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Private Equity

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1. Trends

1.1 M&A Transactions and Deals

The Swiss M&A market enjoyed a long phase of growth, which culminated in mid-2018. This strong market was, in particular, driven by historically cheap acquisition financing and a favourable tax environment. In addition, the Euro crisis caused a significant and enduring appreciation of the Swiss franc against the euro and thus increased the prices of Swiss goods and services. The Swiss export industry responded by significantly increasing its technological edge and competitiveness. This both facilitated the acquisition of foreign targets and made Swiss companies attractive to international investors.

The M&A climate was still positive in 2019, which saw a series of significant transactions, including the USD10.2 billion sale of Nestlé Skin Health SA from Nestlé to EQT and the Abu Dhabi Investment Authority, and the USD4.7 billion acquisition of Panalpina Welttransport Holding AG by its Danish competitor DSV AVS. Studies report a total deal volume of USD160 billion and approximately 400 major transactions for 2019.

Overall, recent years saw a seller's market, characterised by high valuations and more seller-friendly deal terms.

Unsurprisingly, COVID-19 caused a sharp reduction in the number of transactions. Beside the initial economic shock and the increased insecurity, access to acquisition financing today is proving more difficult. Strategic buyers have taken a very cautious approach and increased their cash reserves, making less of their own funds available for acquisitions as well. The situation also affects private equity houses, which are more absorbed with the management of their portfolio companies.

However, the transformed market also presents opportunities. First, the lower valuations represent opportunities for investors who still have the financial means and risk appetite for acquisitions. Also, SMEs still form the backbone of the Swiss economy and a larger amount of M&A deals involve succession planning, a task that in some cases moved up in priority in view of COVID-19. Such investment opportunities will continue to arise. Accordingly, initial surveys show that despite COVID-19, slightly more than 50% of Swiss companies are still contemplating an acquisition in the next 12 months.

1.2 Market Activity

Switzerland has, in relation to its overall economy, one of the largest industrial sectors in Europe. Pharma, IT and other hi-tech companies as well as logistics are key industries. In addition, a growing and dynamic start-up and venture capital ecosystem helps in the building of further successful companies in these areas. Accordingly, an increasing number of M&A transactions cover pharma and biotech, innovative IT and software, as well as other hi-tech businesses.

Private equity houses have a strong footprint on the Swiss market and were involved in a large number of transactions in 2019. The impact of COVID-19 on their market activity is not yet fully clear.

In any case, it is expected that COVID-19 will lead to an increase of distressed M&A and restructuring transactions, in particular in the machinery industry. Over recent years, Swiss companies already had a certain tendency to focus on specialisation and divestiture of non-core businesses. It seems probable that this trend will accelerate, and that the market will see a higher number of carve-out transactions and potentially also asset deals, by which sellers will dispose (only) of selected business unity or divisions.

A further trend is that the Swiss market, which is historically highly integrated in the world economy, is becoming even more international, with a share of approximately 70% of transactions involving a foreign part in 2019. However, it is not yet clear if and how this trend will continue in an economy affected by COVID-19.

2. Legal Developments

2.1 Impact on Private Equity

For the time being, there are no general restrictions on foreign investments in Switzerland (see, however, **3. Regulatory Framework** with respect to certain limitations regarding the acquisition of residential property).

However, the Swiss Parliament is debating a law that would generally make foreign investments subject to a certain level of state control. The legislative work has just begun, and it is as yet unclear what kind of notification or approval requirements may be introduced. The legislative measures are commonly seen as a consequence of the acquisition of Syngenta, a Swiss-based global leader in agrochemical and seed products, by ChemChina.

Furthermore, the Federal Act on Financial Services (FINSA) entered into force on 1 January 2020. The new law considerably widens the regulatory framework for financial service providers – in line with international trends, such as MiFID II in the European Union that led to licensing and supervision requirements for, eg, asset managers of private wealth or trustees. For instance, FINSA rules that not only (as previously) public offerings of newly issued shares or bonds are subject to prospectus obligations. Rather, under the new law, a prospectus has to be

established essentially for all public offerings of securities (ie, also for offerings of previously issued securities).

However, FINSA also contains certain administrative simplifications. For instance, as under the previous law, foreign collective investment schemes that are only offered to qualified investors in Switzerland do not require a financial market licence. However, for such foreign investment products, it was previously necessary to maintain a particular payment agent (who needed to qualify as a bank with a respective licence) in Switzerland. This requirement does not prevail any more if the foreign investment product is offered only to professional investors and, in addition, not to high net worth individuals. This may considerably ease the fundraising of foreign private equity houses in Switzerland.

3. Regulatory Framework

3.1 Primary Regulators and Regulatory Issues

Private equity funds incorporated in or managed from Switzerland are, to the extent that they are not organised as an exempt investment company or SICAF, generally considered as collective investment schemes, which are subject to the Federal Act on Collective Investment Schemes (CISA) – and do thus require a licence from FINMA. The Swiss CISA legislation is sometimes perceived as slightly burdensome. As a result, and despite the tax-friendly environment, most private equity fund vehicles are incorporated or set up in foreign jurisdictions.

The Federal Act on Acquisition of Real Estate Properties by Foreign Persons (so-called Lex Koller) states that the acquisition of residential properties in Switzerland by foreigners is, in general, subject to state approval. The scope of application of the Lex Koller is rather broad and, eg, also includes the acquisition of shares in non-listed real estate companies and of mere construction rights to the extent relating to non-commercial properties. In order to avoid complications for the acquisition process, the purchaser should thus carefully assess if the target company owns any property, right or share that would trigger the applicability of the Lex Koller.

The Federal Cartel Act (CarA) applies to every “concentration of undertakings” (including mergers and acquisitions). The financial thresholds triggering the obligation to notify the Swiss antitrust authority are, however, relatively high. Subject to certain exceptions (eg, in the case of an established market dominance), these are:

- the undertakings concerned together have a turnover of at least CHF2 billion, or a turnover in Switzerland of at least CHF500 million; and
- at least two of the undertakings concerned each have a turnover in Switzerland of at least CHF100 million.

Swiss takeover law needs to be complied with for the acquisition of listed companies (see **7. Takeovers**).

4. Due Diligence

4.1 General Information

The trend is towards more succinct due diligence procedures. Depending on the circumstances, the seller typically allows two to four weeks for the process.

Accordingly, it has become more important to proceed to a clear scoping: before the due diligence, the buyer and its advisers proceed to a preliminary assessment of the target’s business and the related risks, and determine which areas should be reviewed at what depth. It is also common to define clear materiality thresholds. Reports are usually issued as summary red flag reports, which only list material issues and include respective recommendations.

Especially in auction processes, it is not rare that buyers submit a first, non-binding offer on the basis of a preliminary due diligence. In a second phase, the remaining interested parties are allowed slightly more time to conduct a confirmatory due diligence. Usually, more confidential information is then only disclosed in this second stage. Sellers may require that only a “clean team”, which is subject to stricter non-disclosure obligations and clearly separated from the operative organisation of the potential buyer, accedes such classified information.

Almost any due diligence covers the following key topics: ownership of the seller(s) in their shares in the target company, the target company’s IP rights and IP-related arrangements, employment and real estate matters, key contracts, as well as litigation. In recent years, depending on the business model, data protection has also become an important area of review. The further areas of review depend both on the target’s industry and the deal structure. For instance, in tech transactions, particular attention is paid to IP and IT matters, and in biotech deals, regulatory matters (eg, import and export restrictions or licence required to carry out certain clinical tests) play an important role.

Post-closing integration measures are particularly important if the target is to be integrated into a group post-closing. Thus, in such transactions, particular attention is paid, eg, to possibilities of early termination of long-term contracts in the due diligence phase.

4.2 Vendor Due Diligence
The use of vendor due diligence depends on the size and type of the transaction and on the target company's business.

Vendor diligences are more often carried out in bigger transactions involving an auction process. The availability of a vendor due diligence report is then often used as a means to streamline and shorten the bidder's own due diligence process, by limiting the time allowed for it. In certain cases, it may also allow a wider group of potential buyers to be attracted, since the available information allows better assessment of the risks related to the business of the target.

It is also common to see vendor due diligence reports if certain of the target's operations or assets will require a deepened review carried out by highly specialised service providers. This can, for instance, be the case if the target company owns real estate properties that are expected to be subject to contaminations. In such cases, a specialised firm frequently proceeds, eg, to soil analyses, allowing the seller to make its report available to selected potential buyers, often in a second stage.

The level of credence allowed to vendor due diligence reports depends essentially on the author/provider and the level of the reliance given. If appropriate reliance is granted by a reputable service provider, the buyer will usually rely on the reports to a certain extent.

Regarding buy-side diligence reports, the advisers are, under Swiss law, responsible and liable by law for their reports towards their client; ie, the buyer. However, diligence reports are often subject to rather extensive disclaimers and qualifications (eg, regarding the limited areas of review, materiality thresholds or the fact that contracts subject to foreign law have only been subject to a high level review, if at all).

5. Structure of Transactions

5.1 Structure of the Acquisition
In the case of a private target company, most transactions are executed by way of a share purchase agreement.

Fewer transactions are structured as asset deals. In the current environment, asset transactions are, in particular, chosen in distressed situations, if the purchaser only wants to acquire certain (profitable) parts of a business. The tax implications of an asset deal should be explored in detail. In particular, Swiss tax law provides that in certain situations the purchaser may also become liable for certain of the seller's taxes in the event of an asset deal ("tax successor liabilities"). Depending on the circumstances, it might be recommendable to obtain a tax ruling before the transaction.

Swiss law also provides for the possibility of a statutory merger or a "bulk transfer"; ie, the transfer of certain parts of a business (together with the related assets, liabilities, contracts, employees, etc) to the purchaser as a whole. While few acquisitions are carried out by way of merger, mergers are sometimes used for a restructuring before or after an acquisition. Bulk transfers are frequently used to implement an asset deal or a "pre-packaged" share deal; ie, the transfer of all of the assets, employees, agreements and customer relationships in a spin-off entity set up in view of the potential sale.

The acquisition terms are more seller-friendly in the event of an auction sale. In particular, the warranty protection is less extensive (fewer warranties, lower cap, etc). Fewer and lighter closing conditions are implemented, as well. It has, for instance, become rare to see a "material adverse change" clause in an auction transaction.

If the target is listed in Switzerland, the acquisition must be effected by way of a public tender offer, in compliance with the financial market regulations (see **7. Takeovers**).

5.2 Structure of the Buyer
The private equity fund vehicle rarely acts as the purchaser. Rather, private equity funds regularly establish one or more holding companies. One of these companies then establishes a new special-purpose company (SPV), in Switzerland or abroad, which acts as purchaser. A Swiss SPV is, in particular, needed if the acquisition is carried out by way of a merger, given that cross-border mergers are quite cumbersome.

The fine-print of the acquisition structure is mostly tax-driven. Important considerations are the general tax environment in the jurisdictions of the holding company and the acquisition SPV, and, even more importantly, the availability of double tax treaties, allowing for a tax-optimised flow of dividends and sale proceeds to the fund, and ultimately its investors. Luxembourg is a typical European jurisdiction for such holding companies and/or acquisitions SPVs.

5.3 Funding Structure of Private Equity Transactions
Normally, private equity transactions are at least partially debt-financed. The exact structuring of the financing package depends primarily on the acquisition's financial model and the size of the transaction.

A larger transaction usually involves a higher amount of (senior and junior) debt financing. The senior debt is provided as

a secured bank loan, which may be granted by one bank or, in some cases, a bank syndicate. The senior lenders normally require a comprehensive set of collateral, which also covers the assets of the target company. However, a Swiss company can only make any payments under such upstream securities up to the amount of its freely distributable shareholder equity. Additional formal requirements have to be complied with, as well.

The junior debt is often provided by less risk-averse financiers, such as investment funds specifically set up for this type of investment. The junior debt is usually provided in the form either of a subordinated loan with a higher rate of interest or a mezzanine financing, involving a convertible instrument.

The relationship between the senior and the junior lenders is often regulated in an intercreditor agreement.

Equity commitment letters issued by the fund, as well as proof of fund letters issued by the acquisition banks, are becoming more frequent in private equity transactions.

Private equity investors usually acquire a majority participation that allows them to direct the target company's business both at shareholder and board level. In certain circumstances, the fund may opt for a minority investment, if it provides for the same level of control (eg, if the remaining shareholding is fragmented).

5.4 Multiple Investors

Although not very common in Switzerland, syndicates of several private equity funds (or other financial investors) are seen in larger transactions. A recent example of a co-operation by two financial investors (EQT and the Abu Dhabi Investment Authority) was in the USD10.2 billion acquisition of Nestlé Skin Health SA.

The Swiss M&A market is familiar with the concept of "investment clubs" or similar collaborations, where, eg, family offices or high net worth individuals acquire a stake in a company alongside a private equity investor. These investors are often independent third parties not otherwise affiliated to the fund.

6. Terms of Acquisition Documentation

6.1 Types of Consideration Mechanisms

Both locked-box and completion accounts mechanisms are common in private equity transactions. However, a private equity deal with fixed price is rarer.

When investing in a target company, private equity funds might demand to have a completion accounts mechanism in place, which allows a purchase price adjustment, and can therefore be to the advantage of the buyer. On the other hand, private equity funds as sellers tend to prefer locked-box mechanisms because this mechanism ensures a price certainty (provided that there is no leakage).

Currently, since the market is still rather a seller's market (although things might change during the second half of 2020 due to the COVID-19 pandemic), one sees a large number of deals with locked-box mechanisms.

Earn-out clauses are also very common, especially when the seller is the founder of the target company and remains an employee of the company post-closing.

6.2 Locked-Box Consideration Structures

When locked-box consideration structures are used, is it common that private equity buyers pay an amount corresponding to a percentage of the purchase price between the date of the locked-box accounts ("locked-box date") and the signing or the closing date of the acquisition agreement. In the authors' experience, this percentage has varied, in recent years, between 1% and 5%.

6.3 Dispute Resolution for Consideration Structures

When a completion accounts structure is chosen by the parties, it is quite common to have a specific dispute resolution mechanism in place. Usually, the parties shall designate an expert, which is frequently an audit firm, which will determine the final and binding closing accounts and/or the amount of the purchase price adjustment.

On the other hand, in the case of a locked-box mechanism, there is usually no specific dispute resolution mechanism in place to determine, eg, if there has been a leakage, and in the case of disagreement, the parties would ultimately have to initiate court or arbitration proceedings in accordance with the general dispute resolution clause of the share purchase agreement.

6.4 Conditionality in Acquisition Documentation

It is common that the closing of a transaction is conditioned to the realisation of certain conditions ("Conditions Precedent to Closing").

It is typical to see Conditions Precedent to Closing related to regulatory approvals (see also **6.5 "Hell or High Water" Undertakings**).

Other Conditions Precedent to Closing are also often added to the share purchase agreement, such as financing, board approval, or third-party consents. Depending on the deal, third-party consents can be key Conditions Precedent to Closing; for example, when essential agreements contain a clause of change of control and the buyer wants to make sure that such agreements remain in place post-closing.

On the other hand, material adverse change provisions ("MAC Clauses") have been less and less common lately because sellers rarely accept these types of clauses. Therefore, in auction processes, a private equity bidder would rarely suggest adding MAC Clauses to the share purchase agreement for fear of not winning the auction.

6.5 "Hell or High Water" Undertakings

"Hell or high water" undertaking clauses are not common in Switzerland. Usually, notifying the transaction to the Competition Commission (or obtaining a ruling from the Competition Commission that notification is not necessary) is the seller's responsibility. However, the buyer is usually involved in the process and the parties sometimes even agree that the wording of the communication with the Competition Commission must be approved by the buyer beforehand.

In any event, the notification thresholds are rather high in Switzerland, so that merger clearance is not always an issue in private equity transactions.

6.6 Break Fees

In Swiss private equity transactions, there is almost always the possibility to terminate a transaction agreement prior to closing in the event that a Condition Precedent to Closing has not been fulfilled within a certain date ("Long Stop Date").

Usually, if the transaction agreement is terminated prior to closing, such termination shall be without liability of either party. However, if such termination is the result of the wilful or grossly negligent misconduct of one party, such party shall be liable to the other party for damages as a result of such misconduct.

Sometimes, when the buyer terminates the transaction agreement prior to closing, because the seller has not fulfilled a Condition Precedent to Closing, break fees – or liquidated damages – shall be paid by the seller. The break fees seek to protect the buyer for the time, resources and cost already poured into the process.

Reverse break fees – ie, break fees paid by the buyer to the seller – are seen in private equity transactions; eg, in the event the private equity buyer has not obtained the financing. However, reverse break fees are rarer.

6.7 Termination Rights in Acquisition Documentation

An acquisition agreement can be terminated prior to closing by the seller or buyer if the Conditions Precedent to Closing have not been met prior to the Long Stop Date (see also **6.6 Break Fees**).

After closing, under Swiss non-mandatory law, a buyer has (under certain conditions) the right to terminate a share purchase agreement in the event of a severe breach of representations or warranties, and ask for reimbursement of the purchase price by the seller. However, since this outcome would result in a great uncertainty for the seller, the relevant provisions of Swiss law are usually expressly excluded and a specific indemnification process is set forth in the share purchase agreement.

6.8 Allocation of Risk

Risk is allocated via representations and warranties, as well as specific indemnities provided by the seller.

As a matter of principle, the seller provides representations and warranties for risks that have not been identified during the due diligence process and indemnifies the buyer in the event of a breach of those representations or warranties. These remedies are usually limited (see **6.9 Warranty Protection**).

In addition, it is customary that risks specifically identified by the buyer during the due diligence are fully covered by the seller, who would usually indemnify the buyer without limitation in the event that such risks materialise. Unlimited indemnification by the seller also often covers risks related to tax issues and social security issues that occurred pre-closing – without the buyer needing to identify specific risks in this context.

6.9 Warranty Protection

Share purchase agreements (in buyout deals) and investment agreements (in venture and growth capital deals) usually contain a comprehensive catalogue of representations and warranties, including with regard to title, organisation, financial statements, tax, intellectual property, employees and social security, real estate, material contracts and absence of litigation. This catalogue is usually reduced in the case of MBOs, since the buyers have been involved in the management of the target or have profound knowledge about the target or extensive access to the management, or both.

Whereas a private equity seller would provide a full set of representations and warranties on the whole business of the target company in the case of sale of the entire share capital (or assets) of the target company, it would, unlike a corporate seller, tend to limit these representation and warranties as much as possible since its intention is to liquidate the investment and distribute

the proceeds to the investors, which is more difficult with contingent liabilities.

In the case of sale of a minority stake, only limited representations and warranties are usually provided by the private equity seller: authority, valid title to the shares and financial statements are the typical warranties in that context.

As far as managers are concerned, they would usually provide, on exit, warranties related only to the operations of the target company. Often, qualifiers would apply to managers' warranties. The "best knowledge" qualifier is the most frequent, meaning that a manager would only provide warranties to the extent of his knowledge of the business.

Share purchase agreements usually also contain specific indemnities, including full indemnities with respect to taxes or other special risks identified during the due diligence process.

Disclosure Concept

As far as disclosure is concerned, as a matter of principle, the entire data room is considered as disclosed and therefore not covered by the representations and warranties, as long as the information contained in the data room has been fairly disclosed. Hence, under Swiss law, a buyer cannot claim for indemnification due to a defect of the goods if such defect has been disclosed. The definition of "fairly disclosed" is therefore extensively negotiated between the parties. The seller will want a definition as broad as possible; ie, fairly disclosed, meaning, for example, that a fact has been disclosed in a manner to allow, or would have allowed, the buyer, or a diligent third party with a similar profile as the buyer and its advisers, to assess the impact of such fact on the target company. On the other hand, the buyer will want a definition of fairly disclosed documents as narrow as possible.

In order to go against the above, the buyer sometimes tries to obtain from the seller a "fair disclosure warranty" confirming that all documents and information that have been provided to the buyer are accurate and complete in all material respects. Such warranty is very rarely accepted by the seller.

Limitations of Warranties and Indemnities

The representations and warranties are usually limited in time and in the amount. The customary amounts limitations are the following:

- threshold – 1%;
- de minimis – 0.1%; and
- cap – 10 to 30%.

As far as time limitation is concerned, the warranties are usually granted for a time ranging between one and three years. In addition, other customary limitations apply to warranties, such as the duty to mitigate the damage and no double-dip.

Specific indemnities covering risks identified during the due diligence are usually unlimited.

6.10 Other Protections in Acquisition Documentation

Traditional protections for a private equity buyer are the specific indemnities provided by the seller (see **6.8 Allocation of Risk** and **6.9 Warranty Protection**). Some additional guarantees – such as guarantee of a parent company or group company, personal guarantee or bank guarantee – are not unheard of.

In addition, a private equity buyer would very frequently put part of the purchase price in an escrow account, with the escrow amount being used to indemnify the buyer in the case of a breach of representations and warranties by the seller.

On the other hand, an effective protection for sellers is entering into W&I insurance. In Switzerland, W&I insurance is not as common as in other jurisdictions (such as the UK) but is becoming more frequent. Often, a private equity buyer that would offer a W&I insurance as part of the bidding process would have a competitive advantage and might win the auction.

In the event of a deal with W&I insurance, it is less frequent that part of the purchase price is wired to an escrow account to cover a potential breach of representations and warranties, and the full amount of the purchase price is paid to the seller.

6.11 Commonly Litigated Provisions

Whereas claims are rather frequent, proper litigation (ordinary courts or arbitration) is not extremely common, although it has increased in recent years. The provisions of an acquisition agreement that are most contentious are the consideration mechanics, earn-out clauses and claims for breach of warranties.

7. Takeovers

7.1 Public-to-Privates

After a peak in 2016, not many companies have been taken public in recent years.

An example of a recent delisting is Alpiq Holding SA, one of Switzerland's biggest electricity providers. The majority stake in the company was acquired by a consortium of three strategic buyers led by an investment vehicle controlled by Credit Suisse.

The delisting followed the acquisition, in particular to avoid the ongoing costs associated with the listing.

Alpiq's delisting is characteristic for the Swiss market: this activity is mainly driven by strategic investors. Private equity houses are not often involved. More generally, the Swiss public-to-private market is probably less developed than in other jurisdictions. The comparably small number of listed companies may be a reason.

7.2 Material Shareholding Thresholds

The main thresholds are defined in Article 120 of the Financial Market Infrastructure Act (FMIA). The provision states that anyone who directly or indirectly, or acting in concert with third parties, acquires or disposes of (i) shares or (ii) acquisition or sale rights relating to shares of a company with its registered office in Switzerland whose equity securities are listed in whole or in part in Switzerland, or of a company with its registered office abroad whose equity securities are mainly listed in whole or in part in Switzerland, and thereby reaches, falls below or exceeds the thresholds of 3%, 5%, 10%, 15%, 20%, 25%, 33⅓%, 50% or 66⅔% of the voting rights, whether exercisable or not, must notify this to the company and to the stock exchanges on which the equity securities are listed.

The disclosure obligation only pertains to shares (or related derivative instruments), but not to participation certificates, which basically constitute the Swiss equivalent of non-voting shares in other jurisdictions.

The disclosure obligations apply to all shares in a listed company; ie, both to the shares that are listed and to those that are potentially not listed. Although not common, it may happen that, eg, the registered shares are not listed, but the bearer shares.

The ownership in shares created via a capital increase only has to be disclosed once that these shares start bearing voting rights. For Swiss companies, that is the case once the relevant shares have been validly created (subject to subsequent registration in the commercial registry). In practical terms, this means that options allocated via a conditional capital increase are not covered by the disclosure obligation as long as the options are not exercised. Conversely, the respective shares need not be inscribed with the commercial registry.

On the other hand, with respect to shares that have been issued, respective purchase and sale rights (ie, long and short positions) are also taken into account for the disclosure obligations. The purpose is to avoid circumventions of the disclosure obligations.

In the case of a public tender offer, additional disclosure obligations apply, in particular to the bidder and to persons acting in concert with him.

7.3 Mandatory Offer Thresholds

Under Swiss takeover law, the duty to launch a takeover offer is triggered when an acquirer of shares, whether acting directly, indirectly or in concert with third parties, acquires equity securities and thereby, in addition to the equity securities already owned, exceeds the threshold of 33⅓% of the voting rights of a listed company (whether exercisable or not). Listed companies may increase the threshold to 49% ("opting up").

Companies also have the option – before or after becoming listed – to preclude the applicability of the rules pertaining to mandatory offers in their articles of association ("opting out"). In the event that the opting-out is only introduced post-listing, there are certain conditions imposed by the Swiss Takeover Board for the protection of minority shareholders, who must, in particular, be clearly and adequately informed about the majority shareholder's plans and the implications of the opting-out and approve the opting-out in a separate vote.

Furthermore, Article 136 of the FMIA provides for certain further exemptions from the duty to submit a public offer in justified cases. In particular, the Takeover Board may grant such an exemption when the target company is in a critical financial situation and the securities are acquired for restructuring purposes. As a rule, this "restructuring exemption" is granted only as an ultima ratio (ie, only in cases where a restructuring would hardly be possible if the acquisition of the shares would lead to a duty to make an offer and that no other restructuring options seem available). The underlying rationale is that in situations of financial distress, the interest of the shareholders not acquiring additional shares in the continued existence of a company is to be weighted higher than their interest to sell their shares.

In a recent case concerning Schmolz+Bickenbach AG, a company active in the steel industry, two principal shareholders applied to the Takeover Board for an exemption from the obligation to submit a mandatory offer, which would allow them to provide the company with necessary financial means through a capital increase. After an initial rejection of the request by the Takeover Board, FINMA (acting as appellate body) eventually granted the restructuring exemption subject to certain conditions.

Interestingly, FINMA emphasised in its decision that takeover law and practice are subject to constant change and that the requirements for exemptions from the offer obligation must be assessed carefully on a case-by-case basis. It does not seem impossible that in the current economic environment, which is

still heavily affected by COVID-19, the "restructuring exception" will be granted in a more liberal approach. In parallel, the Takeover Board issued a new guidance effective as of 1 October 2020 setting out the documents to be filed together with a request for a restructuring exception.

7.4 Consideration

Under Swiss takeover law, the consideration can be paid in cash and/or in securities. The principle of equal treatment of all shareholders, however, imposes certain restrictions on the offeror. He cannot, eg, offer cash to selected anchor shareholders and securities to stakeholders holding smaller participations. Securities can, nevertheless, be considered cash equivalents, if the respective shareholders are also granted put options, which allow them to realise the value of their securities.

In Swiss takeovers, compensation in cash has historically been, and is still, more frequent than a consideration in securities.

7.5 Conditions in Takeovers

Together with the offer price, the offer conditions constitute the key terms in public takeovers in almost every takeover bid. Swiss takeover law, however, allows conditions in public takeover offers only under restrictive circumstances, terms and timelines.

Voluntary takeover offers can, in general, be made subject to conditions if (i) the offeror has a justified interest, (ii) the satisfaction of the condition is outside the offeror's control and (iii) the condition has clear terms. At the end of the regular offer period, the offeror must clearly state whether the conditions have been satisfied. The offeror can also reserve in the offer the right to waive certain conditions, which is commonly done.

The most frequent common conditions in voluntary takeover offers may be categorised as follows:

- conditions on obtaining control of the target (eg, reaching an equity certain majority);
- conditions on implementing the offer (eg, obtaining a required antitrust clearing); and
- conditions for the benefit of the offeror (eg, no occurrence of a material adverse change).

Mandatory takeover offers may be made subject only to conditions relating to important reasons. This is, eg, deemed to be the case if the acquisition requires a regulatory approval.

Neither for voluntary nor for mandatory offers are financing conditions allowed in the case of cash offers. However, in the case of an exchange offer, the offer may be made subject to the condition that the offered securities can be validly issued (ie, in particular, that the required shareholder approvals can be obtained). The offeror has to undertake all possible steps to ensure that such securities can indeed be issued.

The other main means to improve transaction security are break-up fees and transaction agreements. Break-up fees are commonly used. Although there is no rule as to the maximum amount that a break-up fee can reach, its amount has to be in a certain relation to the transaction volume and potential effective break-up costs of the bidder. The Takeover Board has repeatedly reduced break-up fees deemed excessive, thereby considered preventing competing offers. A key element of transaction agreements is usually an undertaking of the target company not to solicit competing offers, which is allowed under certain conditions.

7.6 Acquiring Less Than 100%

The additional elements required to strengthen the private equity's investor's influence of the target company depend on the target's shareholding structure. In the case of a fragmented shareholder structure, a private equity investor holding a participation of, eg, 30% can often exercise a decisive control. In these circumstances, investors do not necessarily look for ways to further formalise their influence.

However, if this is desired, one option is to proceed to a delisting and to conclude a shareholders' agreement with other shareholders. If the target company's listing shall be maintained, the possibility to conclude a shareholders' agreement is limited, given that if the shares covered by the agreement constitute an aggregate participation of more than 33⅓%, the signatories are generally considered as a group, in particular for takeover purposes. However, if the listing is maintained, the private equity house still has the possibility to conclude a relationship agreement with the target company. Such agreements are, however, rare in practice.

The bidder can proceed to a squeeze-out proceeding if it reaches 98% or more of the voting rights in the target at the end of the offer period. The request has to be filed with the court within three months after the expiry of the additional acceptance period.

If the bidder acquires less than 98% of the voting rights but more than 90% of the share capital in the target company, it can proceed to a squeeze-out merger in accordance with the provisions of the Swiss Merger Act. It will generally use a wholly owned subsidiary to that end.

7.7 Irrevocable Commitments

Bidders will usually seek the support of the target company's anchor shareholders (see **7.8 Hostile Takeover Offers**). Against

this background, irrevocable tender commitments are often obtained.

The negotiations are usually started as soon as possible, and, in any case, before the formal publication of the tender offer.

Under Swiss law, tender commitments are contractual commitments that can generally be freely negotiated between the parties. They can, in any case, be revoked if a competing offer is announced.

7.8 Hostile Takeover Offers

Hostile takeover bids are permitted in Switzerland. With the objective to ensure transparency and the equal treatment of the investors, Swiss takeover law, however, contains a series of provisions in this respect. In particular, the board of the target company has to transparently and comprehensively inform the shareholders of its assessment of the takeover bid. Certain defensive measures are prohibited, and the board of the target company has to inform the Takeover Board in advance of any legitimate measures it intends to take.

However, hostile takeovers are rare in Switzerland. The relatively conciliatory Swiss business culture may play a role. Furthermore, most listed companies have one or more anchor shareholders holding important equity stakes. Bidders appear to be reluctant to launch hostile offers under these circumstances.

8. Management Incentives

8.1 Equity Incentivisation and Ownership

Equity incentives for the management team are very common in private equity transactions. Usually, the level of equity ownership granted to the management team does not exceed 10%.

8.2 Management Participation

The participation of the management team can take various forms: the management team can either be granted shares directly, or via a share plan or an option plan. Alternatively, a management company (ManCo) can be created and the management team subscribes to shares in the ManCo. "Pooling" the managers in one company can have several advantages, one being to avoid too many stakeholders at the shareholders level of the company.

Usually, managers subscribe for ordinary shares rather than preference shares. Sometimes, non-voting shares are granted to the management team.

8.3 Vesting/Leaver Provisions

It is very common that a shareholders' agreement includes good/bad leaver provisions for management shareholders.

A manager would typically be considered as a good leaver in the following situations:

- death, permanent illness or invalidity;
- retirement; or
- termination of the employment agreement by the management shareholder for good cause.

A manager would typically be considered as a bad leaver in the following situations:

- termination of the employment agreement by the company for good cause; and
- if the management shareholder continuously breaches the provisions of the shareholders' agreement or the articles of association of the company.

In the event that the management shareholder leaves the company, the investor shareholder shall have a call option on the leaving manager's shares. Obviously, the price will be lower when the manager leaves as a bad leaver than when he leaves as a good leaver.

Some shareholders' agreements include put options for managers; ie, the right for the management shareholders to sell their shares to the investor shareholder. Among the triggering events, the change of control in the company can typically be mentioned.

As far as vesting periods are concerned, the shares/options granted to the management may be subject to a vesting period, but not necessarily. The typical vesting period would be approximately three years, but would usually not exceed five years.

8.4 Restrictions on Manager Shareholders

Restrictions imposed on management shareholders typically include non-compete and non-solicitation clauses.

Under Swiss law, non-compete clauses shall be limited with regard to scope, duration and geography. According to current practice, a non-compete clause cannot exceed three years but, in practice, non-compete clauses exceeding 18 months or two years are rare.

In the event that a non-compete clause is too broad, it is not declared null and void but is reduced by the judge.

8.5 Minority Protection for Manager Shareholders

Under Swiss law, pursuant to the principle of equal treatment of shareholders, the board and the shareholders' meeting must give equal treatment to all shareholders. Core statutory shareholder rights are the right to participate at shareholders' meetings, information and inspection rights, and the right to receive a share of any dividends and liquidation proceeds. Shareholders also have a pro rata preferential right (which may be restricted for certain important reasons) to any newly issued shares or bonds that are convertible into equity. In accordance with the Swiss Code of Obligations, shareholders representing more than 33.33% of the voting rights can block a number of key resolutions (for example, qualified capital increases, limitation of preferential rights or corporate reorganisations such as mergers).

Moreover, shareholders' agreements typically include minority protections in the form of veto rights – or, rather, qualified majorities, since there is a risk that veto rights cannot be enforceable – on important decisions such as any amendment to the corporate purpose of the company, creation of shares with voting privileges, restriction to the transferability of the shares, and transfer of the registered seat.

A qualified majority can also be applied for important board matters when the management shareholders have a board representative. Moreover, if it is important that no single party has control of the board, the shareholders' agreement may provide for a certain number of independent directors.

Finally, shareholders' agreements customarily restrict the transferability of shares and provide for a combination of rights with respect to the sale of shares (rights of first offer, pre-emption rights, call and put option rights, drag-along and tag-along rights), sometimes safeguarded by share escrow arrangements.

9. Portfolio Company Oversight

9.1 Shareholder Control

The shareholder control of a private equity fund over its portfolio companies very much depends on whether the investment is a minority investment or a buyout transaction.

When the private equity fund holds a majority stake – or the entire share capital – of a company, its control is usually extensive: board appointment right (sometimes even the right to appoint the chairman or the vice-chairman of the board), and veto or qualified majorities rights at shareholders and board level (see **8.5 Minority Protection for Manager Shareholders**), etc.

In the event that the private equity fund only holds a minority stake in a company, it would usually benefit from minority protection rights, such as some veto rights and rights with respect to the sale of shares (rights of first offer, pre-emption rights, tag-along rights, etc). It is also very common that private equity funds, even holding a minority stake in the company, have the right to appoint a board representative.

9.2 Shareholder Liability

A private equity fund, as majority shareholder, can sometimes be held liable for the actions of its portfolio company. However, piercing the corporate veil is rare under Swiss law.

Piercing the corporate veil is admitted when a shareholder is held liable in the case of abusive reference to the separate legal entity. Further, a shareholder may be held liable if it factually controls the company that has become such shareholder's mere instrument.

That said, the board representative of the private equity fund can be held liable for actions of the portfolio company. A damage caused by a breach of a director's duty of care or loyalty or by mismanagement can lead to a liability claim against the board representative of the private equity fund.

9.3 Shareholder Compliance Policy

Unless not systematic, the private equity fund is increasingly imposing its own compliance policies (typically related to reporting, anti-money laundering, anti-bribery, corporate social responsibility, data privacy and other regulations) on its portfolio companies.

10. Exits

10.1 Types of Exit

Exit is obviously extremely important for private equity funds and is already considered at the time of the assessment of the investment strategy.

The typical holding period for private equity transactions before the investment is sold is three to ten years.

The most common form of private equity exit in 2020 by far has been the trade sale. IPOs on the Swiss stock exchange have become increasingly rare.

10.2 Drag Rights

Drag-along mechanisms are extremely common in private equity transactions. The typical threshold is 50%. A private equity fund holding a majority stake in the target company will

make sure it has a straightforward drag-along clause in place to safeguard its exit.

On the other hand, reverse drag along – ie, the private equity fund, holding only a minority stake, being granted a drag-along right – is unusual.

That said, a private equity fund holding a minority stake in a portfolio company will try to negotiate a higher threshold, in order to avoid being dragged in a sale at an inappropriate time. As a minority investor, a private equity fund usually negotiates a minimum price at which the drag along is triggered.

10.3 Tag Rights

Tag-along rights for management shareholders – ie, managers being able to sell together with the private equity fund when it has found a buyer – are also very frequent.

Tag-along rights of institutional co-investors are also common but less recurrent than management tag-along rights.

The threshold to exercise the tag-along right is usually 50% but may depend upon the negotiation power of the parties.

10.4 IPO

On an exit by way of an IPO, investors or members of the management would usually commit to lock-up undertakings. Lock-up arrangements are often put in place for shareholders holding more than 3% equity. According to current market practice, the lock-up period does not exceed a period of one year. Relationship agreements are rare in Switzerland.

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