Company law revision / the Federal Council's proposal Rules on establishing companies and capital

At the end of 2005, the Federal Council fired the starting shot for a revision of company law by presenting a preliminary draft and an accompanying report. Back at the end of 2007, the Federal Council submitted a dispatch and a comprehensive draft, which also contained provisions of accounting legislation. Before the Federal Parliament, however, was even able to start deliberating company law, the popular initiative «against fat-cat salaries» was launched in February 2008. The effect of that was that the company law revision was placed on the back burner. The revision of accounting legislation was separated from the revision of company law. In the meantime, the new accounting legislation has come into force.

After the Swiss people had accepted the initiative «against fat-cat salaries», it was implemented with the Ordinance Against Excessive Remuneration in Listed Companies dated 20 November 2013 (the «Ordinance»). On 28 November 2014, the Federal Council reopened the discussion on reforming company law by submitting a new preliminary draft for consultation. This led to numerous, detailed opinions, and, having worked its way through them, the Federal Council adopted a dispatch on company law revision on 23 November 2016. It is to be expected that in the course of the forthcoming deliberations, the proposal will still undergo several amendments.

We have produced six articles in our «In a nutshell» series, in which we present the proposed changes. This particular «In a nutshell» deals with the rules on establishing companies and capital.

You can consult the other «In a nutshell» articles by choosing the appropriate links:

- General meeting and board of directors **LINK**;
- Unregistered registered shares and shareholders' rights **LINK**;
- Return on benefits **LINK**;
- Threat of insolvency, loss of capital and overindebtedness **LINK**;
- Implementation of Art. 95 para. 3 of the Federal Constitution and gender representation guidelines for listed companies **LINK**.

I. Capital reduction and capital band

The new rules on company share capital set forth in the preliminary draft of the revised company law were generally well received during the consultation procedure and have thus been adopted in the 2016 proposal. These rules are aimed at giving companies greater flexibility, on the one hand, and improving legal certainty, on the other hand.

Companies will now be able to create a so-called capital band. This allows the shareholders' meeting to authorise the board of directors to increase or reduce the company's share capital over a period of no more than five years. The maximum level to which the share capital can be increased or reduced is 50% above or below the share capital entered in the commercial register at the time the decision is taken. It goes without saying that the bottom limit applicable in all cases is the minimum share capital of Swiss Francs (CHF) 100 000. The maximum amount by which the share capital can be increased or reduced must be recorded in the articles of association, together with any other restrictions imposed on the board of directors. The decision must be entered in the commercial register. If the board of directors is only permitted to increase the capital, the capital band comes very close to today's «authorized share capital increase» (with the main difference being that the authorized period of currently two years is increased to five years). If the shareholders' meeting restricts the authorization of the board of directors to reducing the capital, then the decision more or less constitutes an authorized capital reduction, and is thus a novelty in Swiss law. To ensure that creditors are protected, the new legislation stipulates that the shareholders' meeting may only adopt a capital band that provides for a share capital reduction after a call for creditors has been issued and an audit confirmation submitted by an approved auditor. In addition, companies providing for a capital band that permits a capital reduction must have their annual accounts audited at least on a limited audit standard

II. Share capital in a foreign currency

With the revision of the accounting legislation, companies were given the option of conducting their accounting not only in the national currency but also in a foreign currency that is material for their business operations. If the accounts are presented in a foreign currency, the values must also be shown in the national currency. The exchange rates applied must be published in the notes to the accounts and explained where necessary.

For the provisions relating to the share capital (e.g., regarding the use of balance-sheet profit) it is still the values in CHF that constitute the basis in the current legislation. Hence, the question as to whether a company has incurred a capital loss or is overindebted is also determined on the basis of the values in CHF. And, with the principle of prudence that has to be applied, it can happen that an annual profit becomes an annual loss when converted into CHF.

The problem of accounting legislation not being reconciled with Swiss company law is resolved by the 2016 proposal in that it gives companies the option of not only issuing their share capital in CHF but also in a foreign currency that is material for their business operations.

This option makes for legal certainty in Swiss company law and also the ac-counting, auditing and tax legislation. Hence, this liberalisation move met with widespread approval during the consultation procedure already and ought to be well received on all sides now as well.

III. Minimum par value

Following the 1991 and 2001 revisions of Swiss company law, in which the minimum par value per share was reduced in two stages, first from 100 to 10 CHF and then to 1 centime, the 2016 proposal now only specifies that the minimum par value must be greater than zero. This is in response to the need for flexibility in the case of share splits and reductions in par value. At the same time, the revision dispenses with creating artificial no-par shares, since the introduction of such no-par shares would require the modification of a large number of provisions of Swiss company law and no relevant additional benefit would be obtained in this way.

IV. Simplifications for establishing companies

When it comes to establishing a company, the 2016 proposal introduces a number of simplifications. On the one hand, when simply-structured companies are established, a public deed will no longer be required. On the other hand, the so-called (intended) acquisition of assets as qualified form of incorporation is to be eliminated. The elimination of this form of incorporation is also planned for the case of a capital increase.

At present, the establishment and dissolution of a company must be recorded in a public deed. Simple written form is to suffice for establishing a company in the future, providing that the articles of association only contain the statutory minimum contents, the share capital is stated in CHF and the capital contributions have been paid up in full and in CHF. It will also be possible for amendments to the articles of association of such companies to be made in simple written form. The only exception is for capital reductions and in cases where the capital contributions for a capital increase have not been fully paid up in CHF. In these cases, a public deed will still be required. A corresponding rule is also to be introduced for cooperatives. These simplifications were taken up as a result, inter alia, of explicit demands voiced during the consultation procedure and are welcome.

Like the forms of qualified incorporations (cf. Art. 628 Code of Obligations), the (intended) acquisition of assets is a rule that was originally laid down to protect creditors. These rules are intended to prevent the share capital from being eroded right from the start, and it is possible to comply with them inter alia by preparing a founders' report, an audit report by an approved auditor and through publication of this form of a qualified incorporation in the commercial register. In practice, the (intended) acquisition of assets repeatedly leads to unclear situations, since it is frequently difficult to judge whether a specific purchase constitutes an (intended) acquisition of assets or not. Particularly if a certain amount of time has elapsed between the incorporation of a company (or a capital increase) and the acquisition, it is not always clear whether the acquisition is linked to the incorporation of the company (or the capital increase). The subjective component of «intent» makes delimitation difficult. What is particularly disturbing is the legal uncertainty resulting from this, because the legal consequence of non-compliance with the rules for the (intended) acquisition of assets can be nullity of the incorporation. In addition, the (intended) acquisition of assets includes a somewhat arbitrary element, since only the acquisition of assets with the paid-in share capital is captured, and not the conclusion of other agreements, such as consultancy or rental agreements, which almost permit an outflow of funds to be conducted even more easily, e.g., by agreeing on an (excessively) high rent or charging excessively high hourly rates for consultancy services. On the occasion of the last revision of Swiss company law in 2005, the scope of application of the (intended) acquisition of assets rules was limited to acquisitions from shareholders or related parties. This makes sense, since it is primarily in cases of this kind that potential malpractice would be conceivable. Under the terms of the 2016 proposal the requirement of the (intended) acquisition of assets is to be eliminated in its entirety. This is designed to completely eliminate the legal uncertainty that still exists despite the restrictions imposed with the last revision of Swiss company law. It is not to be feared that capital protection will be lost in this way. The existing accountability and capital maintenance rules already offer sufficient protection today. For example, the acquisition of assets from a shareholder at an excessively high price constitutes a violation of the ban on the reclaiming of capital contributions. And in many cases, a covert distribution of profits can be seen in an approach of this kind, which would lead to a claim for restitution as per Art. 678 of the Code of Obligations. In addition, the members of the board of directors are personally liable for the damage incurred by the company in the event of the acquisition of overvalued assets. The accounting legislation provides further protective mechanisms, since it stipulates that the acquired asset must be entered on the balance sheet. If the value of the asset were to be overstated, this would be unlawful, since it would constitute a breach of the principles of economic reality, the principle of prudence and the relevant valuation regulations. Further protective mechanisms result from the regulations in the legislation governing restructuring and from criminal law (e.g., criminal mismanagement, Art. 158 of the Swiss Criminal Code). The abolition of the (intended) acquisition of assets is thus appropriate and ought to meet with widespread approval – as was already the case during the consultation procedure.

V. Reserves and interim dividends

The new statutory regulations are intended to bring the rules governing reserves into line with the revised accounting legislation. At the same time the rules are to be simplified in overall terms and aligned to international practices. As in the revised accounting legislation, a distinction is being introduced between capital reserves (i.e. paid-in reserves, such as share premiums) and retained earnings (i.e. reserves that a company has created itself, i.e., non-paid-out profits). The legislation now explicitly states that the statutory capital reserve may be paid back to shareholders if the statutory capital reserve and retained earnings exceed half of the share capital entered in the commercial register.

In the case of the statutory reserve, provision is made (as in the past) for 5% of the annual profit to be paid into the statutory reserve until this corresponds to 50% (previously 20%) of the entire issued share capital. This increase in the threshold is offset by the abolition of the current obligation to make a second allocation to the reserve (i.e. the allocation of 10% of the amounts distributed as profit above and beyond payment of a dividend of 5%). For holding companies, the threshold for mandatory allocations to reserves remains at 20% of the share capital, as in the past. The percentage for the minimum allocation and the threshold for the reserves may be increased in the articles of association but not, however, reduced.

Interim dividends are not dealt with in the currently valid Swiss company law. In the future, payment of an interim dividend is to be possible if this option is specifically provided for in the articles of association and if the shareholders' meeting's decision to pay a dividend is based on an audited interim financial statement. If the decision to pay a dividend is taken without an auditor's report having been submitted, the shareholders' meeting's resolution will be null and void. Under the new ruling, it will, however, still be possible to decide to pay a dividend on the basis of the annual accounts which is then paid out in quarterly instalments. This does not, however, constitute an interim dividend but is the staggered payment of a divided based on the annual or balance-sheet profit.

December 2016

Dr. Emanuel Dettwiler, LL.M.
emanuel.dettwiler@kellerhals-carrard.ch

Basel
Hirschgaesslein 11
P.O. Box 257
CH-4010 Basel
Tel. +41 58 200 30 00
Fax +41 58 200 30 11

Berne
Effingerstrasse 1
P.O. Box
CH-3001 Berne
Tel. +41 58 200 35 00
Fax +41 58 200 35 11

Lausanne
Place Saint-François 1
P.O. Box 7191
CH-1002 Lausanne
Tel. +41 58 200 33 00
Fax +41 58 200 33 11

Sion
Rue du Scex 4
P.O. Box 317
CH-1951 Sion
Tel. + 41 58 200 34 00
Fax + 41 58 200 34 11

Zurich
Raemistrasse 5
P.O. Box
CH-8024 Zurich
Tel. +41 58 200 39 00
Fax +41 58 200 39 11

www.kellerhals-carrard.ch – newsletter@kellerhals-carrard.ch