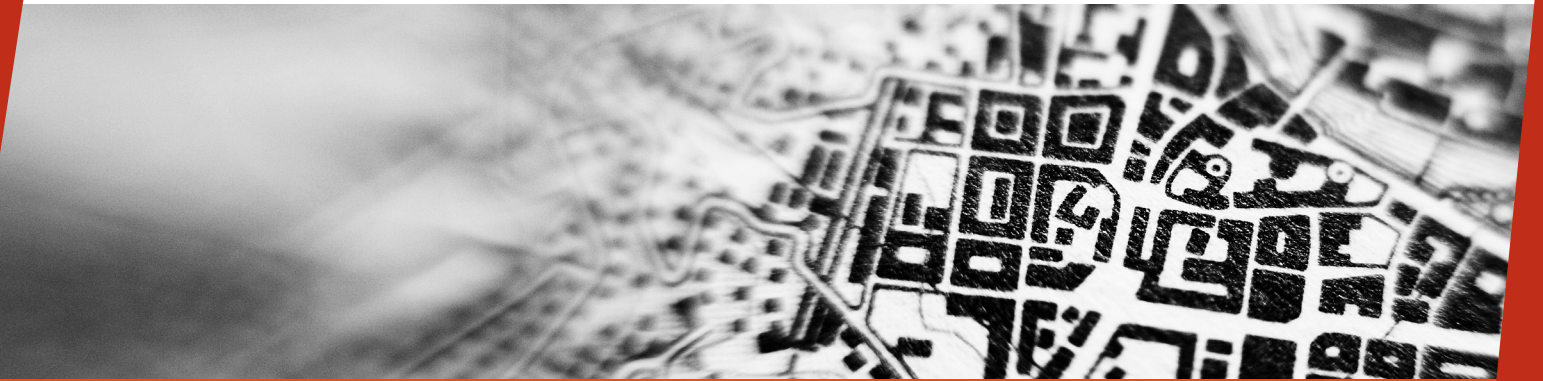


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Key Aspects of M&A Transactions in Switzerland

Contractual Aspects

The article provides an overview of the most important aspects of business acquisitions in Switzerland. While contract templates influenced by Anglo-American standards are commonly used in Swiss transactions, there are nevertheless some peculiarities of Swiss contract law which have to be taken into account. These issues are discussed in the first section below. Further emphasis is put on the rules governing public tender offers which are constantly being developed by the competent authorities. Finally, as in other jurisdictions, careful tax planning will be key to an efficient transaction, and these aspects are therefore discussed in some detail.

General Remarks

The Swiss Code of Obligations does not offer specific provisions for business acquisitions, and the general statutory provisions applying to sales and purchases largely still date from the original enactment of the Code in 1911. These rules are therefore inadequate to appropriately govern business acquisitions; this applies in particular to the statutory warranties. Therefore, it is usual for the parties to such transactions not to rely on the statutory provisions, but to instead provide a comprehensive set of rules governing their transaction in the sale and purchase agreement.

Swiss corporate transactions are heavily influenced by the Anglo-American practice, and it is usual to work with English-language contracts in international transactions. A post-graduate degree from a foreign university and practical training in the UK or in the USA are part of the job profile for young lawyers in the major Swiss law firms. Consequently, Swiss lawyers are usually well used to work with Anglo-American style transaction agreements and are familiar with the typical mechanisms to be found in such contracts (e.g. conditions precedent, closing bring-downs, comprehensive warranties, post-closing purchase price adjustments).

Due Diligence and Disclosure

Standards of Care

A thorough due diligence examination of the target company is nowadays part of the usual procedures in an acquisition. The big law firms and financial advisory companies have developed standard formats for the respective questionnaires and reports.

Since a professional due diligence must be considered to be required under the standards of commonly used care, a purchaser who waives a due diligence examination is considered negligent and cannot claim damages for defects which could have been identified in a due diligence. However, this exclusion of damage claims does not apply if and to the extent the seller has made warranties (see section "Warranties" on page 3 below).

It is also generally acknowledged that the officers of a Swiss company incur a liability risk under Swiss corporate law if they do not conduct a professionally organised due diligence with the assistance of specialised advisors before acquiring

another company. This applies even if the purchasing company is able to obtain a comprehensive set of warranties from the seller, because due to the various limitations of the seller's liability (caps, short warranty periods etc.) there remains a considerable risk that the purchaser cannot take full recourse against the seller for subsequently discovered defects.

Purchaser or Vendor Due Diligence

The due diligence will usually be conducted by the purchaser and his advisors. However, in particular in controlled auctions a vendor due diligence is not uncommon, either; the seller will then warrant the correctness and completeness of his due diligence report. Since in this constellation the advisors of the seller become liable to the purchaser for the contents of the report, they will usually seek a separate agreement with the purchaser on the limitation of their liability.

Disclosure

There is a wide variety of possibilities to contractually agree on the consequences of purchaser's due diligence findings. In particular, the parties will usually agree that only „fairly disclosed“ matters are capable of limiting the liability of the seller; in such case, it is strongly advisable to define „fair disclosure“ in the agreement in some detail, since the Swiss Code of Obligations does not explicitly mention this concept.

As an alternative, it is also nowadays quite common to require the seller to explicitly disclose all matters for which he wishes to exclude his liability, for example in a disclosure letter.

Absent any contractual agreement, the seller will not be liable for any defects which the buyer has discovered in the due diligence, or could have discovered applying due care, except however if the seller has warranted the absence of the respective defects, or has intentionally concealed them.

Due Diligence in Public Tender Offers

As a rule, a prospective purchaser who launches a public tender offer for a listed Swiss company does not have a right to be admitted to a due diligence; further, it is not permitted under Swiss stock exchange regulations to make the admission to a due diligence a condition precedent to a public offer. However, under the equal treatment rule a bidder has the right to be admitted to a due diligence (even if the takeover

bid is hostile) if and to the extent other bidders have been admitted by the target company.

Warranties

At least in larger and international transactions, it is usual to request the seller to give the warranties commonly seen in Anglo-American jurisdictions. Warranty periods of one to three years are common so that the buyer gets the benefit of one or (preferably) two full audits of the annual financial statements of the target company. Longer warranty periods are usually agreed for particularly damage-prone issues such as environmental or tax risks.

As a rule, the seller is requested to make the warranties both as of signing and as of closing. This repetition is important for the buyer, because otherwise the risk of defects passes to the buyer as of signing.

It is also usual to agree as a condition precedent that the warranties have to be accurate as of closing, sometimes with a carve-out for immaterial inaccuracies.

If a best knowledge qualification is agreed, it is important to specify the persons whose knowledge may be attributed to the seller, in particular if the seller is a legal entity, because it is not clear under Swiss law to which extent a company must accept facts known to its officers and employees as its own knowledge.

In the absence of respective contractual provisions, the buyer loses his warranty claims if he does not examine the acquired business immediately, and any warranty claims must be made within one year. Therefore, it is important to explicitly waive the statutory provisions in these areas and to instead stipulate a contractual set of rules.

Transferability of Assets

Switzerland maintains a sophisticated land register system. The direct transfer or encumbrance of real estate becomes valid only upon registration in the land register. Transactions involving shares of a real estate company, on the other hand, do not require registration. For certain restrictions applying to the acquisition of real estate by foreigners see section "Governmental Approvals" on page 4 below. While rights and, under certain circumstances, also obliga-

Regulatory Aspects

tions may be assigned and transferred without the consent of the respective debtor or creditor, contracts as a whole cannot be transferred without the approval of the other contract party. However, special rules apply to employment agreements in the sale of a business or business unit and to lease agreements for commercial premises: the employment agreements transfer to the buyer of the business if the employees do not object, and while a consent of the lessor of commercial premises to a transfer of the lease agreement is required, such consent may not be unreasonably withheld. In both cases, the transferor remains jointly and severally liable under the transferred agreements for a limited period of time.

Governmental Approvals

The Swiss regime with regard to investments made by foreigners is very liberal. In particular, there is no general authorisation requirement for foreign investments in Switzerland or for transfers of funds into or out of the country.

In some industries, a government licence is required for the operation of a business (e.g. banking, insurance, air traffic, job placement, broadcasting), but, subject to very few exceptions, it is not prohibited for foreigners to invest in those industries, even as majority shareholders or sole owners. However, many government licences are not transferable, and therefore new licences will have to be obtained if a business is acquired by way of an asset transaction. Sometimes governmental approval may also be necessary in a share transaction if the target company is active in a regulated industry (e.g. banking, telecommunications).

A special regime applies to the direct or indirect acquisition of Swiss real estate by foreigners: as a rule, only commercial real estate may be freely acquired by non-residents.

Merger Control

Swiss competition law provides for a merger control similar to most European jurisdictions. A merger or acquisition has to be notified to the Swiss Competition Commission prior to consummation of the transaction if the involved companies exceed certain turnover thresholds worldwide and in Switzerland, or if the Competition Commission has previously found that one of the involved companies is market-dominant in Switzerland in a certain relevant market. The Competition Commission may prohibit the transaction or impose conditions and limitations if it is held that the transaction would have a negative impact on Swiss competition.

Public Tender Offer Regulations

General Remarks

The Swiss Stock Exchange Law and its related ordinances also contain provisions on public tender offers for listed companies. The goals of the relevant provisions are, on the one hand, the creation of a level playing field for competing offerors, and, on the other hand, the equal treatment and protection of the interests of the shareholders of the target company.

The relevant provisions govern both voluntary and mandatory tender offers. A mandatory tender offer must, as a rule, be submitted if a shareholder exceeds the threshold of one third of the voting rights of a publicly listed company. Subject to certain restrictions, companies may raise this threshold to up to 49% (opting-up) or may completely exclude their shares from the provisions on mandatory tender offers (opting-out); both an opting-up and an opting-out must be resolved by the shareholders' meeting and must be reflected in the articles of incorporation of the company.

The obligation to submit a tender offer may also be triggered by several parties together, provided they are acting in concert. It must be noted that the competent Swiss authorities (see below) set the threshold for „acting in concert“ very low so that a group of parties may be faced with the obligation to submit a tender offer rather quickly, even if they are only connected by informal ties or only factually act in parallel.

Obligations of the Offeror

The offeror of a tender offer must treat all offerees equally. In particular, if the offeror pays a price for offer shares which exceeds the official offer price, he must offer the same higher price to all shareholders (best price rule). This obligation survives until six months after the final close of the offer.

Subject to the best price rule, the offeror is free in determining the offer price. However, in a mandatory tender offer (and in a voluntary offer which will result in the offeror's exceeding the threshold triggering a mandatory offer), the offer price must equal the higher of a) the stock market price, and b) 75% of the highest price paid by the offeror for offer shares during the twelve months preceding the offer. Consequently, it is possible to pay a control premium within certain limits.

A tender offer may be made subject to conditions. However, a condition is only admissible if its satisfaction is not substantially subject to the influence of the offeror. MAC conditions are admissible provided they comply with the materiality thresholds established by the Takeover Board; however, they may only be reserved as conditions precedent (i.e. satisfaction or waiver prior to expiry of the offer term), but not as conditions subsequent.

An offeror may file a pre-announcement of the tender offer. The date of the pre-announcement replaces the date of publication of the offer for the determination of the relevant time periods for the minimum offer price and the best price rule, and the tender offer-related obligations of the target company (see below) enter into force. In addition, the pre-announcement eliminates the ad-hoc publicity and insider trading risks related to leaks which may occur until the publication of the actual offer. Pre-announcements of tender offers are quite commonplace.

Obligations of the Target Company

During the term of the offer, the target company, and in particular its board, become subject to a number of special obligations. In particular, the possibilities to take defensive measures against unfriendly takeovers are limited; a number of actions (e.g. scorched earth defences, golden parachutes, crown jewel lock-ups) are prohibited unless they are resolved by the shareholders' meeting of the target company (but may even then still be subject to a corporate law appeal by individual shareholders). Further, competing offerors have to be treated equally, and there are limitations to the admissibility of exclusivity undertakings (no shopping or no solicitation clauses) and break-up fees.

Authorities

The most influential authority with regard to the interpretation of the Swiss tender offer rules is the Takeover Board. Its recommendations are of great importance for the tender offer practice. The recommendations of the Takeover Board are subject to review by the Federal Banking Commission, and an appeal to the Federal Court is available against decisions of the Banking Commission.

Minimum Shareholder and Officer Requirements

Currently, the majority of the board members of a Swiss stock corporation still have to be Swiss, EU or EFTA citizens with domicile in Switzerland, and – at least theoretically – the minimum required number of shareholders is three. However, both requirements will soon be abolished in the course of an upcoming revision of Swiss corporate law.

Tax Aspects

Transaction Taxes

Federal Stamp Duty

If a „securities trader“ as defined in the Federal Statute on Stamp Duties is involved in a share sale as a party or as an intermediary, the federal transfer stamp duty at a rate of 0.15%–0.3% of the transaction value is levied. In this connection, it is important to note that not only actual securities brokers in the commercial sense fall within the scope of the statutory definition of a „securities trader“, but also Swiss companies which hold more than CHF 10 million worth of securities subject to federal transfer stamp duty.

Federal issuance stamp duty of 1% is levied on the subscription price if in the course of a transaction new shares of a Swiss company are issued. The first CHF 1 million of contributions to a company are exempt from issuance stamp duty. Reorganisation exemptions may be available under certain circumstances.

Real Estate Taxes

The profits realized from the sale of real estate are taxed both at the federal and the cantonal level. In some cantons, also the profit from an indirect sale of real estate (i.e. sale of a real estate company) may be subject to the special real estate profit tax.

In addition to the real estate profit tax, most cantons levy a real estate transfer tax of usually 1–3%. However, as of July 1, 2009, the cantons will no longer be allowed to levy such taxes on real estate transfers in the course of mergers and restructurings; some cantons already now exempt such transactions from the real estate transfer tax.

Debt Push-Down

In many cases, a buyer will be interested in offsetting acquisition costs against operating profits of the acquired business. While, as a rule, no major obstacles occur in this regard in an asset deal where the business assets are bought by the entity financing the deal, a debt push-down is substantially more difficult in the case of a share transaction for various reasons.

On the one hand, the general corporate law limitations on the granting of financial assistance from a Swiss company to affiliates are rather restrictive: as a rule, any funds advanced to an affiliate (upstream loans) or assets put at risk by securi-

ties granted in favour of debts of affiliates (upstream guarantees) must be covered by the freely distributable balance sheet reserves of the Swiss company. On the other hand, substantial adverse tax consequences may be the result of such refinancing transactions if they are deemed to constitute tax avoidance or are requalified as dividend distributions. In particular, a debt-push down merger subsequent to an acquisition is likely to be regarded as a tax avoidance scheme by the Swiss tax authorities.

However, there are nevertheless a number of possibilities to at least partly achieve a debt push-down which is also accepted by the tax authorities. For instance, free reserves can be distributed and nominal capital can be repaid by the acquired company to the acquisition vehicle, but instead of settling the distribution/repayment obligation, an interest-bearing loan is created between the acquired company and its new parent. If the acquisition vehicle qualifies as a holding company for Swiss tax purposes, it will benefit from a preferential tax rate on its interest income from the loan, whereas the borrower can offset its interest expenses against ordinarily taxed income.

It may even be possible to directly assign at least part of the acquisition debt to the acquired company against credit. The interest rate charged on that credit must be above a certain safe harbour threshold set by the tax administration, but it will usually still be possible to fix this interest rate considerably lower than the rate of the interest on the acquisition debt so that the net effect is a partial set-off of the acquisition financing costs against operative income of the target.

Further, if a group of companies is acquired, it should be examined whether in a first step an operative subsidiary of the target group can be acquired and subsequently be used as the acquisition vehicle for the rest of the group so that part of the acquisition debt is incurred by that operative subsidiary.

In all of these constellations, it is of utmost importance to obtain advance rulings from the competent Swiss tax authorities in order to make sure that they accept the acquisition structure and the contemplated tax benefits.

Financing Rules

Swiss thin capitalisation rules set certain maximum thresholds

for the debt financing of various types of assets. For instance, participations may be debt-financed by a maximum of 70%. If and to the extent these thresholds are exceeded, interest payments on loans from affiliates cannot be offset as business expenses against taxable profits of the borrower, and these interest payments are treated as constructive dividends and therefore subject to Swiss withholding tax.

The federal tax administration regularly publishes the admissible maximum interest rates for loans from affiliates. Again, interest payments exceeding these safe harbour limits are as a rule not admitted as business expenses and are treated as dividends for Swiss withholding tax purposes.

Repatriation of Profits

With a careful balancing of debt and equity financing of the acquisition, a tax-efficient repatriation of profits is usually possible.

Subject to compliance with the thin capitalisation rules and the guidelines of the tax administration on maximum interest rates on loans from affiliates (see section "Financing Rules" above), a Swiss company may deduct interest payments on loans from affiliates as business expenses from taxable profits. Repayments of debt principal can be made tax-neutral from a Swiss tax point of view.

Dividend payments are subject to Swiss withholding tax; however, Switzerland maintains an extensive network of double taxation treaties under which the withholding tax can be partly or fully reclaimed. Foreign tax credits may be available for any non-refundable part of the Swiss withholding tax. Usually, a minimum substance will be required in the domicile jurisdiction of the dividend recipient in order for the double taxation treaty benefits to be available; however, these requirements are not very high, and compliance can be confirmed with the Swiss tax authorities in an advance ruling. In this connection, it is interesting to note that an acquisition structure with a Luxembourg subholding can be used to avoid the real estate profit tax on the sale of a Swiss real estate company (see section "Real Estate Taxes" on page 6).

Finally, it should be noted that the European Union Parent-Subsidiary Directive also applies to Swiss companies, even though Switzerland is not a member state of the EU.

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