

# Hedge Fund Activism in the Netherlands

- An empirical research of the magnitude of hedge fund activism -

Master Thesis

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Author: B.R.M. Swaen 741667

Master Financial Management, Finance Department at the FEB

Supervisor: Dr. P. Sengmüller

Second Reader: Dr. M.M.R. van Bremen

## Summary

This thesis investigates the magnitude of hedge fund activism in the Netherlands by doing a study using public information. Hedge funds are not registered in any regulated database and therefore I've constructed my own database.

As a starting point I used the public database from the Authority of Financial Markets. This database consists of all notifications of substantial amounts shareholders possess in public companies in the Netherlands. By working through this database I was able to find 28 hedge funds with 168 filings of substantial amounts in public companies between 2000 and March 2010. After doing additional news searches I managed to create a dataset of 38 hedge funds and 65 cases of hedge funds having a share in a company.

Since 2004 there is an increase in the number of hedge fund cases, and after 2008 this suddenly diminishes. This effect is most probably a result from the financial crisis. Of the 65 cases I was able to find, 45 hedge fund cases were actively involved in addressing the targeted companies. These 45 cases were having a total of 83 motives/objectives for activism. 38% of these motives were about targeting business strategy and none of these motives concerned the remuneration policy of the management.

Of all the objectives the hedge funds pursue, 40% is actually achieved and 29% partially succeeded. These outcomes are very much alike with results from US studies addressing hedge fund activism in the US. Almost 50% of the tactics hedge funds use, in order to achieve their objectives, are related to deliberately going public to put pressure on the management. And 23% of the tactics involves hedge funds that appeal at the OndernemingsKamer (OK). The average holding period of hedge funds in public companies is 531 days, the median holding period is 319 days.

Hedge funds often appeal at the OK in order to achieve their objectives. The outcomes of various cases show that the OK first always tries to keep the dialogue going between the company and the activists. If there are severe problems the OK often takes immediate provisional measures. These provisional measures usually contain the appointment of independent supervisory members. In sum, hedge funds have a pretty good change of defending its shareholders rights and often partial success is achieved when going to the OK.

As I expected there is no market response to the filing at the AFM of a hedge fund having a substantial amount in a company. The event study did not report any abnormal returns. When it becomes clear in the media that a hedge fund has become active and their objectives are now also clear there is a market response. By doing an event study it became clear that there is an abnormal return of 6.36% during the event window surrounding the activism. So the market perceives hedge fund activism as a positive sign.

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## 1. Introduction

Shareholder activism is becoming more and more a hot topic in the Netherlands. A shareholder activist is an investor who buys a large stake in a publicly held corporation, with the intention to bring change and thereby realize a profit on the investment (Pound (1992)). There are numerous kinds of entrepreneurial activists, but for this thesis hedge funds are of particular interest.

Due to the fact that share ownership of listed companies in the Netherlands is relatively dispersed, and that as many as 70% of the shareholders are foreign shareholders, Dutch companies are particularly vulnerable to shareholder activism by hedge funds in comparison with other continental countries from Europe (Risk Metrics Group (2009)).

There are many examples of shareholder activism by hedge funds that were extensively covered in the media. A few examples are:

- Hermes, a large Océ shareholder, openly challenged the takeover bid by Canon of Océ. It stated that the takeover bid was far too low and thus significantly undervalued the Dutch company's shares.
- Royal Dutch Shell combined its British and Dutch arms in 2004, and so ending a structure that lasted for more than a century, pressured by activist investor Knight Vinke.
- Stork and Ahold both came under pressure from hedge funds Centauris Capital and Paulsen & Co. They pressured with a break-up of the company if certain strategic actions weren't put through.
- ASMI was in 2006 target of fund manager Mellon HBV (changed name into Fursa), who was pushing for a split of the company.

Influential people and even the Dutch government publicly question the instruments hedge funds use in order to achieve their objective. The activists are put down as a short term, high risk and certainly negative part of the globalization. The financial crisis has strengthened this debate and many politicians now argue that shareholders rights should be decreased.

Although there is a lot of discussion about hedge funds and their activism in the Netherlands, literature about hedge fund activism is still in its infancy. Large part of actual data remains vague and the only empirical work on hedge fund activism in the Netherlands that I could find was the research by De Jong, Roosenboom, Verbeek and Verwijmeren (2007).

Therefore I'm investigating the 'magnitude' of shareholder activism of the last decade using data from the Authority of Financial Markets (AFM), news articles and company's press reports. I will be looking at the motives and tactics of hedge funds in the Netherlands of the past decade.

## Research Question

What is the magnitude of hedge fund activism in the Netherlands the past ten years?

- What is hedge fund activism?
- What are the rights of shareholders in the Dutch corporate governance system and in what way differ they from the US and UK?
- How big is hedge fund activism in the Netherlands?
- Which objectives do hedge funds try to achieve, and are they successful?
- Which tactics do they employ?
- How does the market react to the announcement of activism? What is the market's reaction to the filing of a hedge fund?

The rest of this thesis proceeds as follows. Chapter 2 starts with forming a definition of hedge funds and gives an explanation of the definition 'shareholder activism'. I will continue with a review of existing literature on hedge fund activism. The second part consists of a brief description of the corporate governance climate affecting shareholders in the Netherlands during the last decade. It ends with the comparison of the Dutch governance system with that of the US and UK, with respect to shareholders rights. Chapter 3 is the data collection process as well as an overview of the data and its implications. Chapter 4 and 5 are respectively the conclusion and the discussion. The last chapter contains the references.

## 2. Literature Review

### What is a hedge fund?

Hedge funds are not regulated so it's difficult to come to a precise definition. While there are numerous authors that tried to come up with a definition that captures all characteristics of hedge funds none of these are chosen in the literature as 'the definition'. When the Securities and Exchange Commission (SEC) held a discussion on hedge funds in 2003 David A. Vaughan cited 14 different definitions from government and industry publications (SEC (2003))!

Therefore it's better to rely on a short summary of the characteristics in order to define a hedge fund. I believe the summary given by Partnoy and Thomas (2007) is a very precise and accurate one.

In their view hedge funds generally have four characteristics:

1. They are pooled, privately organized investment vehicles.
2. They are administered by professional investment managers.
3. They are not widely available to the public.
4. They operate outside of securities regulation and registration requirements (so they can take short positions without restrictions).

Private equity and venture capital funds also have, for the main part, the same characteristics. But those funds are different from hedge funds because they focus only on one particular private market. Private equity focuses normally on targeting going private transactions by acquiring a larger percentage of ownership than hedge funds. Venture capital normally invests in companies with the prospect of selling it later when the company goes public. They therefore invest at much earlier stages than hedge funds (Brav, Jiang, Partnoy and Thomas (2008)).

Mutual funds from the US are far more regulated than hedge funds because they have to comply with the Investment Company Act of 1940. First they are constrained by tax laws because they take concentrated positions in companies. Second they are subject to restrictions on shorting, borrowing and investing and third the SEC regulates the types of fees mutual funds may charge.

Sometimes the differences between private equity funds, venture capital and hedge funds are less clear than stated above. Therefore I will further elaborate on the characteristics of hedge funds.

Hedge funds often operate outside of securities regulation and registration requirements because they avoid the Investment Company Act of 1940. They do this by making use of the exemptions written in the law. If a fund has no more than 100 investors and the investors are each persons who invest at least \$5 million, the fund isn't obliged to the Company Act and registration rules of the SEC. As a consequence a hedge fund never sells to the main public, and always has investors with enough net worth (Brav et al. (2008)).

A remark is that only hedge funds from the US or from countries like the Cayman Islands, Bermuda and Bahamas are unregulated. Hedge funds from the Netherlands and the UK are under the same regulations as traditional investment funds. Often the hedge funds are sited in tax friendly countries and have only the headquarters in the US or UK. Because of the fact that hedge funds are not established in European countries it is very hard for the European Union to regulate them. And what about those hedge funds from the UK? Only the managers of these hedge funds operate from the UK, the hedge funds themselves are sited in other countries. The UK government is trying to regulate the managers but cannot regulate the hedge fund itself. When I collect my data I will also look at the countries from which the hedge funds work and have their origin.

The average hedge fund is a partnership entity managed by a general manager. The investors are limited partners, and have little to nothing to say in the hedge fund's business (Brav et al. (2008)). Hedge funds are often considered as very active market participants that use leverage aggressively and take both long and short positions (Partnoy and Thomas (2007)). Because hedge funds do not fall under the act of 1940 they can take much larger relative positions, they are permitted to trade on margin and to engage in derivatives trading. Therefore hedge funds are far more flexible in trading than other institutions (Brav et al. (2008)). Also hedge funds can use leverage and financial derivatives to acquire very large positions in companies without the need for a lot of cash.

In most literature from the past decade hedge funds are also always described as pursuing short-term strategies. Brav et al. (2008) argue that hedge fund activists are not short-term in focus, as some critics have claimed. They found that the median holding period of hedge funds acquiring a stake in a firm is about one year. I will come back to this later when I discuss the results from my data.

The funds charges high fees for their operations. Usually around 2% of the assets under management and 20% of the fund's annual return. Because managers are compensated on absolute terms they have a strong incentive to be more aggressive in their strategies than managers at other funds (Partnoy and Thomas (2007)). Managers from other funds can also be awarded performance compensation but they capture a much smaller percentage of any



returns due to the restricting of performance fees under the Investment Company Act of 1940. So their incentives are much smaller.

Also hedge fund managers suffer from fewer conflicts of interest than managers of other institutions. The example giving by Brav et al. (2008) is that of a pension fund that is subject to extensive political control. Hedge funds are not regulated and so have fewer conflicts of interest.

## Shareholder activism

Shareholder activism constitute of all actions taken by shareholders of a company to influence the management and boards of that company. They can range from writing a letter and corresponding with the management to the using of voting rights, going to court or even buy-out the company. Pound (1992) gives the following definition: A shareholder activist is an investor who buys a large stake in a publicly held corporation, with the intention to bring change and thereby realize a profit on the investment.

But why do shareholders actively monitor the company? From theory it is well known that the separation of ownership and control in public firms can give rise to the possibility of agency conflicts between the company's managers and shareholders (Berle and Means (1932), Jensen and Meckling (1976)). Monitoring the firm's management can be helpful in mitigating agency costs. While monitoring may reduce the agency costs, the benefits from monitoring are enjoyed by all shareholders and the costs are only beard by the activists (Grossman and Hart (1980)). Shleifer and Vishny (1986) argue that large shareholders may be able to overcome the potential free rider problems because they have a large equity stake in the firm.

Surprisingly most studies that cover monitoring or activism by pension funds and mutual funds provide little or no evidence consistent with the theory (Opler and Sokobin (1995), Strickland et al. (1996), Karpoff et al. (1996), Smith (1996), Wahal (1996), Del Guercio and Hawkins (1999), Parrino et al. (2003) and Barber (2007)). Karpoff (2001) comes to the conclusion that while activists are able to force some small changes in the targets governance structures, there is little evidence that activism leads to significant increases in operating performance or share value.

Shareholder activism by hedge funds can be, in contrast with other institutional funds, more effective and efficient. The explanation of this lies in the fact that the other institutional funds are more regulated and have to cope with more restrictions. As described above hedge funds have less conflicts of interest, low regulatory constraints and more adequate management incentives to actively monitor. Therefore they should be a more credible threat to target firm management. So in sum hedge funds should be better monitors than other institutional funds. This is also argued by numerous legal scholars (Bratton (2007), Briggs (2007), Kahan and Rock (2007) and Partnoy and Thomas (2007)).

## Relevant research on hedge fund activism

There have been a few research papers aiming hedge fund activism and recent papers study hedge fund activism in the United States. Bratton (2007) and Kahan and Rock (2007) come up with some evidence of hedge fund activism but their methods for acquiring data are not complete and therefore these results are not that robust. Brav et al. (2008), Klein and Zur (2009) and Clifford (2008) use larger and better samples.

Klein and Zur (2009) use a sample of 194 Schedule 13D filings by hedge fund activist from 2003 to 2005. These are mandatory federal securities law filings under Section 13 of the 1934 Exchange Act in the United States of America (US). Investors must file with the US Securities and Exchange Commission (SEC) within 10 days of acquiring more than 5% of any class of securities, of a publicly traded company. They investigate how stock prices react to the announcement that a hedge fund has acquired a significant holding of 5% or more. From the filings they eliminate all cases that aren't aggressive or confrontational and the data is compared with a sample of other entrepreneurial confrontational activists. Klein and Zur (2009) report a 7.2% average abnormal stock return for hedge funds and a 1.9% stock return for other entrepreneurial activists during the period surrounding the initial Schedule 13D.

Hedge funds achieve their goals about 60% of the time and target companies are more profitable and financially healthy than firms targeted by other entrepreneurial activists. Changing the board of directors (26%) and changing the strategy of the company (19%) are the motives most expressed by hedge funds.

Brav et al. (2008) use a large sample of 235 activists' hedge funds between the period 2001-2006, mainly using Schedule 13D filings and news searches. They report a 7% to 8% average abnormal return during the (-20, +20) announcement window, using quite the same methods as Klein and Zur (2009).

Brav et al. (2008) also find out that the activists tend to target companies that are typically "value firms", and that have constant operating cash flows and return to assets. They have also more takeover defenses and pay their CEO's more than comparable firms (industry/size/book-to-market matched firms). Targets have also higher institutional ownership and trading liquidity, Brav et al. (2008) mentions that this makes it easier for activists to acquire a significant stake quickly. 40.6% of the time hedge funds achieve their goals, and 26% is partly successful.

They also look at the hostility of the interactions between hedge funds and the targets (this instead of Klein and Zur (2009)). Hedge funds are in less than 30% of the cases openly hostile. It is more common that the activists cooperate with managers and the funds achieve all or most of their stated goals in about two-thirds of all cases.

Clifford (2008) collects a sample of 197 unique hedge funds over the period 1998-2005. Clifford (2008) also uses 13D filings to collect his data, but uses a control group of passive block holdings by the same group of hedge funds. Surrounding the filing date (-2, +2) targeted firms by activists earn a 3.39% excess return. Passive hedge funds earn a 1.63% excess return.

So these papers find that hedge fund activism creates significantly higher abnormal returns indicating the value of intervention. Hedge funds engage in a new form of shareholder activism that clearly differs fundamentally from other institutional investors from the past. As mentioned above earlier studies show that institutional investors, often mutual funds and pension funds, do not achieve considerable benefits for shareholders.

The following paper from Becht, Franks, Mayer and Rossi (2009) investigates hedge fund activism in the United Kingdom (UK).

Instead of doing a public study using 13D filings, they conduct a study on one large U.K. pension fund, the Hermes U.K. Focus Fund, which is a sort of hedge fund. Unlike the studies of Brav et al. (2008) and Klein and Zur (2009), they find that this fund primarily targets poorly performing firms, and that most of the activism is related to private communication between the hedge funds and the management of the targeted firms. If the management doesn't want to cooperate then the fund seeks out the media.

The American studies are all rather consistent in their findings, mainly due to the fact that the data collection methods are quite similar. I will be able to compare my results with these studies also quite easily because I also use a quite similar data collection method.

The results of the UK study will be more difficult to compare considering the fact that this study only looks at one hedge fund and uses private information.

## The Netherlands

Up to my knowledge there is only one empirical research paper that aims at shareholder activism by hedge funds in the Netherlands. De Jong, Roosenboom, Verbeek and Verwijmeren (JRVV (2007)) have, in assignment of the Dutch Government, investigated hedge funds and private equity funds in the Netherlands. Although they mainly have done a literature review about the characteristics, actions and strategies of private equity funds and hedge funds. They also have done an empirical part on hedge fund activism by doing a study looking at notifications of substantial amounts at the AFM, news searches and sending a questionnaire to public listed firms.

Using the register of the AFM they only look at active hedge funds till July 2007. They find 12 cases in which a hedge fund has an active stake of more than 5% in a listed company starting from 2004. The authors also find 14 cases by doing a research using the newspaper Het Financieele Dagblad in the period 1985 till July 2007. The cases they find using the two methods are not mutually exclusive because some cases are in both samples. The most active hedge fund in the Netherlands is Centaurus following by Paulson and Fursa. The most expressed motive for activism is that hedge funds want the company to refocus its business and spin off some divisions. Second motive is trying to acquire a better price during a takeover. Of the 14 cases 3 hedge funds achieved their objective.

JRVV also sent a questionnaire to 130 Dutch listed corporations. Questions were related to hedge fund activism for three years ending July 2007. 35% of the questionnaires were useful for interpretation. 43% of the respondents report that at least one hedge fund had a stake in the company the past few years. The average holding period of hedge funds no longer having a stake in the company is 691 days, and the median is 273 days. The motives for activism were again mostly refocusing the business and more generally changing the business strategy.

I will later elaborate more about this study when I'm describing my data collection process and discuss my results.

Another interesting paper by De Jong, Mertens and Roosenboom (2006) studies shareholder activism in Dutch listing firms by using a sample of 235 annual general meetings held by 54 firms from 1998 through 2002. Their findings show that the presence and activism by Dutch shareholder meetings is low. On average 30% of the equity capital is present and all proposals at the meeting are sponsored by the management and only 9 out of 1583 are rejected or withdrawn. Their main conclusion is that general meetings do not provide shareholders to have significant influence on the management. This could mean that activist will use other methods.

A paper by Cziraki, Renneboog and Szilagyi (2009) investigates the role of shareholders initiating proxy proposals in European firms including the Netherlands. Although they don't take the Netherlands as a case of particular interest they find some interesting results about Continental Europe. The proposals submissions by shareholders remain relatively infrequent in Continental Europe, and proposal objectives are more focused on specific governance issues like the conventional use of shareholder proposals in the US. In the UK the use of proposals is much more common and also typically relate to a proxy contest seeking personal changes in the board and by doing so changing the strategy of the firm.

## **Corporate Governance**

In this part I will first document the corporate governance climate from the past decade in the Netherlands. I will only discuss those parts that are of interest to shareholder activism (for instance shareholder rights and minority protection). In the second part I will describe the main differences between the UK, US and the Netherlands, and by doing so explaining what kind of differences I will be expecting when confronting my data with that of earlier studies.

### **Corporate Governance in the Netherlands**

The corporate governance system in the Netherlands has undergone a lot of changes in the past decade. The public debate started back in the first half of the 1990s and since then multiple codes and legislation changes were adopted into the Dutch corporate governance system. I will first point out the main characteristics of the governance climate at the beginning of the millennium. After that I will, in time sequence, describe all changes in the system affecting shareholders and their relation with the management. I will end with a conclusion.

The Dutch model of corporate governance is stakeholder oriented like most countries in continental Europe. The share ownership is highly concentrated and there are relatively few listed companies while takeover activity is rather limited if we compare the Netherlands with the US and UK (Cools and van Praag (2007)). Comparing the Netherlands with other countries of continental Europe it becomes clear that ownership concentration is relatively low (Risk Metrics Group (2009)).

The management structure of most listed companies is a two-tier board with both a supervisory and a management board. The management consists of executive directors with the day-to-day management of the company and is responsible for the firm's strategic and operational decisions. The supervisory board consists of nonexecutive directors that supervise the policy adopted by the management board. They are independent and often consist of retired professional members and retired members of the management board. Further the supervisory board members are required by law to act in the interest of all stakeholders instead of only the shareholders (De Jong et al. (2006)).

The firm is in principal shareholder-controlled and therefore the shareholders elect the members of both boards and approve the annual accounts, they also vote on issues as mergers & acquisitions. The dividend policy is arranged by the management with the consent of the supervisory board, and it has to be formally approved by the shareholders (De Jong, De Jong, Mertens and Wasley (2005)). These powers of the shareholders dramatically change when companies are obliged to the Structured Regime.

## **Structuurregime (Structured Regime)**

Whenever a Dutch company has more than 100 employees, a legally installed work council and if the book value of the shareholders equity is in excess of 16 million euro's the company is legally required to adopt for a full structured regime (before 2004 it was 13 million euro's). When the structured regime is in place, it requires that the supervisory board takes over quite some powers from the shareholders:

- The establishing and approval of the annual accounts.
- The election of the management board.
- The co-optation of the supervisory board (it elects itself).

The supervisory board has also more authority over major decisions made by the management. Under the structured regime the supervisory board can determine its own position, and power has shifted from the shareholders to the supervisory board.

Shareholders can still vote on dividend policy and M&A, but their power diminished extensively. That's why often the structured regime is also accounted for if there is spoken about the anti-shareholder devices Dutch corporations can undertake (Cziraki, de Goeij and Renneboog (2010)). I will discuss the anti-shareholder devices more briefly later.

If companies are for the majority owned by a foreign entity they can only adopt a mitigated form of the regime. Under the mitigated structured regime shareholders can vote on the annual accounts and the appointment of the management but the co-optation of the supervisory board is still in place.

The greatest exception to the structured regime is if Dutch companies have more than 50% of their employees outside the Netherlands. These companies don't have to comply with the structured regime, but often these companies voluntarily adopt the full structured regime (De Jong et al. (2005)).

## **General Shareholders Meeting**

The general meetings have to take place within 6 months after the end of the financial year, and each year there should be at least one general meeting. Each shareholder is entitled to attend the general meeting in person.

The proposals at the annual meeting are passed by a simple majority of the votes, so 50% or more. It can however be that in the articles of association of a company or under Dutch



corporate law a larger percentage is required. The articles of association are different for each company although on a large part of these articles there are many resemblances. Important decisions that the structure and organization of the company can change have to be approved by the general meeting of shareholders. Examples are changing the articles of association and issuing of share capital. Other important strategic actions like the start of a joint venture and the split of the company are not in power of the shareholders. Although it is true that the issuance of share capital is in principle a shareholder decision the general meeting can delegate this decision to the management for a period of 5 years. And so in this case the decision to issue share capital is often subject to approval by the supervisory board (Bekkum, Hijink, Schouten and Winter (2010)).

Shareholders don't have the legal authority to submit proposals for the general shareholders meeting. Nevertheless they can get, if they have together more than 10% of the issued capital, the authorization from court to call an annual meeting and propose the agenda themselves.

### **Anti-Shareholders Devices**

It is common in the Dutch corporate landscape to instate defense mechanisms in the form of special securities to deviate from the one-share-one-vote principle. When deviating from this principle the management creates a situation in which the shareholders lose power. The next three types of securities are often used:

- Protective preference shares are the most widespread antitakeover device (Cziraki et al. (2010)). When there is a takeover threat, the management issues preference shares to a friendly trust office or outside investor. An advantage of issuing these shares is, next to the voting rights attached and so being able to vote in favor of the management, the case that the purchaser only has to pay 25% of the amount upfront. So when preference shares are implemented the company does not have that much cash up front. Often the preference shares are issued when the thread of a hostile takeover is perceived to exist.
- Priority shares are special shares that can be issued. The holder of priority shares has special voting privileges about important matters as merger approval, liquidation and the appointment of board members (Cziraki et al. (2010)).
- Certificates (same as Depositary receipts); The supervisory board can exchange normal shares for certificates. A Trust Office (friendly to the management) will administer the certificates, and the legal ownership of the ordinary shares will go to the Trust Office. The certificates will only carry cash flow rights. So when certificates are implemented all voting rights on the shares are obtained by the Trust Office (Cziraki et al. (2010)). Minority shareholders will then lose a lot of power, because now it will be much harder to challenge the company management.

## **Autoriteit Financiële Markten (AFM – Authority Financial Markets)**

“The AFM is the body responsible for regulating behavior on the financial markets in the Netherlands; it monitors all parties’ compliance with the relevant legislation and regulations. The AFM is an autonomous administrative authority that also advises the Ministry of Finance”<sup>1</sup> The authority of the AFM ranges from notification of substantial holdings and investigating insider trading to suspension of trading. Most of the decisions of the AFM are subject to appeal in front of the court in Rotterdam, an administrative court. The AFM has no direct involvement in corporate governance enforcement (Bekkum et al. (2010)).

In the Netherlands there is a regulation that is quite similar with the Schedule 13d filings of the US. This is the Dutch Act on the disclosure of voting power and capital interest in securities institutions regulated by the AFM (Wet Melding Zeggenschap - WMZ and since 2006 Wet op het Financieel Toezicht - Wft). Each person or legal entity that has a substantial holding in issuing institutions has to report this to the Dutch Authority for the Financial Markets.

“An issuing institution is a public limited company (Naamloze Vennootschap) incorporated under Dutch law whose shares are admitted to trading on a regulated market in the Netherlands or in another Member State of the European Union or an EEA State, or a legal entity incorporated under the law of a state that is not an EU Member State and whose shares are admitted to trading on a regulated market in the Netherlands (AFM.nl).”

As soon as the substantial holding of an investor equals or exceeds the 5% level of the issued capital then the shareholder should report this to the AFM. Further the shareholder should also notify the AFM if the substantial holding reaches, exceeds or falls below a threshold. Since November 1<sup>st</sup> 2006 the thresholds are: 5%, 10%, 15%, 20%, 25%, 30%, 40%, 50%, 60%, 75% and 95%. Before November 1<sup>st</sup> 2006 the thresholds were 5%, 10%, 25%, 50%, 66⅔%.

I will use the notifications published by the AFM for this thesis, and will further elaborate on them later on in the data collection process.

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<sup>1</sup> Gathered from AFM.nl, from the explanations of the activities of the AFM.

## **OndernemingsKamer (OK – The Enterprise Chamber of the Amsterdam Court of Appeal)**

The OK is a specialized judicial body and is unique in Europe. It is part of the Court of Justice in Amsterdam and has to judge disputes involving legal entities. Since the early 1970s the OK successfully solved many business disputes and the verdicts of the OK are also very influential in contributing to the Dutch corporate governance system. The judges of the OK consist of people expert in legal professions as well as commercial fields ([www.rechtspraak.nl](http://www.rechtspraak.nl)).

### **Inquiry Procedure**

Inquiry procedures before the OK provide an efficient method for (minority) shareholders to object to controlling shareholders and/or management. And it is an effective method to enforce rules and principles of the governance system. Also inquiry proceedings are a nice tool to obtain information, since one of the purposes of this right is to obtain clarity with respect to the affairs to the company (Bekkum et al. (2010)).

Any shareholder or group of shareholders that has a minimum of 10% of the issued capital/depositary receipts or having together at least 225,000 euro's nominal value worth of shares can go to the OK.

### **Controlling Shareholder**

A controlling shareholder is subject to legal norms in the Netherlands and has a fiduciary duty towards minority shareholders. According to the Corporate Governance Code (will be handled later); "the greater the interest which the shareholder has in a company, the greater is his responsibility to the company, the minority shareholders and other stakeholders". Minority shareholders ask for an inquiry procedure if they believe the principle of reasonableness and fairness is violated.

### **Management of the Company**

Whether the OK grants an inquiry depends on that there has to be sound reasons to doubt the proper policies of the company (management) and/or its business. If after inquiry mismanagement is concluded the OK can take immediate measures for the duration of the proceedings. Mismanagement is determined when elementary principles of responsible entrepreneurship have been breached.

Immediate measures the OK can take are:

- The dismissal of directors.
- The appointment of independent members to the supervisory board.
- Prohibiting the company from taking defensive measures.

Shareholder activist seem to have frequently initiated inquiry proceedings. When covering hedge fund cases, I will further elaborate on this.

### **Changing the corporate governance system**

The Dutch corporate governance system obviously imposes a stakeholder rather than a shareholder orientated system. During the first half of the 1990s a public debate started because of the wide arsenal of defensive measures companies had, and were using, in order to rescind takeovers. The Peters Committee was the first to write something down.

### **The Peters Committee**

Back in 1997 the Peters Committee initiated the debate on corporate governance. They issued forty recommendations that can be regarded as the first corporate governance code in the Netherlands. The report did not address the inherent problems of the structured regime involving the shareholders rights, but focused on making the structured regime more accountable to shareholders without changing shareholders rights (De Jong et al. (2005)).

De Jong et al. (2005) studied the extent to which Dutch firms complied with the recommendations made by the Peters Committee. The recommendations had no effect on corporate governance characteristics and in most cases the firms only comply formally but didn't implement major changes in corporate activity. It became clear that this "code" wasn't sufficient.

### **Code Tabaksblat**

On January 1<sup>st</sup> 2004 the new Dutch Corporate Governance Code came into effect (Tabaksblat Code). As of this date companies are required to write an additional chapter about corporate governance in their annual reports. The code is, just as many other national corporate governance codes, enforced by using a "comply-or-explain" approach. This means that in principle firms have to comply with the code, but if a company chooses not to it will have to explain and report this in the annual report. The Code is for all firms listed on the Dutch stock exchange and foreign companies with a statutory residence in the Netherlands (Akkermans et al. (2007)).

It contains 21 principles of good governance representing "the latest general views on good corporate governance" and of which has several points that try to improve the rights of the shareholder (Corporate Governance Committee (2003)). Generally the Dutch Code aims at changing the behavior of management in a more transparent way, and to improve the quality and integrity of both the management and supervisory board.

Some important aspects of the code that are also pointed out by Cziraki et al. (2010) are:

- It tries to facilitate the shareholder communication better by advising companies to adopt the possibility of proxy voting.
- Depositary receipt holders should be granted voting rights at all times.
- It is calling for a more active role of institutional investors in the general meetings.
- It set caps on the number of supervisory board members that come from other listed companies and are also in the supervisory board or management board of those companies (Cziraki et al. (2010)).

Also the Code provides that supervisory directors may hold office for a period of three four-year terms max. Bekkum et al. (2010) argue that staggered boards are not applied by listed companies (so that for instance only one-third of the board comes up for election each year). Although often provisions in the articles of association describe, that members can only be dismissed by the general meeting with a majority of two thirds of the votes.

Akkermans et al. (2007) investigate the implementation of the Dutch Corporate Governance Code in 2005. They conclude that in order to assess the actual impact of the Code a much longer perspective is needed, but the first signs are rather positive.

### **The Corporate Governance Code Monitoring Committee**

The Monitoring Committee monitors trends in the application of the Code and issues yearly reports. The Dutch government established the Monitoring Committee on December 6<sup>th</sup> 2004. Below I will give a summary of the findings of three years monitoring the Code by the Committee (2004-2006).

A lot of companies have dismantled their anti-takeover mechanisms under market pressure. The Committee states that shareholders since the introduction of the Code have taken a more active approach. In some cases this has led to disputes between the management and the shareholders, and in which interesting rulings by the OK were taken. The rate of compliance to the code is stabilized to 95% of all listed companies by 2006 (this means that they adopt the code in their communication with the shareholders), and the rate of application rose from 87 to 90% (this means that they applied with the code). The average attendance rate at general meetings of shareholders is 57% in 2006. Since January 2007 a legal basis is created for the use of electronic means to communicate, so the Committee expects the attendance rate to rise in the future. Explanations for non-application of parts of the Code were increasingly standardized by the companies; this is considered as an undesirable trend.

## Structured Regime Reform Act

The Structured Regime Reform Act is a change in law of the old Structured Regime. Effective from September 1<sup>st</sup> 2004 the act cuts back some of the authority of the supervisory board and also increases the shareholder power in other areas.

- Shareholders and the works council are allowed to recommend candidates for supervisory membership prior to the nomination made by the supervisory board.
- The firm's annual accounts and the remuneration of both boards have to be approved by the general meeting.
- A general meeting of shareholders with at least one-third of the issued capital present may reject nominations for supervisory board members and dismiss the supervisory board with a majority vote.
- Shareholders also have to approve for more transactions that will have a material impact on the nature of the company, so for instance joint ventures or divestures.
- Both shareholders and holders of depositary receipts can place resolutions on the agenda of general meetings if they have a stake of at least 1% or 50 million euro in the company's shares. A notion to make is that often certain important proposals can only be requested by the management or the supervisory board. For example proposals to change the articles of association, issue shares and authorize management to sell company's assets (De Jong et al. (2006)).
- Companies (Trust Offices) will have to give depositary receipt holders voting rights if they request this at an annual meeting. But there are some exceptions to this, if the company is under threat of a hostile takeover and if the issuer of the depositary receipts has the opinion granting those voting rights would be strongly against the company's interest.

Since 2007 it is also possible to attend the general meeting electronically, but this has to be arranged in the articles of association. Proxy voting is still in a development stage in the Netherlands (proxy voting is that you can vote from a distance if you can't attend the annual meeting). This is mainly because of the major obstacles that are still in place in the Netherlands and that oppose a well-functioning proxy voting system. Most shares in Dutch listed firms are dematerialized bearer shares, and so for companies it's hard to trace the identity of the shareholders. This makes it difficult for companies to distribute information (Bekum et al. (2010)).

## **Proxy Solicitation**

Proxy solicitation is a way in which shareholders try to get in contact with other shareholders and with their approval vote for them in upcoming annual meetings. Due to the fact that proxy voting is still in a development stage it is also difficult for shareholders to contact each other. There is a proposal by the Dutch Ministry of Finance to enable investors to communicate with one another. Shortly it will mean that investors that individually or collectively hold 10% or more of the shares may request the company to extract the identity of its investors. And the investors may also request that the company will distribute information to these shareholders on behalf of them (Bekkum et al. (2010)).

## **EU Directive on Takeover Bids**

On the 28<sup>th</sup> of October 2007 the public bid rules came into force in the Netherlands. This was an implementation of the EU Directive on Takeover Bids. This directive was aimed to override potential measures that management undertakes during a takeover bid to frustrate a bid. In the Netherlands a mandatory bid rule was introduced at 30%. This means that any shareholder who acquires an interest in a company of 30% or more has to make a bid for all other shares.

Although there were intentions to impact the range of anti-takeover devices management could adopt, no severe measures were undertaken. For instance the board neutrality rule and the breakthrough rule are almost never used, since the Dutch legislature has only implanted these rules as an option for companies to include these in their articles of association.

Case law that developed during the decade provides more information for analyzing the climate of the use of anti-shareholder devices in the Netherlands. The Supreme Court (April 2003, JOR 2003), in the case concerning fund Rodamco, elaborated that defensive measures can be justified if they are needed for the long-term continuity of the company and its stakeholders. So this explicit means not only the shareholders. Making use of defensive measures for an indefinite moment of time is not justified.

The above verdict by the Supreme Court refers mostly to the post-bid defensive measure of preference shares. Pre-bid defensive measures like the depositary shares are since the Structured Regime Reform Act a bit weakened. Like said before the administration office is required by law that it issues proxies to holders of depositary shares who so request, but in case of a hostile takeover this isn't mandatory. The Corporate Governance Code is more strict in stipulating that the use of depositary shares as an anti-takeover measures is not allowed. Research from Raaijmakers, Elst and De Jong (2007) found out that the use of depositary

receipts for shares decreased extensively between 1992 and 2006. Generally it has become less common for listed companies in the Netherlands to have various types of defensive measures.

The squeeze-out right of shareholders and the sell-out right are laying both at the 95 percentage. So if shareholders acquire 95% of the shares, they may push out the existing shareholders at a fair price. The minority shareholders may also demand due to the sell-out rule that the majority holder buys them out at a fair price. Both the rights should be exercised within three months of the expiration of the offer (Bekkum et al. (2010)).

### **The new Corporate Governance Code (Code Frijns)**

In December 2008 the Monitoring Committee published an updated version of the Code (Code Frijns), this new code came into force on January 1<sup>st</sup> 2009. The Code became more stringent on parts of remuneration and risk management and appears to be aiming on mitigating the influence of activist shareholders. The new provision about proxy proposals is a good example. If a shareholder intends to put an item on the agenda for the coming shareholders meeting and this agenda point could result in the change of the company's strategy, the management board is given the opportunity to wait with a respond up to 180 days.

Also the Dutch government has recently proposed additional legislative measures that have the effect of limiting shareholders power. Shareholders should only be entitled to put points on the agenda if they have 3% of the issued capital (instead of 1%) and the disclosure requirements of shareholders should go from 5% to 3%. Also shareholders that exceed this threshold will have to disclose whether or not they agree with the strategy of the company.

### **One-Tier Board**

In November 2008 the Dutch Parliament presented a bill in which Dutch companies would get the opportunity to obtain for the one-tier board structure. December 8<sup>th</sup> 2009 the bill passed and it is expected that the law will be put in place in the end of 2010. Companies with a foreign legal entity and on the Dutch exchange can already have a one-tier board structure. A report by the Spencer Stuart (2009), one of the world's leading executive search consulting firms, investigates board trends and practices at 100 leading companies in the Netherlands. In 2008 10% of the companies have a one-tier board; examples of these are Royal Dutch Shell, Unilever and LogicaCMG.

Bekkum et al. (2010) argue that in practice the operation of a one-tier board and a two-tier board in the Netherlands may not differ fundamentally. Although the one-tier board is often associated with more meetings of the board, and a stronger involvement of non-executive



directors, this can also be achieved without difficulty in a two-tier model. So the differences seem to be more in perception than in reality.

## **Conclusion**

The Dutch corporate governance is quite unique on some points. Most companies are obliged to the structured regime and shareholders can ask for an inquiry procedure at the OK. It also became clear that a lot has changed when we look at the rights of shareholders in the Dutch corporate governance system.

The system still remains stakeholder orientated, but certainly during the decade power has shifted from the management and supervisory board to the shareholders. For example shareholders can now since 2004 submit proposals for the annual meeting when they have more than 1% of the issued capital. Depositary receipt holders have gained more power, although the situation for shareholders is still not ideal.

The shift from power from the management to the shareholders is of extremely importance to possible activist because in this way they will have more changes to become successfully active (for instance they can put better pressure on the board). That is also why I expect that during the decade activism by hedge funds did increase, and that they also went more successful in achieving their objectives.

Mainly due to the financial crisis media and politicians seem to argue that the 'restore of shareholder powers' has gone too far. Often heard arguments are that companies are now more subject to the aggressive en short-term thinking of activists and that this is negative for the stakeholders. If this debate will continue, than it could be possible that in the future shareholders have to hand in some of their power.

I believe that due to the crisis many activists will have trouble to stay active because they themselves will also be severely affected. So although fundamental revisions of the shareholder power in the governance system don't have occurred yet, I do expect the last few years a strong decline in hedge fund activism.

## **Comparison of the US, UK and Netherlands legal and institutional hedge fund activism environment, the key differences and similarities**

In order to compare my results with those of research from the US and partly the UK I need to point out the differences and similarities between the legal and institutional hedge fund activism environment. I will only cover those aspects that are relevant for hedge fund activism and I will use the current corporate governance system in the Netherlands for comparison.

Because of the fact that there are large differences on legislation and shareholder rights between states in the US it's hard to compare those. The academic literature often chooses the state of Delaware as example for the US as a whole (Becht et al. (2009)). They do this because many US firms are legally incorporated in this state. Therefore I also rely on the state Delaware as proxy for the legal and institutional activism environment of the US.

### **Extraordinary General Meeting (EGM)**

In principal special meetings cannot be called by shareholders in the US, only when there are specific provisions in corporate charters it can be possible. In the UK a shareholder or group of shareholders with at least 10% of the company's voting capital can request an EGM, the company's articles cannot deprive the shareholders of this right (Becht et al. (2009)). In the Netherlands there is also 10% of the voting capital needed to request an extraordinary meeting (Cziraki et al. (2009)).

### **Shareholder proposals**

Shareholders in the US can ask the company to add proposals for the coming meeting if they own 1% of the voting shares or \$1000 in market value, but not regarding issues relating to elections (Cziraki et al. (2009)). Also those proposals receiving a majority of the vote are in general not binding on the board. A shareholder or group of shareholders holding 5% of the total voting rights, or 100 or more shareholders each with at least 100 pounds paid-up capital can add proposals to the coming meeting in the UK and these proposals are legally binding (Becht et al. (2009)). In the Netherlands shareholder proposals are also not legally binding (Cziraki et al. (2009)). In the Netherlands shareholders with a stake of at least 1% or 50 million euro of the company's shares or certificates may submit a proposal. But for many topics only management or the supervisory board may propose. These are topics including the most important parts of strategic decisions namely, share issues the changing of the articles of association, asset sale etc.

Also if a general meeting would like to change provisions in the articles of association, that limit the general meeting's power to amend these articles, there has to be a unanimous vote where 100% of the share capital has to be represented in the Netherlands (Cziraki et al. (2009)). Also in the US shareholders cannot initiate a change in the articles of association. In the UK this is no problem; shareholders can always change the contract without agreement of the board (Bebchuk (2005)).

#### Board election

Under Delaware Law plurality voting applies by default, this means that the candidate that gets the most votes wins. So this doesn't mean that the majority of the votes are always needed (so not always 50% of all votes). In the UK, for each separate resolution, cumulative majority voting applies, this means that each director has to receive more than 50% of the votes. Irrespective of the provisions in corporate chapters the shareholders can always remove the board in the UK (Becht et al. (2009)). Since 2004 the shareholders of Dutch firms can now appoint the members of the supervisory board, although there are some restrictions. A general meeting of shareholders with at least one-third of the issued capital present may reject nominations for supervisory board members and dismiss the supervisory board with a majority vote.

#### Tenure

In the US it is also possible to stagger the terms of directors, so that only one-third of the board comes up for election each year (this is common under Delaware Law). The tenure of the board in the UK is determined by the articles but shareholders can always remove managers by ordinary resolution (Becht et al. (2009)). In the Netherlands staggered boards are not applied by listed companies, often provisions in the articles of association describe that members only may be dismissed with a majority of two thirds of the votes.

#### Restriction of voting power

In the US it is possible under the Delaware Law to issue shareholder right plans that limits voting power. Often this implies that shareholders are limited in the concentrating voting power they have above certain threshold (typically 10-15%) (Becht et al. (2009)). Poison pills and restrictions to the voting power of shareholders are largely not present in the UK. As mentioned above the Netherlands knows a lot of anti-shareholder devices, since 2004 the company's (Trust Office) will have to give depository receipt holders voting rights back if they request this at an annual meeting. But there are some exceptions to this, if the company is under threat of a hostile takeover and if the issuer of the depository receipts has the opinion granting those voting rights would be strongly against the company's interest. In those cases no voting rights have to be exchanged.

### Proxy Sollicitation

Shareholders proposals can be made doing a full proxy solicitation in the US. The costs of such a procedure are born by the shareholders (Becht et al. (2009)). In the UK the solicitation request is distributed to all shareholders at no major cost for the activist (Cziraki et al. 2009). Due to the fact that proxy voting is still in a development stage in the Netherlands it is difficult for shareholders to contact each other. That is why proxy solicitation is almost impossible in the Netherlands (Bekkum et al. (2010)).

### Court Protection

The Netherlands is quite unique because shareholders can go to the OndernemingsKamer when there are disputes between shareholders and management/majority shareholders. The OK can take immediate measures.

### Conclusion

Looking at the activism environment it becomes clear that the UK has a very good climate for hedge fund activism, almost on all cases the UK 'scores' better than the US and Netherlands. The US and the Netherlands seem to be closer to each other. This conclusion is also being made by Martynova and Renneboog (2010). They investigate the convergence of corporate governance regimes across countries. When looking at the corporate governance regulation indices of 2005 the values of the shareholder rights protection index and the minority shareholder right protection index of the US and the Netherlands lie close to each other. The index of the UK is clearly higher.

The better the (minority) shareholders are protected the more (successfully) active hedge funds can be. When I compare my data with that of studies from the US I therefore don't expect to find great differences in success rate. I expect to find different tactics employed by hedge funds between the Netherlands and US. For instance the calling of an EGM is in principle not possible in the US while it is in the Netherlands. Also in the Netherlands there is more often deviated from the one-share-one-vote principle than in the US. So it expected that shareholders in the Netherlands will choose more often for more 'radical' measures than shareholders in the US.

It is much harder to compare data with the UK, because of the lack of studies from the UK.

### 3. Data collection and data overview

This thesis looks at hedge fund activism from the beginning of 2000 till March 2010. Using such a large time frame has a few advantages and disadvantages. A first advantage is that I now look at hedge fund activism in times of financial prosperity and financial distress (the financial crisis (2007 till present)) in the Netherlands. Another advantage is that I now have better and more data about the holding periods of hedge funds in Dutch companies. If the chosen time frame was shorter, deriving conclusions would be harder.

A disadvantage of choosing such a large timeframe is obviously the large amounts of data that will have to be checked. Later I will comment more on the data sources I've been using. Another disadvantage that became clear in the previous chapter is that corporate governance practices and legislation changed quite dramatically during this timeframe. This can have a great effect on my results. So when deriving conclusions I will have to take this into account.

There is no regulated central database for activist hedge funds. I therefore have to construct my own independent database. As described before there are numerous studies that have investigated shareholder activism by hedge funds in the US. The studies from Brav et al. (2008) and Klein and Zur (2009) constructed their databases mostly using Schedule 13D filings. These are mandatory federal securities law filings under Section 13 of the 1934 Exchange Act in the US. Investors must file with the US Securities and Exchange Commission (SEC) within 10 days of acquiring more than 5%, of any class of securities, of a publicly traded company. Also investors have to file its reasons for acquiring the shares.

In the Netherlands there is also regulation that is quite similar with the Schedule 13d filings of the US. This is the Dutch Act on the disclosure of voting power and capital interest in securities institutions regulated by the AFM. This regulation is briefly described in the previous chapter.

Every filing is listed by the AFM in a public database. This public database is therefore my starting point for creating my dataset. I will look at each 'issuing institution' from this database between 2000 and March 2010, and the corresponding notifications. So this means that I will look at each public Dutch company and foreign companies that are traded in the Netherlands. The Dutch study by Jong, Roosenboom, Verbeek and Verwijmeren (2007)(JRVV) studied hedge fund activism partly by using also this database. They found some interesting results as described before.

There are numerous reasons why I take this public database as a starting point. First of all by taking this database I get a rather complete picture of all notifications about substantial amounts in public listed companies in the Netherlands. If we look at hedge fund activism, the hedge funds should often have a substantial amount of the issued capital to become active.

Although only 1% of the issued capital is needed to add a proposal to the coming shareholders meeting, having a larger stake means more power. So by looking at these notifications I can filter out all hedge funds active in the Netherlands. Second the filing of a substantial amount is mandatory and regulated by Dutch law, so this list should be very accurate. Third this list easily downloaded and copied to excel.

There are also a few disadvantages. One of them is also a big difference in comparison with the US. With a Schedule 13D filing the filer also has to mention why he is investing in the firm, in the Netherlands the filer never has to mention why he is investing in the firm. So for acquiring the motives of hedge funds to become active I will have to collect my data elsewhere.

A second disadvantage is that the filer also doesn't have to say what kind of investor she is. So for each filing I will have to check if the investor is a hedge fund or not. This is also a big difference with the method adopted by JRVV. They use the AFM database only as a first insight and they search for hedge funds in the database by typing in names of hedge funds that they found by searching through news media. The AFM database is of much more importance to me, and I therefore will check for each investor (each filing) if it is a hedge fund or not (so this is the other way around). In this way I will not only cover active hedge funds that were in the media, but also hedge funds that were not active or just didn't catch the media attention. I believe that hedge funds can be active, while not being hostile to the company and these cases will not make the media that often. So I believe I will find more filings by hedge funds than the study by JRVV.

When working through the data I also came to a third disadvantage. After three months that a company is delisted, the data of that company will be removed from the public database of the AFM. This could mean that some companies that are of interest to my study aren't in the list. I will come back to this later. Fourth hedge funds that don't cross the 5% threshold will not be visible to me. You could state that those hedge funds that have a smaller interest in a company would have a very hard time to become active (because of lack of power). But in very large companies an interest of only a small percentage could already be of big importance, certainly when the hedge funds cooperate with each other.

So while the public database of the AFM isn't perfect, it is a good start for investigating hedge fund activism.

From 2000 till March 2010 there are a total of 5214 filings in 421 companies. Of these 421 companies I immediately filtered out 134 companies from who was clear that they were investment funds, paper administration offices or no regular companies. I deleted those because for this thesis hedge fund activism in regular companies is of interest. On the next page there is a table with a few examples of filings.

Table 1. Few examples of filings

Date	Issuing Institution	Filer	%Capital	%Voting Power
24-March-10	Koninklijke Wessanen N.V.	Delta Partners, LLC	10.03	10.03
26-March-10	DIM Vastgoed N.V.	Equity One Inc.	90.84	90.84
29-March-10	Efes Breweries International N.V.	F.E. Eaton	0	0

So on the 24<sup>th</sup> of March 2010 Delta Partners acquired a 10.03% stake of the issued capital of Koninklijke Wessanen. This means that Delta Partners went above the threshold of 10%, and therefore had to report this to the AFM. This does not immediately mean that this is the first time Delta Partners acquired a stake in the company, it could namely be that Delta passed the 5% threshold a few years earlier. So for each filer I will have to check when the first notification took place.

In the next step I've looked more in depth to 'issuing institutions'. I wanted to know where the company was traded, if they have had perhaps a name change in the past and if they still exist. Although this was time consuming it was important for me, because in this way I could get a better feeling about the companies and I could check the reliability of the public list by the AFM. This research is done with online databases that were accessible through the University of Tilburg Library. The databases are; company.info, Zephyr, REACH and Corporate Affiliations.

There were some interesting and affirmative results:

- On the list are quite a few companies that aren't traded in Amsterdam but on other exchanges in Europe.
- Some companies have a foreign legal entity and are on the list, because they are traded in Amsterdam.
- Some companies are cross listed, in the sense that they for instance are traded in Amsterdam as well as in Frankfurt.

In the third step I scanned for every company that was left in the database (so those companies already excluded weren't covered), the entity of the filers. In this way I can filter out all filers that aren't hedge funds and so are not of interest to this study. Again I used the online databases but now I also looked at the company's websites. Persons, banks, normal companies, governments and insurance companies could be easily identified by going through the company's websites.

Identifying the rest of the filers is a lot more difficult. For each filer I checked if the filer had the same characteristics as a hedge fund. One way in which I was able to filter out some filers was looking in the database of the SEC. One of the characteristics of a hedge fund is that it is not

registered as an investment company with the SEC in the US. So running through the database, I was able to filter out these filers that were registered with the SEC. Next I also used news searches with LexisNexis using the filer's name. I combined these results with results from the company's websites. In this way I was able to make a dataset of all hedge funds filing in the Netherlands between 2000 and March 2010.

The database consists of 28 hedge funds with 168 filings in 27 'issuing institutions'. The first filing date is September 16<sup>th</sup> 2002 and the last is from March 9<sup>th</sup> 2010. Concentrating on only the first time a hedge fund reported a substantial amount in a company, there are 41 filings. So it becomes clear that hedge funds often change their stake in the issued capital of a company after their first filing. Namely after the 41 'first time' filings, there are another 127 reports to the AFM. Below is an example of notification by a hedge fund, with some additional explanation.

*Table 2. Notifications by Hermes in Océ*

<b>Date</b>	<b>Issuing Institution</b>	<b>Filer</b>	<b>%Capital</b>	<b>%Voting Power</b>
<b>24-Oct-08</b>	Océ N.V.	Hermes Focus Asset Management Europe Limited	10.14	10.14
<b>27-April-09</b>	Océ N.V.	Hermes Focus Asset Management Europe Limited	9.57	9.57
<b>6-July-10</b>	Océ N.V.	Hermes Focus Asset Management Europe Limited	4.93	4.93

Hermes made their first filing on the 24<sup>th</sup> of October 2008 with a stake of 10.14%. It now also becomes clear that Hermes in their first notification passed at the same time the 5 and 10% threshold. So in my dataset it can be easily seen if a company passed thresholds before. Hermes also had 2 additional filings, so Hermes has changed their stake in Océ 2 times at a minimum. This is the minimum because the AFM works only with thresholds, and so only these 2 extra filings are visible to the public. It could be very possible that Hermes did change their stake in the company more often but that it didn't 'hit' any threshold. So the total of 127 reports of changes in the notifications of substantial amounts after the 41 'first timers' is just a first insight, in fact it is much more plausible that hedge funds change their interest in issued capital much more often.

28 out of the 41 cases had their first filing before August 2007. In comparison JRVV had 8 less filings namely 20. This is due the fact that I performed my data collection process the other way around as they did, as explained before.



Given that the amount of capital to be acquired is 5% before a hedge fund will have to report this to the AFM this method could bias the data toward smaller targets. As mentioned before it can be that a hedge fund is active but that it doesn't have a stake of at least 5%. This is especially true in very large companies. A good example of this is The Children's Investment Master Fund Ltd. that had only approximately 1% of the issuing capital of ABN-AMRO when it launched its activism campaign in 2007 (and so was able to add proposals to the shareholders annual meeting). To incorporate activism events that are not accompanied by the AFM public list I collected information through news searches (LexisNexis) using combinations of 'hedge fund' and 'activism' as key words (both in Dutch and English).

After doing extensively news searches I managed to add to the dataset 10 complete new hedge funds and a total of 24 new cases. I also came up with the interesting case of Corporate Express. Although hedge fund Centaurus had a stake of over 5% in June 2007, this filing wasn't in the dataset. After contacting with the AFM, they explained that after 3 months a company was delisted from an exchange all data was removed. But this explanation is in contrast with other companies in my sample. For instance Stork is no longer listed, but the data is still available. So although the 3 month rule may apply for the AFM public list, most of the data about the companies is still available. After doing these extensively news searches I even can't find any company other than Corporate Express in which a hedge fund had a stake of more than 5% and isn't on the list. This is also the reason that by adding the 24 new cases to the original data I am convinced that this dataset is very accurate and complete.

So in sum the sample consists of 38 hedge funds with 41 'first time' filings and an additional 24 cases from news searches. The total number of filings from hedge funds in the public AFM list is 168. Below is an example of a hedge fund case that I've found doing news searches.

*Table 3. TPG-Axon in AkzoNobel*

<b>Date</b>	<b>Issuing Institution</b>	<b>Hedge Fund</b>	<b>%Capital</b>	<b>%Voting Power</b>
<b>2007</b>	AkzoNobel N.V.	TPG-Axon	?	3.5

The hedge fund with an active stake in AkzoNobel is TPG-Axon. Doing news searches it became clear that TPG-Axon had approximate 3.5% voting power and that it started their activism in 2007. Often it didn't become clear how big the interest in the issued capital was, but for the cases it did the data was implemented. The year in which the hedge fund became active was inserted as the year in which the hedge fund had a share of the issued capital for the first time. Later when I examine stock returns I will look for the exact date in which the media reported that the hedge fund became active.

## The country of origin

Below there is a table in which the countries, from which the hedge funds operate, are noted for each hedge fund in my sample. I've looked at the location of the headquarters and by doing so finding out what the countries of origin are. The hedge funds are most often, according to the articles of association, sited in tax friendly countries as described before. But it is very hard to find out which countries those exactly are. Therefore I only look at the location of the headquarters. Remind that although some hedge funds operate from the UK (the managers work in the UK), they still cannot be regulated because the hedge fund itself is not regulated in the UK.

*Table 4. Headquarters Location*

<b>Headquarters Location</b>	<b>Number</b>
<b>Monaco</b>	1
<b>Spain</b>	1
<b>UK</b>	17
<b>US</b>	19

## Number of Cases

In the table below I noted the year in which the hedge funds had, for the first time, a share in the company. This is only an indication of the year in which hedge funds became active for two reasons. First there are still cases in the sample where activism has not occurred (yet), I will look at activism more in the next part of the chapter. Second although hedge funds often become active immediately after acquiring a stake in the company, the first filing date isn't always the exact date activism started. Later when I examine stock returns it also becomes clear that some hedge funds are in the media before they even filed an interest with the company to the AFM.

*Table 5. Number of cases*

<b>Year</b>	<b>Cases</b>
<b>2000</b>	0
<b>2001</b>	0
<b>2002</b>	3
<b>2003</b>	1
<b>2004</b>	7
<b>2005</b>	9
<b>2006</b>	13
<b>2007</b>	18
<b>2008</b>	11
<b>2009</b>	1
<b>2010 (till March)</b>	1

There is not enough data to calculate a trend and we have to be careful when deriving conclusions. But there are some interesting things to say about the data. Since 2004 there is an increase in the number of cases that declines after 2007 and almost entirely stops in 2009. The increase in 2004 and further can be explained by an increase of shareholders powers in the Netherlands as we have seen in the previous chapter. If hedge funds think they are not able at all to achieve their objectives due to the corporate governance climate of a country I believe they will seek their business elsewhere.

The expected effect of the financial crisis that started during 2007 and made his way till now and the corresponding declines in the stock markets worldwide occurred. A sudden drop in het number of hedge funds having a stake in Dutch companies is the result. A good example of this is the hedge fund Fursa (formally known as Mellon). In an article by Het Financieele Dagblad of January 10<sup>th</sup> 2009, Fursa is mentioned as one of the hedge funds that is lowering their interest in multiple companies because they suffered great losses due to falling stock markets. Of one case I wasn't able to find out the year in which the hedge fund had an interest for the first time.

I can compare the number of hedge fund cases from the last decade with the total sample of filings from the list published by the AFM. In this way I may get a clearer picture. I've looked at the total of filings of all companies, the filings of only the companies were hedge funds had/have a share in, and the first time filings of the companies were hedge funds had/have shares in (all data is from the last decade). In the table below are the results.

*Table 6. Number of filings*

<b>Year</b>	<b>All filings, all companies</b>	<b><math>((t+1)-t)/t</math></b>	<b>All filings, only companies with hedge fund interest</b>	<b><math>((t+1)-t)/t</math></b>	<b>Only first time filings, only companies with hedge fund interest</b>	<b><math>((t+1)-t)/t</math></b>
<b>2000</b>	651	-	34	-	27	-
<b>2001</b>	467	-28.26%	36	5.88%	26	-3.70%
<b>2002</b>	322	-31.05%	36	0.00%	27	3.85%
<b>2003</b>	305	-5.28%	41	13.89%	17	-37.04%
<b>2004</b>	364	19.34%	57	39.02%	37	117.65%
<b>2005</b>	373	2.47%	53	-7.02%	20	-45.95%
<b>2006</b>	994	166.49%	203	283.02%	99	395.00%
<b>2007</b>	570	-42.66%	148	-27.09%	43	-56.57%
<b>2008</b>	582	2.11%	168	13.51%	52	20.93%
<b>2009</b>	475	-18.38%	103	-38.69%	30	-42.31%
<b>2010</b>	111	-	26	-	6	-
<b>Total</b>	5214	-	905	-	384	-

It immediately stands out that 2006 is a year in which there was a high increase in the number of filings. The explanation for this is that by November 2006, the number of thresholds of substantial amounts increased and therefore a lot of filings were reported. In 2009 there is also a decrease in the number of filings, but this decrease is not as drastic as with the hedge fund cases. So the effect of the financial crisis as mentioned before seems to be more dramatic for hedge funds than other filers.

In 2004 all filings increased, but it stands out that the first time filings increased a lot. This is consistent with my findings relating hedge funds. By 2004 shareholders powers increased so it became more interesting for different parties to invest in companies.

## Motives

After establishing the sample of hedge funds having an interest in issuing institutions the next step is looking at the motives and tactics of the hedge funds. Having just a stake in a company doesn't mean that there is a form of activism. As said before, in the US when filing at the SEC the filer has to file also the purpose of acquiring a stake in the company. This is in contrast with the Netherlands, where such a filing purpose isn't mandatory and never given.

In order to get an insight in the motives and tactics of the hedge funds I will have to rely on news searches again. Using LexisNexis with the issuing institutions and the belonging hedge fund as key words, I can construct for each case the possible motives and tactics of the hedge funds. In addition there is also searched into annual reports and the minutes of the annual meetings (also using the hedge fund as key word).

This thesis is using the same framework for motives as Brav et al. (2008). Using the same framework for categorizing the motives of hedge funds as the paper from Brav et al. (2008) has some advantages (on some part there are some adjustments). First after analyzing my data I can compare the results quite easily with the data from Brav et al. (2008). Second by using this framework researchers can use my data in the future more easily for comparing it with other countries.

The motives behind hedge fund activism can be classified in 5 categories, with some subcategories. A extra category is also added, in this 6<sup>th</sup> category are all hedge funds where no information whatsoever could be found using news searches and the company's reports. The events are also divided between successful, partial successful and no success. An event is classified as successful when the main objective of the hedge fund is achieved. Partial success is achieved if the hedge fund and the issuing institution reach some kind of settlement through negotiation and only part of the main objective is fulfilled. Although formally some cases are still pending, the possible outcome for each fund was easily predictable.

The first category includes events in which the hedge fund simply recognizes or believes that the issuing institution is undervalued and/or that the fund can help the manager maximize shareholder value. There is further no activism to achieve certain specific goals, beyond perhaps communicating with the management before the end of March 2010.

The second objective includes activism targeting the firm's payout policy and capital structure. In the first subgroup of this category, the hedge fund proposes changes toward the reduction of excess cash, increase in firm leverage or more/higher payouts to the shareholders either using stock repurchases or increase in dividends. The second subgroup of this category involves suggested equity issuance, such as stopping or reducing equity offerings by the target companies or proposed debt restructuring.

The third category of events includes activism targeting the business strategy. There are 5 subgroups that fall within this group. The first subgroup consists of general operational efficiency, cost cutting and tax efficiency-enhancing proposals. Second group consists of proposals to spin off some divisions or refocus the business strategy. This is in cases the activist believes that the company lacks business focus or exhibits excess diversification. Third, hedge fund may attempt to play an activist role in a pending merger or acquisitions, normally by asking for a better price when the firm is the target of the acquisition or by trying to stop the pending acquisition. Fourth, hedge funds may attempt to play an activist role in a pending merger or acquisition when the firm is the acquirer (also if the hedge funds attempt to stop a pending acquisition). Finally, hedge funds that make proposals stressing that the issuing institution better pursues its growth strategy.

The fourth objective involves activism demanding or urging the sale of the target. If hedge funds forces a sale of the company to a third party it ends in the first subgroup. If it wants to take over the company themselves it is the second subcategory.

The fifth category all activism targeting the firm governance is included and there are five subgroups. These are ranging from rescind takeover defenses; to remove the CEO or chairman; to challenge board independence and fair representation; to demand more information disclosure and question potential fraud; and to challenge the level or pay-for-performance sensitivity of remuneration. The categories, except the first and the sixth are not mutually exclusive as a hedge fund can target multiple issues. On the next page at table is given with all the outcomes.

Table 7. Motives

Motives/Objectives Categories	Events /Cases	% of Total Sample	% of Objectives (1) through (5)	% Success	% Partial Success
<b>1. General Undervaluation/ Maximize Shareholder value</b>	6	5.83%	7.23%	-	-
<b>2. Capital Structure (Total)</b>	15	14.56%	18.07%	66.67%	6.67%
-Excess cash, under-leverage, dividends/repurchases	13	12.62%	15.66%	61.54%	7.69%
-Equity issuance, restructure debt, recapitalization	2	1.94%	2.41%	100.00%	0.00%
<b>3. Business Strategy (Total)</b>	39	37.86%	46.99%	25.64%	35.90%
-Operational efficiency	2	1.94%	2.41%	0.00%	100.00%
-Lack of focus, business restructuring and spinning off	18	17.48%	21.69%	33.33%	55.56%
-M&A; as target (against the deal/for better terms)	13	12.62%	15.66%	23.08%	15.38%
-M&A; as acquirer (against the deal/for better terms)	5	4.85%	6.02%	20.00%	0.00%
-Pursue growth strategies	1	0.97%	1.20%	0.00%	0.00%
<b>4. Sale of Target Company (Total)</b>	5	4.85%	6.02%	40.00%	20.00%
-Sell company or main assets to a third party	5	4.85%	6.02%	40.00%	20.00%
-Take control/buyout company and/or take it private	0	0.00%	0.00%	-	-
<b>5. Governance (Total)</b>	18	17.48%	21.69%	38.89%	33.33%
-Rescind takeover defenses	6	5.83%	7.23%	100.00%	0.00%
-Oust CEO, chairman	4	3.88%	4.82%	0.00%	25.00%
-Board independence and fair representation	8	7.77%	9.64%	12.50%	62.50%
-More information disclosure/potential fraud	0	0.00%	0.00%	-	-
-Excess executive compensation/pay for performance	0	0.00%	0.00%	-	-
<b>6. No information besides AFM notification</b>	20	19.42%	-	-	-
<b>Sum of categories (1) through (5)</b>	83	80.58%	100.00%	-	-
<b>Sum of categories (2) through (5)</b>	77	74.76%	92.77%	37.66%	28.57%
<b>Sum of all categories</b>	103	100.00%	-	-	-

Of the 65 cases in the sample there were 20 cases where no additional info besides the AFM notification could be found. One could say that these hedge funds are thus not active. But as we have seen in the paper by Becht et al. (2009) and what also the research from JRVV concludes hedge funds often just communicate with the management. Only when that doesn't help hedge funds take more severe measures. One thing that is certain is that these hedge funds aren't hostile and cooperate with the management. The cases would otherwise have reached the media for certain, and so the motives of these hedge funds would also become clear.

Because I also studied the minutes of annual meetings and publications by the management regarding strategic and business developments there are only 3 options that these hedge funds will fall under.

- A hedge fund is just not active at all.
- The hedge fund's motive is increasing shareholder value (other motives would have become clear when studying the material).
- The hedge fund isn't active yet.

The remaining 45 cases from hedge funds, that were active for certain, had a total of 83 motives! There are even four hedge funds that had 4 motives for activism. In the table are the events as percentage of the total sample as well as the events as percentage of the first 5 categories given.

What stands out is that 38% of all motives by activists are in targeting business strategy when comparing with the total sample. Especially business restructuring and acting in a merger or acquisition are objectives often adopted by hedge funds. A third one that comes up often is changes proposing in the reduction of excess cash, increase firm leverage or higher payouts to shareholders using dividends or stock repurchases.

From this table it also becomes clear that hedge funds don't have any problem with the remuneration policy of companies in the Netherlands. In none of the 65 cases hedge funds were active in challenging the remuneration policy. This is of course in contrast with the current public debate in the Netherlands, where politicians often put pressure on the business climate to come up with regulation regarding the remuneration policy of corporations.

When I compare my results with the paper from Brav et al. (2008) some numbers point out. While in the US only 50% of the motives are other than maximizing shareholder value, 75% of the Netherlands is. Operational efficiency and the selling of the company or its main assets to a third party are motives that occur more in the US.

A striking resemblance is the success and partial success rates. They are for both countries respectively around the 40% and 25%. This confirms my hypothesis that I've stated when I



compared the governance climate of the Netherlands with that of the US. The (minority) shareholder protection index is quite the same for both countries, and indeed the success rate is also the same.

## **Tactics**

In order to achieve their objective, hedge funds need to act. In this part I will investigate which tactics activist use. In learning about the tactics hedge funds use in order to get their demands fulfilled we're able to tell something about the corporate governance climate in the Netherlands. For instance when hedge funds often choose to go to the OK, they maybe think that the powers of the shareholders to act in at the annual meeting are not sufficient for achieving their objectives.

There are numerous ways to look at tactics. Although hedge funds sometimes have more than one tactic to achieve an objective, news searches most often only extensively cover the most drastic/aggressive one. I therefore again also look at the annual reports and minutes of annual meetings. For each motive I was able to find out which tactics the hedge funds were using.

I will only report that tactic the hedge fund is using, that is the most drastic one. The advantage of this is that the data will explain how far hedge funds are willing to go. And possible tactics that I missed because of the unavailability are now less of importance; often tactics are unavailable because of lack of information in the minutes of shareholders meetings. So for each motive 1 tactic is recorded. I'm ordering the tactics from the least drastic to the most drastic.

I will also look at hostility. You could say that the least drastic is also the least hostile, but in some cases this isn't true. I will come back to this later. Where there is more than one hedge fund active in a single issuing institution (at the same time), I will also check if the activists work together to achieve their goals. On the next page there is a table.

Table 8. Tactics

Tactic Categories	Events	% of All Events
1. No explicit tactics, the hedge fund just intends to communicate with the management/board on a regular basis with the goal of enhancing shareholder value.	6	7.23%
2. The hedge fund tries to achieve their goals using the shareholders annual meeting. Either by threatening or putting agenda points on the coming meeting, to vote against certain propositions and/or to threat or call in for an extraordinary general meeting.	16	19.28%
3. The hedge fund goes deliberately public either using a public letter send to the management/board or by putting publicly pressure and/or announcing that it seeks other partners to go alongside with to take further action.	39	46.99%
4. The hedge fund threatens to go to the OndernemingKamer.	1	1.20%
5. The hedge fund goes to the OndernemingsKamer.	19	22.89%
6. The hedge fund intends to take over the company.	0	0.00%
7. Other	2	2.41%

The tactics only belong to the 83 motives that the 45 cases by hedge funds have. Obviously the remaining 20 cases in which no additional info was found are not covered here.

Two tactics belong to the 'other' category, this are tactics employed by Trafalgar Asset Managers and SRM Advisors. These two hedge funds were active in ArcelorMittal during the acquirer of Arcelor by Mittal. In short; both hedge funds were not satisfied with the takeover bid from Mittal. They eventually went to the Court in Rotterdam (so not the OK) accusing the AFM of not trying hard enough to get good information surrounding the takeover that could help the hedge funds. The hedge funds won this, and the AFM has to do a new investigation and this is still pending.

Almost 50% of the hedge funds are going deliberately public to achieve their objectives. This means that most hedge funds don't have enough trust in the corporate governance system. So although shareholders only need 1% of the issuing shares to add proposals and that more power has shifted from the managers to the shareholders. Hedge funds will often use public channels to achieve their goals, this is consistent with the paper from de Jong et al. (2006).

What really stands out is that 22.89% of all tactics involves going to the OndernemingsKamer (OK). The OK is a special legal authority in the Netherlands. Because of the uniqueness of this institution I will briefly discuss this topic later on in this chapter. A tactic is considered hostile if

it belongs to tactic 3 till 6. In these cases the management obviously doesn't agree with the motives of the hedge funds, otherwise these tactics wouldn't even occur. Tactic 1 is always non hostile but tactic 2 is a grey area.

It could be that putting an agenda point on the next annual meeting isn't hostile. If the board agrees with the agenda points than it will be considered as not hostile, but in some case this is in fact hostile. The example of The Children's Investment Master Fund Limited (TCI) active in ABN-Amro clarifies a lot. In 2007 the TCI wrote a letter to the board of ABN-Amro with the demand of putting certain new agenda points for the coming annual shareholders meeting. ABN-Amro soon made public that it was against the propositions from the TCI and advised all shareholders to vote against these propositions. In this case the tactics of TCI were indeed hostile.

There are only 5 cases in which category 2 tactics weren't hostile. So in total there were 11 events in which the hedge fund weren't hostile. If we add the 20 cases where no extra information was available of, there are a total of 31 cases where there was no hostility. This is almost a third of all cases (31/103). Because of the fact that only 11 of the 83 motives were not hostile it's difficult to say something about the success rate from hostility tactics compared with not hostile tactics. There is simply not enough data.

Running through the data it became soon clear that hedge funds often work together. Of the 36 issuing institutions in my database, 14 of them had more than 1 hedge fund acquiring a share in the company's issued capital. In 10 of these 14 companies hedge funds were working together to achieve their goals. In one case the hedge funds publicly disagreed with each other. This is consistent with the study by JRVV.

By creating a database using the public list of the AFM it is also possible to look at the investment horizon of the hedge funds. Hedge funds are often cited by critics as short term investment companies but Brav et al. (2008) argue that this is not true. They report an average holding period of 369 days, and mention that using their method of calculation this number is in reality most probably higher. Although in the US this number may be perceived as long-term I think that in the Netherlands this will be perceived as short term. Certainly when people compare hedge funds with the traditional pension funds as they most probably will do in the Netherlands.

So it is interesting to look at the holding period of the activists. The first filing date of the notifications of substantial amounts is taken as the starting date. The end date is the time when the hedge fund lowers its stake below the 5% threshold. For funds that I could find extra information about breakdown of exit I adjusted the end date to be more precise. By applying this method the average holding period is a careful measure of the actual holding period. Often

hedge funds have already a stake but just don't reach the 5% threshold, and funds that are still holding an interest less than 5% are not accounted for in this calculation. This of course means that the result underestimates the true duration of hedge funds investment. But it will give a nice image of the current situation. Again the holding period doesn't have to be same period as the active period.

*Table 9. Voting power and holding period*

<b>Average initial voting power %</b>	8.06%
<b>Median initial voting power %</b>	5.62%
<b>Average maximum voting power %</b>	10.10%
<b>Median maximum voting power %</b>	7.11%
<b>Average length of holding period (days)</b>	531
<b>Median length of holding period (days)</b>	319

<b>Percentile</b>	<b>Initial voting power %</b>	<b>Maximum voting power %</b>	<b>Length of holding period (days) (rounded up)</b>
<b>5%</b>	2.96%	2.96%	7
<b>25%</b>	5.11%	5.18%	176
<b>50%</b>	5.62%	7.11%	319
<b>75%</b>	8.54%	10.91%	808
<b>95%</b>	24.34%	30.49%	1699

The average length of holding period is 531 days, this is almost 1.5 years. And the median holding period is 319 days. The distribution is skewed to the right, while there are some cases where the holding period is extra long. The holding period is quite longer than that of Brav et al. (2008).

JRVV have done a questionnaire study addressing listed companies asking them about hedge fund activism. They find that the holding period of completed cases is on average 691 days. Logically this is more than what I have found, because my observations only start when they reach the 5% level. In the case of JRVV the exact complete period is reported.

The average initial voting power is 8.06%. This means that when the first filing is imported on average only the first threshold of 5% is breached. The median is 5.62%. We have to take into consideration that while I mostly use data from the AFM the average initial voting power will lay somewhat higher than the true one. This because initial voting power of below 5% is due to the method of data collection often not recognized. What also stands out is that hedge funds aren't generally involved in controlling blocks of stock. The interquartile of hedge funds initial stakes is from 5.11% to 8.54% and even the 75<sup>th</sup> percentile of the maximum ownership falls below 11%. This is also consistent with the paper from Brav et al. (2008). The average maximum voting

power is 10.10%, this is actually a very high outcome but the distribution is also skewed to the right.

### **Ondernemingskamer (OK - Dutch Enterprise Chamber)**

It immediately stood out that almost 22.89% of all tactics were regarding the OndernemingsKamer (OK - The Dutch Enterprise Chamber). Therefore I will look at the OK in more detail in this chapter. All court decisions are published and are available in a database. Using the Wolters Kluwer Online Research and the hedge funds and issuing institutions as keywords I'm able to check for each hedge fund if they appealed at the OK. I will only report the cases in which the hedge fund is reported as the party that requested the procedure at the OK.

As said before inquiry procedures are an efficient method for (minority) shareholders to object to controlling shareholders and/or management. When the OK reaches a verdict they can take provisional measures immediately. Any shareholder or group of shareholders that has a minimum of 10% of the issued capital/depository receipts or having together at least 225,000 euro's nominal value worth of shares can go to the OK.

On the next page there is a table in which all publications of the OK summed up. They are first ordered in alphabetic order of the issuing institution and then on the date the OK reached a verdict and/or made a publication.

Table 10. Cases at the OK

<b>Issuing Institution</b>	<b>ARO number</b>	<b>Date</b>	<b>Hedge fund(s)</b>
<b>ASM International N.V.</b>	2008, 106	May 20 <sup>th</sup> 2008	Fursa and Hermes
<b>ASM International N.V.</b>	2008, 112	June 27 <sup>th</sup> 2008	Fursa and Hermes
<b>ASM International N.V.</b>	2008, 154	September 8 <sup>th</sup> 2008	Fursa and Hermes
<b>ASM International N.V.</b>	2009, 6	December 22 <sup>nd</sup> 2008	Fursa and Hermes
<b>ASM International N.V.</b>	2009, 77	May 13 <sup>th</sup> 2009	Fursa and Hermes
<b>ASM International N.V.</b>	2009, 127	August 5 <sup>th</sup> 2009	Fursa and Hermes
<b>ASM International N.V.</b>	2009, 187	November 19 <sup>th</sup> 2009	Fursa and Hermes
<b>Océ N.V.</b>	Forthcoming	March 3 <sup>rd</sup> 2010	Hermes
<b>Stork N.V.</b>	2007, 21	January 17 <sup>th</sup> 2007	Centaurus, Greenway and Paulson
<b>Stork N.V.</b>	2007, 180	November 13 <sup>th</sup> 2007	Centaurus, Greenway and Paulson
<b>Stork N.V.</b>	2008, 28	January 24 <sup>th</sup> 2008	Centaurus, Greenway and Paulson
<b>Unilever N.V.</b>	2005, 113	May 4 <sup>th</sup> 2005	Fursa
<b>Unilever N.V.</b>	2006, 116	June 30 <sup>th</sup> 2006	Fursa
<b>Versatel Telecom International N.V.</b>	2005, 182	September 27 <sup>th</sup> 2005	Amber, Centaurus and Fursa
<b>Versatel Telecom International N.V.</b>	2006, 3	December 14 <sup>th</sup> 2005	Amber, Centaurus and Fursa
<b>Versatel Telecom International N.V.</b>	2006, 71	March 24 <sup>th</sup> 2006	Amber, Centaurus and Fursa
<b>Versatel Telecom International N.V.</b>	2006, 199	December 8 <sup>th</sup> 2006	Amber, Centaurus and Fursa
<b>Versatel Telecom International N.V.</b>	2007, 35	February 12 <sup>th</sup> 2007	Amber, Centaurus, Dorchester and Fursa
<b>Versatel Telecom International N.V.</b>	2007, 154	September 14 <sup>th</sup> 2007	Amber, Centaurus, Dorchester and Fursa
<b>Versatel Telecom International N.V.</b>	2008, 23	January 24 <sup>th</sup> 2008	Amber, Centaurus, Dorchester and Fursa

ARO (Actuele Rechtspraak Ondernemingspraktijk) is the journal in which all verdicts/publications of the OK are published. In the case of Océ the journal isn't yet published but a summary of the verdict is available on [www.rechtspraak.nl](http://www.rechtspraak.nl).

Although 22.89% of all tactics involves the Enterprise Chamber there are only 5 companies actually been involved with hedge fund activism through the OK. This constitutes to the most part that these hedge funds happen to have many motives and almost all work together. Therefore the number of OK cases seems limited, but almost more than 20% of the tactics employed by the hedge funds to accomplish their goals is appealing at the Enterprise Chamber.

The hedge funds had five motives for going to the OK; proposals to spin off some divisions or refocus the business strategy, attempts to play an activist role in a pending merger or acquisition, to oust the CEO or chairman, to challenge board independence and fair representation and to demand stock repurchases for a higher price.

For each case I will give a brief summary. In this way it becomes clearer what kind of actions the OK takes.

### **Fursa and Hermes against ASM International**

Fursa and Hermes have some disagreements with the board of ASM International concerning the strategy direction of the company. The activists want the current CEO to resign and to choose new members for the supervisory board. They are also against the new option of preference shares for the Stichting Continuïteit that is merely a defensive mechanism by the ASMI board to defend themselves from hostile takeovers. In 2007 they also wanted that the Asian activities of ASMI would be sold, but on that case they reached consensus with ASMI.

During the first quarter of 2008 the conversations between the activist and ASMI went downwards. Hermes together with Fursa went to the OK.

On May 20<sup>th</sup> 2008 the OK made some provisional measures. Hermes and Fursa should again start up the discussion with ASM International to try to get a consensus. Until then the annual meeting is postponed.

On July 15<sup>th</sup> an extraordinary annual meeting should take place that would treat all agenda points arranged by Hermes and Fursa.

On June 27<sup>th</sup> 2008 the OK, on request of all parties, adjourned the verdict by the OK of the ordered extraordinary annual meeting till further notice. This because there are two possible candidates, that have reported themselves, that have an interest in acquiring the front-end activities of ASMI.

On the 8<sup>th</sup> of September 2008 the OK again adjourned the ordered extraordinary shareholders meeting till further notice.

On December 22<sup>nd</sup> 2008 the OK again adjourned the ordered shareholders meeting. The OK reports that it is in the interest of all parties that, after the cancellation of the negotiations between ASMI and possible takeovers, all shareholders and the board have the opportunity to arrive to a consensus about previous cases.

On May 13<sup>th</sup> 2009 the OK decided that the option for new preference shares as defensive measures is prohibited. The old options that are already placed are still allowed, but this construction may not last forever. On all other cases the OK explains that it still doesn't have enough information and that the debate will have to be continued in very short notice.

August 5<sup>th</sup> 2009 the OK mentions that there are enough reasons to start an investigation in the adopted policy by ASMI against its shareholders.

November 19<sup>th</sup> 2009, the investigators are being assigned.

The outcome of this investigation is still ambiguous. But after the coming of two new big shareholders, the power of Hermes and Fursa is extensively decreased. ASMI did cancel their defensive mechanism (under strong pressure from the OK), so this is something Hermes and Fursa did achieve.

### **Hermes against Océ**

Hermes thought the takeover bid by Canon off all the shares of Océ was too low. Hermes didn't wanted to sell their shares, and now feared that after the takeover they would become jammed as minority shareholders. Therefore Hermes together with USS went to the OK, to ask for certain provisional measures. Hermes and USS asked the OK to appoint three special members for the supervisory board at Océ that could watch over the interest of minority shareholders. The Enterprise Chamber has dismissed the requests by Hermes and USS.

### **Centaurus, Greenway and Paulson against Stork**

Paulson, Centaurus and Greenway launched a shareholder campaign to split up the company. They thought that Stork was a conglomerate of unrelated business. Stork disagreed and therefore the 2 parties had a total different opinion about the strategy of the firm. The hedge funds ordered an extraordinary shareholders meeting with two main agenda points, the dismissal of the entire supervisory board and the strategy change. Stork responded with exercising the call option on preference shares for the Stichting Stork, the traditional defense



measure. In this way it would become impossible to vote for the agenda points on the current meeting. In responds to that the hedge funds went to the Dutch Enterprise Chamber.

January 17<sup>th</sup> 2007 the OK first states that the current climate between the hedge funds and Stork is no longer positive. Three provisional measures are taken; first the OK demands that the preference shares of Stichting Stork will be withdrawn. Second there will be an investigation of the current situation at Stork. Third the extraordinary shareholders meeting is cancelled and that instead there are 3 new supervisory board members chosen that will have a decisive voice in the coming annual shareholders meeting regarding the agenda points suggested by the hedge funds.

In the spring of 2007 a takeover candidate presented himself. Candover wanted to take over Stork and then sell a few divisions. After intervention of the 3 new supervisory board members the hedge funds agreed to sell their shares. Later Candover withdrew their bid because one other new big shareholder didn't want to sell their shares. In November 2007 Candover was working on a new bid.

November 13<sup>th</sup> 2007 and January 24<sup>th</sup> 2008, the OK first completed their investigation and in January the hedge funds wanted that the OK demanded the dismissal of some members of the board and supervisory board. They also thought there was mismanagement. Eventually the activist withdrew their demands because of the fact Candover did increase their bid and the hedge funds agreed to sell their shares. The OK concluded that since the hedge funds withdrew their claims no further investigation was necessary.

So the hedge funds were rather successful in the sense that Stork was being sold and partly split up.

### **Fursa against Unilever N.V.**

In 1999 Unilever distributes a super dividend of 16 billion euro. Unilever gives shareholders the possibility to choose between cash or cumulative preference shares (cumprefs). Cumprefs are fiscal attractive. It happens to be that the cumprefs are badly tradable and that the price of cumprefs soon becomes less than the issue price. Unilever makes public it wants to convert the cumprefs against a price far below the issue price, this resulted in a sharp loss in cumpref value. The VEB ("Association of Shareholders") sues Unilever and in the end Unilever settles with the VEB. Every cumpref holder that had held cumprefs in the evening before the announcement by Unilever will get a compensation.

After the news Fursa buys a large stake of cumprefs and counts on it that Unilever will buy them back for the issue price. Unliver communicates that Fursa falls not under the settlement

because it bought its cumprefs after March 23th 2004 (the day before Unilever made public it wants to convert its shares)

After this event Fursa went to the OK with the goal of getting compensation. On May 4<sup>th</sup> 2005 the OK decides that there is no reason to take immediate provisions and Fursa lost the case.

June 30<sup>th</sup> 2006 the OK again ruled in favor of Unilever. Fursa wanted that the OK determined mismanagement.

From the beginning of the dispute it was clear that Fursa was in a difficult position to win. It simply bought its cumprefs after March 23th and therefore wasn't entitled to the compensation.

### **Amber, Centaurus, Fursa and Dorchester against Versatel**

In 2005 Tele2 acquired a majority stake in Versatel. During the year Tele2 bought almost all shares from existing shareholders. Amber, Centaurus, Fursa and Dorchester didn't want to sell their shares because they thought that the existing bid was too low.

September 27<sup>th</sup> 2005; Amber, Centaurus and Fursa went to the OK. There were multiple reasons for this, first they thought that Tele 2 and Versatel agreed on different and better terms than Versatel and other shareholders regarding the takeover bid. And they wanted an investigation at Versatel regarding the handling of the takeover by Tele 2. The OK disagreed with the hedge funds. The investigation was postponed, and the takeover could go through.

December 14<sup>th</sup> 2005. In the annual shareholders meeting the supervisory board was replaced with new members all from Tele2 AB (daughter company of Tele2). The minority shareholders voted against this, but Tele2 has a majority stake so it went through. The OK takes one provisional measure. There will be 3 new independent supervisory board members elected, and all agenda points regarding rules that deviate from the Dutch Corporate Governance code are forbidden.

March 24<sup>th</sup> and December 8<sup>th</sup> 2006. During the first months of 2006 Versatel, Tele2 Holdings and Tele2 Finance made public their plans in the merger of the three companies. March 24<sup>th</sup> the OK took a provisional measure. It forbids the plans to go through because it isn't in line with the Corporate Governance code together with minority shareholders rights. During the year 2006, Versatel and Tele2 changed their plans. By December 8<sup>th</sup> the OK concluded that the merger was legit and that no further investigation was taken.

In their last try the hedge funds were again going to the OK. They mentioned that now that the merger was put through there were no fair exit terms for the existing minority shareholders.

The OK disagreed with the hedge funds and didn't create special exit terms for the hedge funds.

After the last verdict by the OK the hedge funds sold their shares to Tele2.

Note: Dorchester worked together with the other hedge funds, but only went alongside with the other hedge funds the last three times.

### **Conclusion OK**

In two of the five cases the companies used protective defensive measures in order to dilute the activist shareholders (ASMI and Stork). The general view is that defensive measures are justified if they are necessary to preserve the long term continuity of the company and its stakeholders. And only if the defensive measure can help in achieving a status quo of the takeover, so that negotiations can start. Having defensive measures for an infinite amount of time is not allowed. Both ASMI and Stork issued preference shares to protect themselves. Stork had, by demand of the OK, the obligation to withdraw its preference shares. The preference shares were issued so that shareholders couldn't vote for the dismissal of the supervisory board and this did not qualify for the use of defensive measures. At first ASMI was allowed to issue preference shares, because the replacing the entire supervisory board including the CEO was being judged as a raid. But the foundation that kept the preference shares was being found not independent of the board. And so not the status quo would have been preserved, but the management was just protected (Bekkum et al. (2010).

So it depends very much on the circumstances if a shareholder can address the OK to cancel the use of defensive measures. It is for certain that due to the power of the OK, shareholders in the Netherlands have a better opportunity to rescind to anti-shareholder measures.

In the case of Stork and ASMI, the activists tried to force the companies to spin of some divisions to refocus its strategy. There are two conclusions that can be made. First the authority of setting the company's strategy lies still with the management board, and under supervision of the supervisory board. Second when there is a large disagreement between shareholders and the management the OK takes some provisional measures; it tries to keep the dialogue going, both management and shareholders may not take actions that are irreversible and if a solution isn't found the OK will often appoint new supervisory board members that are independent.

This means that often hedge funds will reach a compromise with the company, and this is also seen in the data. More than 50% of all cases in which the motive of a hedge fund was, refocusing the business, the hedge fund had a partial success of their objective.

The verdict by the OK in the case of Stork also illustrates that the management board in the Netherlands is not able to ignore wishes of a majority of its shareholders. Although the hedge funds were unable to dismiss the supervisory board of Stork the OK appointed three supervisory board members and gave them special powers. The effect of this was that the power of the existing board strongly decreased.

The case of Versatel is a good example of minority shareholders that asked for an inquiry procedure at the OK against the block holder. As mentioned earlier, the corporate governance code has a notion about the responsibility of the large shareholders. "The greater the interest which the shareholder has in a company, the greater is his responsibility to the company, the minority shareholders and other stakeholders". Minority shareholders ask for an inquiry procedure if they believe the principle of reasonableness and fairness is violated. Following the case of Versatel the principle of reasonableness and fairness is violated when the controlling shareholders used his power to appoint members of the supervisory board. This means that minority shareholders have a fair chance at the OK, if they feel they are being oppressed by the block holders.

## **Market response to the filing of hedge funds and their activism**

The American studies have all be doing event studies surrounding the filing dates of the hedge funds in order to calculate the announcement effects of activism. As mentioned before hedge funds that file at the AFM don't have to give an explanation for the fact that they are taking an interest in the company. Therefore I expect that there will not be increase in the stock price around the filing of a hedge fund. Simply because the objectives of the hedge fund are not clear yet.

I'm conducting an event study by using methodology described by Frank de Jong (2007). I will first look to the hedge fund filings at the AFM. For each filing I know the exact date on which the filing took place and this date is the event date. The event window is the same as in the study by Brav et al. (2008), namely (-20, +20).

I define the abnormal returns as the residuals of the market model, and for the market index I choose the Amsterdam SE All share index for the listed companies on Euronext Amsterdam. For companies that are listed abroad, I pick the corresponding mayor indices of the particular country. For each company the total return index is downloaded from Datastream and if companies are cross listed, the Dutch total return index is taken. As an estimation window I use 150 days of data preceding the event period.

The results are as I expected. The event study consists of 34 cases and the average of abnormal returns (AAR) on the event date is almost zero, there is also no form of run-up before the filing. The cumulative average abnormal return (CAAR) after the end of the event window is also close to zero. So this means that the market does not react to a filing of a hedge fund at the AFM.

That's why it is interesting to look at the market response after the objectives of a hedge fund are clear (so when they become active). In the data collection process (described before) I was able to find an additional of 24 cases in which hedge funds became active that were not in my AFM list. By searching the news I've checked for each case on what date a first impression must have came that the hedge fund was active. I did this by using LexisNexis.

I also checked for every hedge fund, that I found in the AFM list, the date in which they became active. In some cases this was even before the date of a filing of a notification by the AFM. In sum I was able to collect 25 events (there are only 25 events because a lot of hedge funds became active on the same date in the same company). The event study was conducted by using the same methodology as before. To be clear; the event dates are now the dates on which for the first time it became clear why a hedge fund had an interest in a company and that it became active.

*Table 11. Abnormal Stock Returns Surrounding the Activism Events Dates by using the Market Model*

This table shows the abnormal average returns and cumulative abnormal average returns for the activism event dates. The event window is (-20,+20) and the estimation window is 150 days of data preceding the event period. The abnormal performance is tested by using a simple t-test.

\*\*\*significant at the 0.01 level; \*\*significant at the 0.05 level; \*significant at the 0.10 level.

Day	AAR	t(AAR)	CAAR
-20	-0,0002	-0,0544	-0,0002
-19	-0,0012	-0,5611	-0,0014
-18	0,0009	0,2760	-0,0006
-17	0,0001	0,0393	-0,0005
-16	0,0040	1,1955	0,0035
-15	-0,0032	-1,0046	0,0003
-14	-0,0006	-0,1279	-0,0003
-13	0,0012	0,5022	0,0009
-12	-0,0001	-0,0424	0,0008
-11	0,0021	0,6317	0,0029
-10	0,0006	0,1934	0,0035
-9	0,0028	0,9489	0,0064
-8	-0,0028	-0,8061	0,0036
-7	-0,0017	-0,4014	0,0019
-6	0,0057	1,7704*	0,0075
-5	0,0001	0,0173	0,0076
-4	0,0074	2,5125***	0,0150
-3	0,0049	1,4833	0,0199
-2	0,0112	1,9588*	0,0312
-1	-0,0019	-0,4596	0,0293
0	0,0248	2,9780***	0,0540
1	-0,0020	-0,5214	0,0521
2	0,0050	1,6083	0,0571
3	-0,0042	-1,1045	0,0529
4	0,0038	0,9962	0,0567
5	0,0006	0,1709	0,0573
6	0,0025	0,9217	0,0598
7	-0,0028	-0,9617	0,0569
8	-0,0004	-0,1730	0,0565
9	0,0002	0,0916	0,0567
10	0,0026	0,6323	0,0592
11	0,0001	0,0122	0,0593
12	-0,0061	-2,0443**	0,0532
13	0,0014	0,3064	0,0546
14	0,0021	0,5907	0,0568
15	-0,0017	-0,4346	0,0551
16	0,0037	1,5741	0,0588
17	0,0010	0,3565	0,0598
18	0,0056	1,2685	0,0653
19	0,0021	0,7864	0,0674
20	-0,0038	-1,3221	0,0636

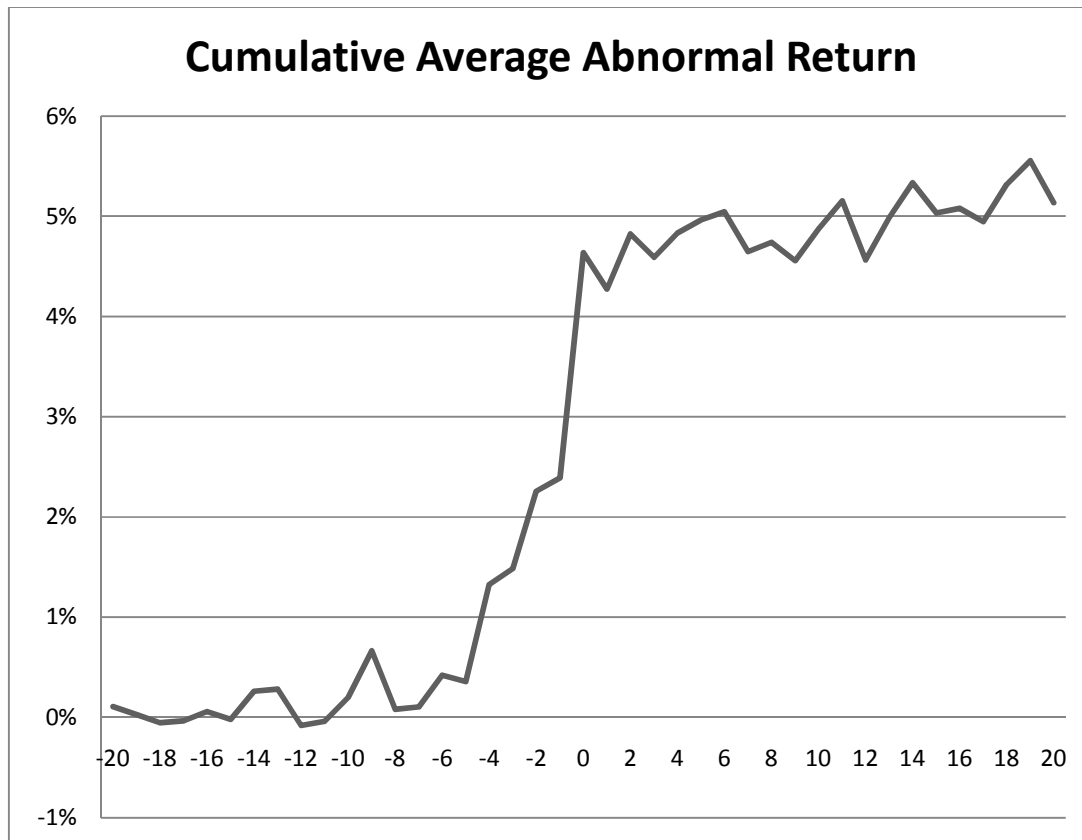
**Table 12.CAAR**

This table shows the cumulative abnormal average returns for the stock returns surrounding the activism event dates for two time intervals, namely (-4,-1) and (-20,+20). The cumulative returns are tested by using a simple t-test. \*\*\*significant at the 0.01 level; \*\*significant at the 0.05 level; \*significant at the 0.10 level.

Days	CAAR	t(CAAR)
<b>(-4,-1)</b>	0,0217	3,0608***
<b>(-20,+20)</b>	0,0636	2,1735**

**Figure 1. CAAR**

This solid line plots the cumulative average abnormal return around the event date of a hedge fund becoming active. The returns are calculated as residuals of the market model and the event date is (-20,+20)(days).



The abnormal return on the event date is 2.48%. And if I assume that the abnormal returns are independently and identically distributed and that they follow a standard normal distribution. Doing a simple t-test the null hypothesis of no abnormal performance is rejected with a confidence level of 1%.

There is a run-up of about 2.17 % between 4 days to 1 day prior to the event date. Afterwards the CAAR keeps trending to about 6.36%. So it becomes clear that there is a positive market response to the activism by hedge funds. And that this positive response only occurs after investors know what the objectives of the hedge funds are. The abnormal returns are slightly lower in comparison with the paper from Brav et al. (2008) but the jump at the event date is quite the same.

As a robustness check I also calculated the abnormal returns using the market adjusted returns method. This method assumes that the “beta” of each stock is equal to one and that the alpha is zero. Again the AAR is almost zero at the event date of the filing of a hedge fund at the AFM. The event study surrounding the activism of the hedge funds gives slightly different results than when calculating abnormal returns as residuals of the market model. The abnormal return on the event date is 2.6% and the CAAR keeps trending to about 6.1%. The abnormal and cumulative returns are slightly more significant using the market adjusted returns method. But I will report the results that I calculated using the market model; this is consistent with studies from Brav et al. (2008), Klein and Zur (2009) and Clifford (2008).



## 4. Conclusion

After doing an extensive research aiming hedge fund activism from the last decade using public information some very interesting results were found.

As expected the market response to the filing of a hedge fund did not appear to exist at all. But it does exist in the cases in which it becomes clear what the objectives of the hedge funds are. On the event date there is a 2.48% abnormal return and the CAAR after the total event window is 6.36%. So when a hedge fund becomes active in the Netherlands this is perceived as positive news and clearly investors believe that this creates value for the firm.

The financial crisis has also reached the hedge funds and this was immediately seen in the number of hedge funds that were having an interest in a company. Since 2009 only 2 new cases of hedge funds are known to me. My research eventually led to the finding of 38 different hedge funds having 41 'first time' filings from the AFM and an additional 24 cases from news searches.

The motives of the hedge funds were divided between 6 different categories. Of 20 filings I couldn't find any motives for acquiring a share in the company. The remaining 45 cases had a total of 83 motives of which a few hedge funds had even 4 motives each. When looking at all cases almost 38% was aimed at trying to change the business strategy. When the 20 filings are left out, even 47% of the cases were aiming business strategy. Changing the remuneration policy of company is no objective for all hedge funds.

A striking resemblance has been seen between the success rate of Netherlands and that of the US. In the study by Martynova and Renneboog (2010) it already became clear that shareholder protection was almost equal between the US and the Netherlands. This corresponded in the fact that the success rate for both countries is around the 40%.

Of the 36 listed companies in my database 14 of them had more than 1 hedge fund acquiring a share in the company. 10 of those were working together to achieve their goals. The average length of hedge funds holding a share in the company is 531 days. Although Brav et al. (2008) may find this long-term period, my opinion is that 531 days is still to be seen as short-term.

The average percentage voting power is initial 8.06% and the maximum average voting power is 10.10%. By looking at this data it can be concluded that hedge funds are not generally involved in acquiring controlling blocks of stock.

Due to the fact that shareholders have the opportunity to go to the OK they have a fair chance of getting their demands fulfilled. The OK likes to solve disputes between shareholders and management by taking provisional measures that will help improve the dialogue between the

two parties and as a consequence compromises will be often found. Defensive measures that are taken by the management only to oppress shareholders are prohibited and minority shareholders can change the way in which they are treated by majority holders by appealing at the OK.

## **5. Discussion**

Doing an extensively study at shareholder activism by hedge funds for the past decade is a lot and precise piece of work. But although I didn't use any private information this study gives a good insight in hedge fund activism in the Netherlands.

I did a simple event study regarding the abnormal returns surrounding an active hedge fund. While this gives some pretty nice insights I am aware of the fact that there are still some other factors that may explain the results that I get. Although I would be happy to invest some more time into looking at market responses to hedge fund activism, this would be too much work for this master thesis.

### **Further Research**

The topic of hedge fund activism still needs a lot of attention. For cases in the Netherlands the following topics could be interesting; which companies are being addressed by hedge funds?, is lowering the power of the shareholders intended by the public opinion really necessary and will hedge fund activism even come back in the Netherlands? But also as I have expressed before, the comparison between other continental Europe countries could give more insight in the hedge fund activism climate in the Netherlands.

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