# Switzerland

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## General overview

**What legislation governs M&A activity in Switzerland?**

M&A transactions are governed by the Swiss Code of Obligations and, depending on the acquisition structure, the Swiss Merger Act. Acquisitions of participations in listed companies, both friendly and hostile, are also governed by the Swiss Act on Stock Exchanges and Securities Trading (the SESTA). The Swiss Antitrust Statute applies if the turnover of each of the parties involved exceeds certain thresholds.

If a transaction structure provides for the issuance of new securities by an issuer listed on a stock exchange, the listing rules of that stock exchange apply.

**What impact have recent legislative changes had on the nature and amount of M&A activity?**

A big issue for tax practitioners in the M&A area has been the so-called *successor holding company decision*, which further extends a theory introduced in the 1980s by the Swiss Federal Supreme Court referred to as *indirect partial liquidation*. Essentially, a debt-financed sale of a company from an individual to a corporate acquirer may be treated by the tax authorities as a *de facto* liquidation of the target company, triggering dividend-type taxation for the seller on the entire equity of the target to the extent it exceeds the nominal capital, that is, retained earnings (including unrealized and so undisclosed reserves). The Supreme Court's unexpected and shocking decision rendered the sale by one or more individuals to a legal entity difficult, if not impossible, prohibiting the possibility of a smooth transition of a family business to the next generation or to a new owner if the acquirer (or its lenders) rely on the assets and/or the cash flows of the target company (rather than those of the buyer) to finance the acquisition. If certain criteria are met, the theory of indirect partial liquidation allows the tax authorities, independent of any actions of the seller after the transaction and even years after the sale, to re-qualify the (otherwise tax-free) capital gain from the sale of the shares into dividend income subject to income tax. Because share purchase agreements regularly provide for an indemnification clause that states the purchaser has to hold the seller harmless from any income tax levied on them based on this theory, the tax burden is often shifted to the purchaser in case income tax is levied.

The detailed wording of the provisions relating to indemnification sought by sellers and the allocation of risk relating to any further changes of assessment practice of, or extension of the theory by, the tax authorities after the sale more often than not became the subject of lengthy negotiations and drafting debates involving both corporate as well as tax specialists. The restrictions stemming from these indemnification provisions affect the acquirer's ability to restructure the target after the acquisition: the acquirer is limited in transferring parts of the acquired business to other entities of its group and in most cases cannot merge with the target within a five-year blocking period, while a merger between the target and a down-stream affiliate entity can be arranged if certain criteria are met.

As a reaction to the Federal Supreme Court decision and the restrictive guidelines of the tax authorities published shortly after, the federal parliament proposed and adopted new legislation in 2006 providing for a less extensive application of the theory of indirect partial liquidation, which came into force on January 1 2007.

The new legislation provides that the theory of indirect partial liquidation will be applied if: (i) shares representing at least 20% of a target company are sold; and (ii) within five years after the share sale, assets not necessary for the operational business of the target (in practice often excess cash or cash equivalents and non-operational real estate) are distributed to the acquirer. As a further requirement the assets not necessary for business operation (or their replacement assets) must have been held at the time of the transaction and the target company needs to have been in a position (according to the applicable provisions of corporate law) to distribute the assets to the shareholders before the transaction.

The new legislation adopted certainly has a positive effect on the legal certainty of both seller and acquirer in a share sale transaction, but some restrictions remain. In particular, the acquirer will in many cases not be able to merge with the target in the five years after the sale, and the acquirer's plans to restructure the target and its business will require detailed review and scrutiny. Under the new draft guidelines issued by the federal tax authorities implementing the new law, certain issues still remain unclear, for example, to what extent undisclosed reserves on certain assets not necessary for the operational business have to be (even though under corporate law not technically distributable) taken into consideration. Another still-debated issue is the fact that the draft guidelines apply the theory also to the acquisition of listed shares, for example, to sales in a public offer. If the tax authorities maintain this view, tender offers could be negatively affected because, due to the aggregation of all shares sold in a transaction when calculating the 20% trigger threshold, private shareholders (even those holding less than 20%) tendering their shares would be exposed to severe tax consequences depending on the acquirer's structuring of the transaction and so might prefer not to tender their shares.

Given the uncertainty in the application of the new law and the guidelines of the tax administration, any proposed transaction structure should be discussed with the tax authorities beforehand and confirmed in a binding tax ruling.

Further legislative action relates to the disclosure rules regarding interests held by a potential acquirer in a listed company. The federal parliament is discussing (and has already partly approved) a proposal that would force investors to reveal their interest once they buy 3% of a target's shares. This proposal was triggered by intense takeover activity and speculation mainly in the industrial sector. Current regulations allow investors to remain incognito as long as they buy less than 5% of a target's voting shares and less than another 5% in call options entitling them to acquire voting shares. This regime has been heavily criticized, because the combination of long positions and option positions allows a potential acquirer to control up to 10% of the voting shares without having to disclose their identity, making it too easy for speculators to gain an important interest in the target before the market and the target become aware of the move and before the target can prepare a strategy to fend off a hostile takeover bid. A connected issue to come under scrutiny are the disclosure requirements relating to cash settled options because this type of options has been used by potential acquirers in recent

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## Author biography


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Alexander Vogel is a partner and heads Meyer Lustenberger's M&A/corporate group. He regularly advises companies and financial institutions on cross-border mergers and acquisitions, public takeovers, banking and finance, corporate law and corporate governance, investment companies and international business transactions. Alexander Vogel graduated from the University of St Gallen and obtained a Master of Laws from Northwestern University School of Law. He is a member of the Swiss Bar and is a notary public.

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transactions to build up and *de facto* control larger quantities of shares in a target without having to disclose their interest.

The new Merger Act entered in force in mid-2004 and provides for a comprehensive set of rules relating to mergers, demergers, reorganizations of entities and asset deals. Since its introduction, a number of issues have been resolved or at least clarified, increasing planning and legal certainty in transactions based on the new law, for example, when using a squeeze-out merger where minority shareholders can be forced based on a 90% majority vote of all outstanding shares (rather than the 98% majority provided for in the SESTA) to accept cash or a cash equivalent as consideration instead of shares in the surviving entity.

**What have been the most significant M&A transactions in Switzerland over the past year?**

In general, the volume of M&A transactions increased in 2006 compared with 2005, while the absolute number of M&A transactions has slightly decreased. The percentage of cross-border transactions slightly increased in 2006. Important transactions of Swiss targets by foreign acquirers include the acquisition of Winterthur insurance group by the French insurance company AXA Group from Credit Suisse Group for about SFr12.3 billion ($10.2 billion), the acquisition of Serono by German Merck KGaA from the Bertarelli family and the minority shareholders for SFr16.6 billion, and the acquisition of SR Technics Holding by Dubai Aerospace Enterprise from 3i Group for about SFr1 billion. Swiss companies were also active on the M&A scene: by far the largest transaction was concluded by Xstrata Zug, which acquired Canadian Falconbridge for $19.2 billion. Other important transactions of Swiss acquirers acquiring foreign targets with purchase prices exceeding SFr1 billion include the acquisition of GE Insurance Solutions by Swiss Re from General Electric Capital Corporation (SFr11.56 billion), the acquisition of Chiron Corp by Novartis, the acquisition of Vodafone Group's 25% stake in Swisscom Mobile by Swisscom, the acquisition of GN ReSound by Phonak Holding and the acquisition of ICI Chemicals & Polymers´Quest division by Givaudan. Among the substantial number of acquisitions of Swiss companies by Swiss acquirers, the acquisition of Novartis' nutrition division by Nestlé for about SFr3 billion and the acquisition of the discounter chain Denner by retailer Migros need to be mentioned.

Among various public tender offers, there were also in 2006 a few hostile offers: SWX-listed companies Saurer, Bank Lindt and SIG were the targets in these takeovers battles. The takeover bid by OC Oerlikon Corporation (formerly Unaxis Holding, and who was itself the target of a successful hostile acquisition by Austrian Victory Industriebeteiligung in 2005) on Saurer successfully ended after a long defence battle of the board of directors, although at a much higher price than originally offered by OC. The hostile offer by Glarner Kantonalbank on Bank Lindt failed due to the resistance of the target's board of directors and a more attractive bid submitted by a white knight selected by the board (Liechtensteinische Landesbank). Also the hostile offer of Ferd and CVC Capital Partners on SIG Group was successfully challenged by Rank Group Holdings acting as a white knight.

Other public tender offers include the going private of Mövenpick-Holding and X-Rite's offer for the shares of Amazys Holding.

**How, and to what extent, is foreign involvement in M&A transactions in Switzerland regulated or restricted?**

In general, foreign investors acquiring an interest in a Swiss business (by way of a share purchase or an asset deal) face few restrictions and limited requirements to obtain government authorization to carry out an acquisition. Exceptions apply for certain regulated industries, mainly in the area of banking and finance, for example, relating to the acquisition of banks, securities dealers or asset management companies, where special approval requirements or notification obligations apply. Similar restrictions apply to the acquisition of a substantial interest in a Swiss insurance company.

In an asset deal transaction, certain restrictions and/or approval requirements stem from the fact that the legal entity conducting the (acquired) business changes and certain permits, concessions or public franchises cannot be transferred from the selling entity to a new entity. Further restrictions govern the acquisition of real estate in Switzerland by foreigners to the extent the real estate is not used, or intended to be used, for commercial purposes, that is, mainly residential property and farm land. The relevant legislation is under revision and should be further liberalized.

## Due diligence

**What are the principal disclosure requirements in a typical M&A transaction?**
The rules for private transactions are set out in the Code of Obligations. The seller's disclosure obligations under the Code are limited and depend on the circumstances, that is, the negotiations between the parties, the contractual disclosure obligations and the reliance of the buyer in the statements of the seller according to the principles of good faith.

In a private M&A transaction, extended disclosure is usually granted once the prospective acquirer has entered into a confidentiality agreement. The documents to be disclosed are either prepared based on a due diligence request lists provided by the acquirer or according to the secrecy needs of the seller that prepares a data room. The latter is typical in an auction procedure.

While privately held companies do not have to file or disclose any financial information, corporations, whose shares are listed on a stock exchange or that have issued bonds, are obliged to publish the annual financial statements and (if applicable) the consolidated financial statements. Companies listed on a stock exchange are also required to comply with various additional disclosure obligations. In particular, they are obliged to publish any changes with respect to its significant shareholders within two days after receipt of the information and to immediately disclose any price relevant information (*ad hoc* publicity).

Further, listed companies must publish an interim financial report at least semi-annually and a comprehensive business report annually. The business report contains the board's annual report, the auditors' report, the audited financial statements, information relating to corporate governance and shareholders and organized groups of shareholders holding more than 5% of the company's share capital.

If a transaction includes the issuance of new equity or debt instruments to be listed, the prospectus and listing requirements of the relevant stock exchange apply. In a public offer, the content of the offering prospectus is regulated in detail by the SESTA and its implementing regulations, and its accurateness and completeness must be confirmed by an independent auditor.

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**How significant an issue is prospectus liability in a typical M&A transaction?**
So far, prospectus liability has not played any significant role in M&A transactions in Switzerland, although the content of the offering prospectus to be used in a pubic tender offer is regulated in detail by the SESTA and its implementing regulations.

The SESTA does not determine the consequences of a violation of its rules relating to the content of the prospectus. According to the prevailing view, the liability of an offeror would have to be determined according to the general rules relating to prospectus liability stipulated in the Code of Obligations. Based on these provisions, any person or legal entity that is directly or indirectly responsible for an incorrect prospectus is liable for the damages caused by its action or omission. In a recent case the Federal Supreme Court confirmed that the plaintiff has the burden of proof to show that they relied on a particular wrong or misleading statement in the prospectus when entering into the transaction at issue and that, under Swiss law, there is no statutory or legal presumption for the benefit of the plaintiff assuming this reliance that would have to be rebutted by the defendant.

**How have recent M&A transactions and/or legislation dealt with the issue of material adverse change clauses?**
In private transactions it is common practice for the buyer to request the inclusion of a material adverse change (MAC) clause to limit the buyer's risks resulting from changes in the period between signing and closing, because the default provisions of the Swiss Code of Obligations put that risk otherwise on the buyer unless the buyer can claim an error, fraud or duress or request the application of the *clausula rebus sic stantibus* rule. The form and content of a MAC clause vary depending on the nature and size of the transaction. Considering the seller's market in recent years, buyers in certain cases had to accept, and have accepted, clauses that were limited in their reach and provided only limited comfort. In general, there are no legal restrictions relating to the content of a MAC clause and the parties are free to narrow or widen the scope of the clause according to their bargaining power. The clause usually gives the purchaser the right to pull out of the deal and walk away from an acquisition or at least to renegotiate the terms of the transaction before closing if events occur that are detrimental to the target company.

In voluntary public tender offers, the Takeover Board considers MAC clauses admissible to the extent that they do not grant the offeror the possibility to cancel the offer based on a small deterioration of the target's results and give the offeror a decisive control whether or not the condition is fulfilled. The Takeover Board requires that a MAC clause be based on meaningful thresholds. In its recent decisions, the Takeover Board concluded repeatedly that MAC clauses providing for a threshold of 10% relating to EBITA or turnover are acceptable, while a threshold of 5% relating to equity or to turnover were considered to be borderline cases. Conversely, in a mandatory tender offer, MAC clauses are not allowed.

**What are the key unresolved issues in your jurisdiction?**
One of the main unresolved issues relating to M&A transactions relates to the limitations of financial assistance granted by the target company to the acquirer in the form of loans or guarantees. It is generally accepted that upstream or cross-stream guarantees (or loans) by a target company in favour of the acquiring new parent company or one of its affiliates will only be granted against adequate consideration based on market conditions and to the extent the parent company has the financial capacity to repay their loans. However, there is a debate to what extent (even if the above mentioned conditions are met) the target's ability to grant financial assistance is further limited to the amount of it's freely disposable shareholder equity and, if so, at what point the freely disposable equity should be determined: (i) at the time the guarantee or loan is granted; (ii) at the start of the proceedings for enforcement; or (iii) at both times, whereby the lower amount is relevant. It is also debated whether the amount needs to be determined by the target's auditors on the basis of an audited annual or interim balance sheet and if the amount to be paid by the target needs to be approved as distribution by a duly convened meeting of the shareholders of the target. Court decisions provide little guidance on these issues, so practitioners will continue to struggle to find a balance between legal certainty and practical solutions.

**“Practitioners will continue to struggle to find a balance between legal certainty and practical solutions”**

## Public takeovers

**Are there any specific regulations and/or regulatory bodies governing takeovers in Switzerland?**
Public tender offers on issuers listed on an exchange in Switzerland are governed by the Federal Act on Stock Exchanges and Securities Trading (the SESTA). Pure merger transactions, however, are not subject to the provisions of the SESTA, but to those of the Merger Act referred to above. The SESTA defines when a purchaser is required to make a mandatory offer for all outstanding equity securities of a target, which is the case if an acquirer directly or indirectly controls more than 33.3% of the company's voting rights. Exceptions apply if the target had increased this threshold in its articles of incorporation to 49% (opting up) or if they contain an opting-out clause

Once a public offer has been pre-announced, the board of the target may not take any defensive measures that could significantly alter the assets or liabilities of the target but rather has to submit such measures to the shareholders' meeting for approval. The board is also not allowed to issue shares based on authorized share capital without granting subscription rights to the existing shareholders, except in limited cases. The target may not enter into incentive plans, severance agreements or similar arrangements with members of the board or senior management with unusually high compensation.

Compliance with the rules provided for in the SESTA is supervised by the Takeover Board, which issues binding recommendations. Any recommendation rejected by one of the parties can be brought to the Federal Banking Commission for review. The Commission can also issue binding administrative orders if the Takeover Board's recommendations are not complied with by any party. Any party can make an appeal to the Federal Administrative Court against decisions of the Federal Banking Commission and, failing that, against the Court's decisions to the Federal Supreme Court.

The Swiss Antitrust Statute provides for a preventive merger control procedure led by the Swiss Merger Control Commission if a transaction exceeds certain minimal thresholds.

**What are the thresholds for disclosing an interest?**
Shareholders and groups of shareholders acting in concert have to report to the issuer and the relevant stock exchange purchase or sale transactions as well as certain derivative positions in a Swiss company listed on an exchange in Switzerland, if they reach, exceed or fall below the thresholds of 5%, 10%, 20%, 33.33%, 50% or 66.66% of the voting rights. During a public tender offer, further disclosure obligations relating to transactions in the shares of the target (and in an exchange offer, the offeror) apply.

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