* 1992 No. 174 (*Nimox*). See section 2.1 of this article for the meaning of this judgment.

directors who have been made liable by the company can have recourse against any shareholders who are under an obligation to pay back distributions to the company.

4. Amendment of the Second Company Law Directive

4.1 **Introduction**

The Dutch legislature has the power to amend the national law on private companies in an independent way. Large parts of this law have not been harmonised by EC directives. This is different in respect to the law on public companies. The Dutch legislature has to remain within the boundaries specified in the Second Company Law Directive when amending capital maintenance rules for public companies, which leaves very little room for manoeuvre. Because of the recent amendment of the Second Company Law Directive by Directive 2006/68/EC, the room for manoeuvre will become a little bit larger.

4.2 **History of Directive 2006/68/EC**

The first move towards amending the Second Company Law Directive was the report of the SLIM[96] working group, published in the autumn of 1999.[97] The assignment of the SLIM working group was to report on possible ways of simplification. This limitation meant that proposals for a fundamental review of public company capital protection law were not possible. The SLIM report therefore only contained proposals for the simplification of the Second Company Law Directive.

A further step was made by the report of the High Level Group of Company Law Experts of 4 November 2002, entitled: 'A Modern Regulatory Framework for Company Law in Europe'.[98] Regarding capital protection law, the High Level Group recommended that the Second Company Law Directive should be simplified in the near future on the basis of the recommendations of the SLIM working group, with some additions (SLIM Plus). An alternative regime for creditor and shareholder protection should then be presented based on the abolition of the concept of issued capital. According to the High Level Group, an important

[96] The abbreviation SLIM stands for Simpler Legislation for the Internal Market.

[97] See E.E.G. Gepken-Jager and J.N. Schutte-Veenstra, 'Voorstellen SLIM-werkgroep ter vereenvoudiging van eerste en tweede EG-richtlijn' [Proposals of the SLIM working group for simplifying the First and Second Company Law Directives], *Ondernemingsrecht* (1999) pp. 423-425.

[98] The text of the final report of the High Level Group can be found on the European Union's website, at: <http://ec.europa.eu/internal_market/company/modern/index_en.htm>.

element of this alternative regime should be the linking of distributions to shareholders to a 'solvency test'.

Partly in response to the report of the High Level Group, the Commission published a 'Company Law Action Plan' on 21 May 2003, indicating that the European regulatory framework for company law and corporate governance should be updated and improved.[99] In this context, the Commission announced that it would put forward a proposal in the short term (2003-2005) for simplifying the provisions of the Second Company Law Directive. In keeping with its announcement, the Commission published a proposal for a directive to amend the Second Company Law Directive on 29 October 2004.[100] On 6 September 2006, the European Parliament and the Council adopted Directive 2006/68/EC.[101] Member States must implement the provisions of this Directive into their national laws by 15 April 2008. However, the importance of the amendments made to the Second Company Law Directive is relatively small. The amendments leave the pillars of the current capital regime in place. Amendments have only been made in certain parts.

4.3 Amendments made by Directive 2006/68/EC

In this section we will discuss the most important amendments made by Directive 2006/68/EC.[102] It concerns the simplification of the rules in respect of the required independent expert's report in the case of a contribution in kind, the relaxation of the rules in respect of an acquisition of the company's own shares and the relaxation of the prohibition on public companies providing financial assistance for the acquisition of their shares by third parties.

First, Member States are authorised to eliminate the requirement for an expert's valuation report in the case of a contribution in kind where there already exists a clear point of reference for valuation. Three exceptions are made to the rule that there has to be an expert valuation. The first exception involves the contribution of transferable securities and money-market instruments on the condition that these securities or instruments are duly valued at a market price

[99] In full: Communication from the Commission to the Council and the European Parliament – Modernising Company Law and Enhancing Corporate Governance in the European Union – A Plan to Move Forward, COM (2003) 284 final, 21 May 2003, available at: <http://ec.europa.eu/internal_market/company/modern/index_en.htm>.

[100] The text of the amendment proposal is available at: <http://ec.europa.eu/internal_market/company/capital/index_en.htm>.

[101] Directive 2006/68/EC of the European Parliament and of the Council of 6 September 2006 amending Council Directive 77/91/EEC as regards the formation of public limited liability companies and the maintenance and alteration of their capital, *OJ* 2006 L 264/32.

[102] See further J.N. Schutte-Veenstra, 'Europese vereenvoudiging van het kapitaalbeschermingsregime voor de NV' [Simplification of the capital protection regime for the public company], 17 *Ondernemingsrecht* (2007) pp. 606-613.

based on a weighted average price calculated within a given time range before the contribution takes place. An expert valuation is also not required in cases where the asset to be contributed has already been the subject of an independent expert valuation. Finally, an expert valuation is not required in cases where assets are contributed whose fair value is derived from the audited accounts of the previous financial year, provided that these accounts have been established in accordance with the European Community's latest accounting and auditing provisions.[103]

However, the board is required to take due account of significant changes in the value of the asset at issue through revaluation. In this respect, an independent expert's valuation report is required. In case the board of directors does not revaluate the asset of its own accord, minority shareholders have the possibility to request an additional valuation by an independent expert.

In order to compensate for the above-described exceptions to the requirement of an expert's valuation report, the board of directors is obliged to publish a declaration with information as to the asset contributed and its valuation within one month of the effective date of the asset contribution.

Furthermore, the rules in respect of the acquisition of the company's own shares have been relaxed. In the original Directive, the maximum length of the period of authorisation granted by the GMS for acquisitions of the company's own shares was set at eighteen months. According to Directive 2006/68/EC, this maximum length shall be determined by national law without exceeding five years. Currently, a public company may acquire its own shares on the condition that the shares acquired must not amount to more than 10 per cent of the issued capital. This 10 per cent limit becomes optional for Member States. An acquisition of a company's own shares is permitted up to the limit of distributable reserves, even if the latter amounts to more than 10 per cent of the issued capital.

Last but not least, the prohibition on companies providing financial assistance for the acquisition of their shares by third parties has been relaxed. Member States are given the option to enable public companies to provide financial assistance for the acquisition of their shares by a third party up to the limit of distributable reserves, having regard to certain specific requirements. One of the requirements is that the transaction shall take place under the responsibility of the board of directors at fair market conditions. Furthermore, the GMS has to approve the transaction by means of a resolution adopted by a two-thirds voting majority. This resolution is based on a written report of the board of directors about the reasons for the transaction, the interest of the company therein, the conditions of the transaction, the risks for the liquidity and solvency of the company and the price at which the third party is to acquire the shares.

[103] The accounts must have been subjected to an audit in accordance with Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, *OJ* 2006 L 157/87.

4.4 Dutch implementation of Directive 2006/68/EC

In May 2007, a Bill to implement Directive 2006/68/EC into the Dutch law on public companies was approved by the Dutch Council of Ministers and sent to the Council of State. The content of the Bill is still confidential. The impression created by a press release issued by the Ministry of Justice is that the Dutch legislature will make use of all the possibilities Directive 2006/68/EC offers in order to simplify the capital protection requirements for the NV.[104] The greatest advantage for legal practice will probably be the enlarged possibility to repurchase shares.

4.5 Future perspective

Directive 2006/68/EC does not change the pillars of the Second Company Law Directive. In its Company Law Action Plan, the Commission let it be known that the introduction of an alternative regime for creditor protection is to be addressed in the future. A feasibility study must first be carried out. See also Recital (2) of Directive 2006/68/EC: '… the need to proceed without delay to a general examination of the feasibility of alternatives to the capital maintenance regime which would adequately protect the interests of creditors and shareholders of a public limited liability company.' This feasibility study shall be carried out by KPMG Germany. Once the results of the study are published, further actions of the Commission are to be expected in the field of capital maintenance.

5. Conclusion

There is every indication that far-reaching changes will be made to the capital protection rules applicable to the Dutch BV. The concept of capital will no longer play a role in the protection of creditors. This means that rules with respect to the raising of capital can be abolished. In the future, the creditors of a BV will be protected by rules that aim to ensure that the BV does not make distributions to shareholders when this would be imprudent. The payment of dividends and payments made as a result of share repurchases and reductions of capital will be subject to a liquidity and solvency test known as the distribution test. It follows from existing case law[105] that the liquidity of the company must be taken into account when making payments to shareholders. However, there will be a greater

[104] See: <http://www.justitie.nl/actueel/persberichten/archief-2007/meer-ruimte-voor-inkoop-van-eigen-aandelen.aspx>.

[105] See HR 8 November 1991, *NJ* 1992 No. 174 (*Nimox*); and HR 6 February 2006, *JOR* 2004/67 (*Reinders*).

emphasis on the liquidity and the solvency of the BV when making distributions, because the distribution test will be codified and because the law will expressly provide that directors bear responsibility for the execution of this test.

The proposed changes to the capital protection rules may seem radical to the outsider. It should be kept in mind, however, that the BV was introduced quite recently, in 1971, for a rather pragmatic reason. It was considered necessary to create a stock company that, unlike the NV, would be subject to the European Company Law Directives on annual accounts.[106] At that time, a fundamental discussion of the function of the BV in relation to the NV did not take place. From the start, the law applicable to the BV was almost an exact copy of the law applicable to the NV. In view of this fact, it is hardly surprising that, during the 1980s, when the Second Company Law Directive needed to be implemented, the Dutch legislature chose to amend both the capital protection rules applicable to the NV and those applicable to the BV, although it was under no obligation to do so in the latter case. The fundamental debate about the way in which company law should protect creditors of a BV is finally taking place twenty years later. This brief sketch of the genesis of the BV will perhaps make it easier for the outsider to understand the apparently far-reaching proposals to amend the capital protection rules applicable to the BV.

If the proposed changes are implemented, the creditor protection rules applicable to the BV will differ considerably from those applicable to the NV. After the publication of the draft Bill, it was suggested that the rather strict treatment of directors and shareholders in the case of distributions made within one year prior to the opening of insolvency proceedings could lead to an increased popularity of the NV.[107] Because it is now clear that less severe rules have been adopted in the final Bill, there seems to be no reason to fear that the BV will have to compete with the NV. Time will tell whether the fundamental reform of the law applicable to the Dutch BV leaves it well equipped to contend with foreign competition.

[106] De Kluiver, loc. cit. n. 75, at pp. 48-49.

[107] See B. Bier, 'Het verleden, heden en de toekomst van de kapitaalbescherming' [The past, present and future of capital protection], in *De vereenvoudigde BV, preadviezen voor de Vereeniging handelsrecht* [The simplified BV, report for the Commercial Law Association] (Deventer, Kluwer 2006) p. 254. See also the report of the discussion that took place at the meeting of the Commercial Law Association on 20 June 2006: 'Verslag van de vergadering van de Vereeniging handelsrecht', 20 juni 2006, in *De vereenvoudigde BV*, ibid., at pp. 55-57.

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