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3. Share Capital and Shares

41

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3.1 Share Capital

3.1.1 Definition

145 Share capital (also called registered or nominal capital) is the fixed amount of capital, designated in Swiss francs (CHF), determined in advance (CO 620 I), *i.e.* laid down in the articles of association (CO 626 Sec. 3), and published in the commercial register (CO 641 Sec. 4) and the Swiss Official Commercial Gazette (CO 931). It is the minimum amount of capital that shareholders undertake to contribute to the company assets. It corresponds to the sum of the nominal value of all shares and the associated obligations to make contributions that the company members as a whole have assumed. The share capital is a purely notional figure, not a real sum. It is a debit or barrier figure below which the net assets of the company may not be permitted to sink voluntarily and it constitutes a sum which is meant to be linked permanently to the company assets. From an economic point of view it represents first of all the minimum risk capital that the shareholders have to guarantee and, secondly, it determines the amount of shareholders' equity in the company to which the liability of the company members is limited[1].

42

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1 In addition to the barrier figure for the share capital, there possibly also is participation certificate capital issued by the company limited by shares. This likewise represents shareholders' equity in the company (CO 656a II together with 663a III). The participation certificate capital may not amount to more than double the share capital (CO 656b I), but it can be any smaller amount as well (CO 656b II). In relation to regulating participation certificate capital, the law, subject to other provisions, refers comprehensively to the regulation of the share capital (CO 656a II). *Cf.* N 194 et seq. below.

146 The law specifies a minimum share capital amounting to CHF 100 000 (CO 621). A proportionate relationship between the share capital and the assets or economic importance of a company limited by shares is not a legal requirement[2]. The minimum capital must be maintained both on incorporation and in the event of a reduction in capital (CO 732 V). On incorporation, however, share capital amounting to only 20 percent of the total sum requires to be paid in full (CO 632 I), whereby in every case an amount of CHF 50 000 must either be paid in cash or covered by contributions in kind (CO 632 II). If the share capital is not fully paid up, the outstanding amount represents a claim by the company against the respective shareholders. However, the capital must be paid up in full when bearer shares (CO 683 II) or voting shares (CO 693 II) are issued.

147 Share capital must be distinguished from shareholders' equity and from actual company assets. The shareholders' equity includes, together with share capital, all other resources that either derive from the shareholders (*e.g.* the share premium in the case of issues above par or participation capital) or that have been realised by the company itself and not distributed to shareholders (reserves and carried forward profits). In contrast to this, there is borrowed capital that is made available to the company by third parties (*e.g.* banks). The company assets, however, consist of the total value of all the assets of the company (gross assets) after deduction of all its debts (net assets). Assets appear in the balance sheet as positive resources, *i.e.* assets; shareholders' equity including share capital and borrowed capital appear as liabilities (CO 663a I). Insofar as the company does not show a carried forward loss, the gross assets reflect the sum of company capital and borrowed capital, while net assets are equal to the shareholders' equity. Unlike share capital, company assets are subject to constant change. As a result, based on the share capital as the minimum amount to be contributed, no conclusions can be drawn regarding the state of the assets of a company limited by shares and thus regarding its effective underlying foundation for liability.

43

3.1.2 Function

148 The central function of share capital is to act as security for debts owing to creditors. This is because the members of a company limited by shares have no personal liability (CO 620 II), and this is why the company itself must make adequate provision to cover for any liability. The capital resources and the company's shareholders' equity basis thus markedly influence its credit and risk capacity and thus its rating and its funding potential[3].

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2 Exemptions exist as a result of special regulations for individual sectors: banking companies for instance must have a fully paid up minimum capital of CHF 10 million. (BankA 3 II lit. b together with BankO 4 I), investments companies a fully paid up minimum capital of CHF 1 million (CCIA 28 II) and insurance institutions, depending on the insurance sector they represent, a minimum capital of CHF 3 to 20 million (InsA 8 I). In addition banks, insurance and investment companies are required to possess a minimum amount of shareholders' equity (*cf.* BankA 4 together with BankO 11 et seq. as well as the agreement on shareholders' equity approved by the Basel Committee for Banking Supervision at the end of June 2004 ("Basel II"); *cf.* also CCIA 32 together with CCIO 32, 22 and 23 as well as InsA 9).

3 The larger the amount of shareholders' equity there is, the more financial resources the company has available for funding projects itself or for covering losses. Too great an amount of shareholders' equity, however, can suggest that the company lacks the capacity for investment and growth. The larger amount of shareholders' equity and security is thus "bought" here at the expense of lower shareholders' equity returns.

3.1.3 Protection of share capital

149 Share capital is only able to fulfil this function as a guarantee of minimum liability basis when the capital is actually paid up on incorporation and in the event of an increase in capital and is available in its entirety and unconditionally to the company and when, in addition, it is not subsequently paid back to the shareholders directly or indirectly. Accordingly, the law seeks to ensure the provision of and retention of capital for the company through a number of statutory regulations.

150 Nevertheless, the barrier figure "share capital", for all its restrictions, does not amount to a guarantee for creditors. Losses, for example, can result in a reduction or even a total disappearance of a company's shareholders' equity. Since share capital as a part of shareholder's equity must appear on the balance sheet as a liability in terms of company equity (CO 663a III and IV), thereby determining the minimum amount of the company assets at any given time, it can nonetheless indirectly assume a sort of guarantee function in that the law imposes certain duties to act on the board of directors in the event of loss of capital and overindebtedness (CO 725)[4].

3.1.3.1 Safeguards for raising capital

151 The assurance that company assets equal to the share capital will be raised is guaranteed in particular by the following statutory regulations:

152 (i) *Prohibition on issuing shares below nominal value (CO 624)*: Shares may be issued only at their nominal value or above it (the so-called "below-par prohibition"). The ban on below-par issues also applies to any concealed reduction in the payment obligations imposed on shareholders,

44

such as the granting of commissions, discounts etc[5]. The issue of new shares remains reserved when they replace cancelled shares (CO 624 second sentence). If, for instance, a shareholder forfeits his rights due to non-fulfilment of his obligation to pay in full (CO 681 II; 682), new subscribers are allowed to be offered new shares for an amount below the nominal value. The new subscriber undertakes the obligation to pay in full the contribution to capital still outstanding on the forfeited shares.

153 (ii) *Requirement that the shares be fully subscribed (CO 629 II, 630; 652)*: Both on incorporation and in the event of an increase in capital, shares may be issued only when they are fully subscribed. Subscription constitutes the unconditional obligation on the part of the shareholder to pay to the company a capital contribution equal to the issue price of the shares (CO 630 II Sec. 2). Subscription is irrevocable.

154 (iii) *Minimum payment obligation (CO 632)*: On setting up a company limited by shares, a capital contribution of a minimum of 20 percent of the nominal value of each share must be made (CO 632 I). Altogether the capital contributions made must amount to a minimum of CHF 50 000 (CO 632 II). The obligation for payment in full of the subscribed shares prescribes in 10 years in accordance with general principles of the law of contract (CO 127; BGE 102 II 353). Whether and when the shareholder is required to pay in full is a matter for the board of directors to decide. The board may require an outstanding capital contribution to be paid at any time (CO 634a I) and, if necessary, can initiate legal proceedings. This assumes that the shareholder is known to the company, which is why shares that are not fully paid-up cannot be issued as bearer

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4 *Cf.* N 166 et seq.; *cf.* also N 470; N 479; N 579 below.

5 It is however permitted to use the paid up amount to settle costs for incorporation and increases in capital, for paying the stamp duty on new issues, as well as other expenditures not benefiting the shareholder in connection with the contribution of capital. These costs that reduce the yield from the issue may be incurred, but must be written off within five years (CO 664). *Cf.* N 363 below.

shares but only as registered shares (CO 683 I)[6]. The board of directors can however also declare that the defaulting shareholder has lost his rights deriving from the subscription to the shares and his paid instalment, declare the forfeiture of the shares and issue new shares to replace the cancelled ones (*cf.* CO 681 II)[7]. To do this, the board has to issue a call for payment to the shareholder in default specifying a one-month grace period for

45

payment and stating explicitly that his shareholders' rights will otherwise be withdrawn. In the case of bearer shares, this notification is effected through being published three times in the SOCG (CO 682 I), in the case of registered shares by means of registered letter sent to the shareholder listed in the share register (CO 682 II). If the shareholder fails to pay in full even after the expiry of the grace period, the board of directors can deprive the shareholder of his membership and can declare him to have forfeited the payments he has already made. Again, the notification of forfeiture is achieved via publication in the SOCG or through a personal communication. If the cancelled share certificates have already been issued and can no longer be produced, the fact of their forfeiture must of necessity be published in the SOCG as well as in the form provided for in the articles of association (CO 681 II second sentence)[8]. With forfeiture the shareholder is excluded without compensation from the company; he loses all his shareholders' rights and the partial payments he has made for the cancelled shares. Forfeiture also has the effect of cancelling the share certificate subscribed by the shareholder concerned. In order to guarantee that the share capital is fully covered, the board of directors is obliged to issue new shares to replace the forfeited ones. At the discretion of the board, the issue price may be fixed if necessary at below nominal value (CO 624 sentence 2). If the company makes a profit on the forfeiture, brought about by the fact that the total of the partial payments made on the cancelled shares and the proceeds from the new shares issued in their place exceed the nominal value, the surplus stays with the company and is assigned to the statutory reserves (CO 671 II Sec. 2). If the company suffers a shortfall from the forfeiture, the shareholder whose shares have been forfeited is liable for the relevant loss (CO 682 III).

155 (iv) *Special protective provisions in the case of qualified incorporations and increases in capital (CO 628; 634; 635 and CO 652c; 652e; 652f)*: Special protective provisions are in place to cover cases in which the payment in full of the share capital is effected not in cash, but in tangible assets, or in which the company undertakes during the foundation phase to acquire certain assets. Such contributions in kind and acquisitions in kind must be specified in the articles of association (CO 628 I and II) and the

46

founders are required to provide a written report on the reasonableness of the valuation (CO 635 Sec. 1). In addition, an auditor is required to examine the incorporation report and to confirm in writing that it is complete and accurate and that the valuation is

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6 Registered shares that are not fully paid up are in addition subject to the statutory restriction based on statutory financial grounds (CO 685). *Cf.* N 204 below.

7 Because the issue price that is decided by the general meeting must be made available to the company before registration to the commercial register, there exists expert opinion that the forfeiture only applies to the "non-versé" in the case of a partial contribution in the sense of CO 632 and cannot apply before the respective registration to the commercial register. *Cf.* also BGE 132 III 668.

8 Up to the declaration of forfeiture, the shareholder can legally pay up in full and thereby prevent the loss of his rights. In the case of a minor delay (up to one day in reported cases) forfeiture is in practice unlawful (BGE 113 II 275). According to expert opinion, forfeiture and the accompanying expropriation without compensation is also unlawful from the point of view of proportionality when the partial sum already paid constitutes almost the whole of the shareholder's obligation to contribute and the collecting of the remaining amount does not seem to be inordinately difficult.

reasonable (CO 635a)[9]. For increases in capital the law makes analogous provisions, requiring the written report to be made by the board of directors (CO 652e Sec. 1) and the audit confirmation by the auditor (CO 652f I)[10].

3.1.3.2 Safeguards for the maintenance of capital

156 The maintenance of the share capital is promoted in particular by the following statutory regulations:

157 (i) *Prohibition of contribution repayments (CO 680 II)*: The maintenance of the share capital is primarily guaranteed by the principle that the shareholder may not demand that his capital contribution be paid back (CO 680 II), which means that the assets of the company are protected vis-à-vis the shareholders in favour of the creditors (BGE 110 II 293; BGE 109 II 128). According to expert opinion and practice, this does not merely preclude the shareholder from actually demanding to be paid back, but also prevents the company, other than in cases of a reduction of share capital (CO 732 et seq.), from using the protected company assets in order to provide benefits to shareholders ("prohibition of contribution repayment"). Such benefits include not only actual distributions to the shareholder from share and participation certificate capital (CO 656a et seq.)[11], but also all financial transactions that indirectly produce such a repayment. The prohibition also includes loans to shareholders, for example, that are not covered by the company's freely disposable resources or the acquisition of its own shares by the company, insofar as this acquisition results in whole or in part from the use of the nominal capital. It also follows from the prohibition of contribution repayments that dividends must be paid only from balance sheet profits and from

47

reserves created specifically for this purpose (CO 675 II). A repayment of capital is also meant to be prevented by means of the requirement that no interest may be paid in respect of share capital (CO 675 I)[12]. In terms of a special provision under company law governing cases of unwarranted personal gain (CO 62 et seq.), members of the board of directors or shareholders are furthermore required under certain conditions to repay any unwarranted benefits they may have received from the company (CO 678 f.)[13]. Any direct and indirect obligation for repayment on the part of the company is totally null and void and results in the reinforcement of the obligation to contribute (BGE 109 II 129).

158 (ii) *Restrictions on the acquisition of own shares (CO 659-659b)*: Through the acquisition of its own shares, the company weakens its assets, for the shares of a company constitute a kind of quota of its own assets. The company limited by shares

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9 On the special protective provisions for types of qualified incorporation, *cf.* N 67 et seq. above.

10 For the special protective provisions covering qualified forms of payment in full of an increase in capital, *cf.* N 245 et seq. below.

11 A controversial issue is whether and to what extent the premium arising from an above par issue comes under the ban on reimbursing contributions. In favour of accepting a general prohibition, it can be argued that the shareholder only has the right to a proportionate share of the balance sheet profit "to the extent that it is to be distributed among the shareholders in accordance with the law or the articles of association" (CO 660 I), and the premium paid by the shareholders does not represent either a balance sheet profit or reserves created for distribution to shareholders. It has also been claimed, however, that the company can return the share premium indirectly to the shareholders via a dividend to be borne by the general statutory reserves as soon as it has been entered in the statutory reserves (CO 671 II Sec. 1) and when these statutory exceed one half of the nominal capital (CO 671 III).

12 An exception to this is the payment of construction period interest (CO 676).

13 A shareholder can however be related to his company limited by shares not just as a company member, but also as a contractual partner like any other person or third party. The claims arising from such contractual relations form part of the company's liabilities and it is required to meet them (*cf. e.g.* BGE 121 III 319).

accordingly receives nothing in return for the purchase price it pays for the acquisition of its own shares, since it already owns its assets. The acquisition of own shares furthermore leads to the distribution of the company's own resources outside the legally provided resources for effecting this (dividend payments, reduction in capital). If the distribution is effected from tied up capital, in particular from share capital, it amounts in addition to a prohibited contribution repayment (CO 680 II). Companies can however have a legitimate interest in the acquisition of a limited number of their own shares. Thus, for a small company with just a few shareholders, the transitory acquisition of its own shares may become pressing if a shareholder wants to sell his participation, but from the point of view of the company, there is no suitable purchaser available and the company wishes to take over the shares itself (CO 685b I). In the case of publicly traded companies, the acquisition of their own shares from time to time serves to support the market price[14], or shares may be procured as a bargaining chip in anticipation of takeovers or for distribution to employees in terms of an

48

employee participation scheme. Company law takes these needs into account in that it allows the board of directors the acquisition of the company's own shares under the following conditions[15]:

159 For the purchase of its own shares the company is permitted to use only freely disposable shareholders' equity. The resources must accordingly derive from the balance sheet profit or from free reserves. Neither the share capital nor reserves tied up in terms of the law or the articles of association can be used (CO 659 I). The existence of adequate own resources is determined on the basis of the most recent annual accounts, audited and approved by the general meeting.

160 The total nominal value of these shares may not exceed 10 percent of the company capital including participation certificate capital (CO 656b III; 659 I). In the case of the acquisition of unlisted registered shares with restricted transferability that the company is making because it cannot reject the new shareholder for good cause (CO 685b II)[16], the limit is set at a maximum of 20 percent[17]. The own shares acquired in excess of 10 percent of the share capital, however, must be sold within two years or cancelled through a reduction in capital (CO 659 II).

161 For its own shares, which are listed in the assets of the balance sheet, the company is required to create under liabilities a statutory reserve equal in value to the resources used for the acquisition of the shares (CO 659a II; 671 a). The diminution in value of its own shares must accordingly be covered by other assets. This reserve can be

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14 By participating in the capital market, the company can increase the market liquidity of its shares and this generally produces a higher share value. Price support for smoothing out unjustified fluctuations of share prices is not merely permitted, but is considered to be required when needed. What is not permitted, however, is price manipulation designed to combat justified market swings; *cf.* SPC 161bis. *Cf.* in this context also BGE 6S.156/2006 of 24 november 2006 that denied the culpability of a banker who had raised the share price manipulatively within the last minutes of the year of stock market trade in order to achieve a better closing price in the accounts.

15 The decision to acquire own shares lies in the exclusive competence of the board of directors. The consent of the general meeting is, unlike in EU law, but in keeping with US law, not required.

16 *Cf.* also N 214 et seq. below for more on the restriction on the transferability of unlisted registered shares.

17 These statutory limits are also applicable to the acquisition of own participation certificates, which must be included in the calculation of the equity securities in the possession of the company. The company limited by shares may accordingly acquire shares and/or participation certificates, provided their total nominal value does not exceed the statutory limits. In consequence, by way of example, a company limited by shares that has issued participation certificates up to the legal limit of twice its share capital can hold up to 30 percent and for short periods even up to 60 percent of its own shares. Not applicable, however, are the statutory limits on profit sharing certificates since these do not represent nominal capital (CO 657 III).

eliminated only through the sale of the shares or through their cancellation by means of a reduction in capital (CO 671a). It must accordingly remain in existence as long as the company holds its own shares.

Transactions involving own shares must be indicated in the annex (CO 663b Sec. 10).

49

162 In the acquisition as well as in the selling on of own shares, in principle, the company and/or the board of directors must treat all shareholders equally (*cf.* CO 717 II), and this is why the purchase proposal or bid offer must be communicated to all shareholders at the same price. If the offer is limited to individual shareholders, this must be well founded, necessary and not excessive[18]. As long as the own shares are in the possession of the company limited by shares, the right to vote and associated rights are dormant (CO 659a I)[19]. Finally it is worth taking note of the tax implications that can arise from the acquisition of own shares[20]. If a company has a majority holding in subsidiaries, the acquisition of its own shares by the subsidiaries is subject to the same limitations and consequences as apply to the acquisition of its own shares (CO 659b; *cf.* also BGE 72 II 275 et seq.). Unlike the prohibition on contribution repayments (CO 680 II), the prohibition of the acquisition of own shares is only an administrative rule. If it does not at the same time violate the prohibition on contribution repayment, *i.e.* the acquisition is not funded from tied up capital, a legal transaction involving own shares is valid despite its infringement of CO 659 (BGE 110 II 299 et seq.; BGE 96 II 21) and can in the event of loss lead at the outside to the liability of the board of directors (CO 754).

163 (iii) *Stricter accounting and valuation regulations (CO 662a-670)*: Like all persons registered in the commercial register, companies limited by shares are subject to the general statutory rules on commercial accounting (CO 662a IV together with CO 958 et seq.). For the company limited by shares, however, stricter and more precise obligations have been set up in respect of accounting and valuation requirements (*cf.* CO 662a-670). The intention here is above all to prevent the financial position of the company from appearing too positive and especially to avoid balance sheet profits being indicated (and distributed) that in reality have not been achieved at all[21].

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164 (iv) *Requirement to create reserves (CO 671-673)*: The rules on the maintenance of capital are supplemented by the provisions on the creation of reserves (*cf.* CO 671-673). The company limited by shares is obliged to assign part of its annual profit to general reserves (CO 671). In addition to the further statutory reserves for own shares (CO 671a) and for the revaluation of real estate and shareholdings (CO 671b), the company can also create additional reserves in keeping with the articles of association (CO 672 et seq.) or a resolution of the general meeting (CO 674 II and III). The statutory reserves like the other reserves are to be shown in the balance sheet under shareholders' equity as independent balance sheet items (CO 663a III). Neither the term "reserves" nor "share capital" designate any specific assets. Like share capital they represent an accounting barrier figure designed to prevent distributions to shareholders

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18 Public offers by companies limited by shares to buy back their own listed shares are in principle subject to the rules on public takeover offers in the Stock Exchange Act (SESTA 22 et seq.), *i.e.* they must in particular be submitted before publication to the TOB for its comments. Generally exempted from this are buy-backs amounting to a maximum of 2 percent of the shares. Subject to certain conditions, buy-backs of up to 10 percent of the capital may also be partly exempted from the takeover rules, but they must be notified to the TOB. *Cf.* Communication No. 1 of the Swiss Takeover Board of 28 March 2000.

19 This regulation is not aimed at asset protection so much as preventing the board of directors from using shares the company has bought as a means of influencing general meetings.

20 *Cf.* N 1182 et seq. below.

21 For the accounting regulations of company law, *cf.* N 339 et seq. below.

from assets that are required for the complete coverage of share capital and reserves (CO 674 I)[22].

165 (v) *Regulations on the reduction in capital (CO 732-735)*: The law allows a reduction of the share capital only when special protective provisions are complied with. The intent is to prevent the reduction in capital from harming the interests of creditors, *i.e.* the basis for liability and the fixed share capital (of CHF 100 000) cannot be reduced to their detriment (BGE 102 Ib 23)[23].

3.1.4 Measures for loss of capital and overindebtedness

3.1.4.1 Measures for loss of capital

166 The statutory protective measures outlined above for safeguarding share capital do not just in themselves provide a guarantee that the share capital will always remain totally intact. Poor business performance can lead to losses. These must be indicated separately in the balance sheet as a so-called "balance sheet loss" (CO 663a IV). As long as the company's assets still fully protect its liabilities and only the shareholders' equity is no longer fully covered, we are dealing with what is referred to as a balance sheet deficit.

167 In the case of loss of capital, however, we have a special form of balance sheet loss. This loss arises when the assets no longer cover half of the share capital (including any participation capital; *cf.* CO 656b III) and the statutory reserves

51

(CO 725 I). In such a situation the board of directors is required to convene an immediate general meeting to which they must propose restructuring measures (CO 725 I). As well as the more obvious measures affecting operations (*e.g.* disposals, restructuring or stopping certain business areas or loss-bringing activities), possible restructuring steps to be considered in the case of loss of capital affecting (or "cleaning up") the balance sheet include the following:

168 (i) *Offsetting the loss against reserves*: If this has not been done already, the rule is that the first step is to offset the loss against the reserves. Apart from free reserves, a portion of the statutory reserves can also be used for this purpose (CO 671 III). Offsetting against free reserves, however, although it results in a reduction of the balance sheet loss, has no effect on the capital loss, for this latter is calculated independently of free reserves. In contrast, offsetting against the statutory reserves does reduce the capital loss.

169 (ii) *Revaluation of real estate and shareholdings*: Fixed capital assets may normally be valued only at acquisition or construction costs, under deduction of the required depreciation (CO 665). In the event of a loss of capital (the law speaks here incorrectly of a balance sheet deficit), the company is permitted to assess real estate and shareholdings at their true value (market value), *i.e.* the hidden reserves within these assets may be liquidated (CO 670)[24].

170 (iii) *Increase in capital*: An increase in capital (CO 650 et seq.) can also be used for restructuring purposes since the issue of new shares for value leads to additional assets flowing into the company. This results in an increase in current assets on the assets side

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22 An exemption from the ban on distributions is constituted by the dividend reserve that can be approved by the general meeting with the aim of paying out consistent dividends despite business fluctuations from one year to another (CO 674 II Sec. 2). For more on the regulations governing reserves *cf.* N 370 et seq.

23 For more on the reduction in capital, *cf.* N 256 et seq. below.

24 For real estate in particular the true value may exceed the purchase price many times over. Such revaluations must be audited (CO 670 II); in addition, the amount of revaluation must be indicated separately in the balance sheet as a revaluation reserve (CO 670 I; 671b), and the annex must supply details on the subject matter and the amount of the revaluation (CO 663b Sec. 9).

reflecting the capital contributions and increased share capital on the debit side. Although the contribution of new asset value via an increase in capital does not influence the balance sheet loss, in some circumstances a loss of capital can at least be averted or eliminated.

171 (iv) *Reduction in capital*: The reduction of share capital can also be considered as a possible restructuring step[25]. This means that the share capital is reduced by the company taking back a number of shares without any return consideration and subsequently cancelling them or the nominal

52

value of the shares is reduced. A consequence of this is a reduction in the balance sheet total; to this extent there is a change in the relationship of the balance sheet loss with the share capital and the statutory reserves. A sufficiently large reduction thereby obviates the loss of capital.

3.1.4.2 Measures for overindebtedness

172 Overindebtedness exists when the assets no longer completely cover the share capital (including any participation capital; *cf.* CO 656b III) and the reserves and also the liabilities. The debts of the company limited by shares are in excess of assets owned by the company. If there is a justified concern about overindebtedness, the board of directors must draw up or have drawn up an interim balance sheet to be submitted to the auditor's inspection. If it emerges from this that the claims of company creditors can be covered neither by going-concern values (*i.e.* on the assumption that business operations will be continued) nor by liquidation values (*i.e.* on the assumption of liquidation)[26], the board of directors must notify the court unless company creditors subordinate their claims to those of all other company creditors to the extent of the deficit (CO 725 II; *cf.* also CO 716a I Sec. 7)[27]. When there is a threat of bankruptcy proceedings, creditors with close ties to the company (*e.g.* major shareholders who have provided loans to the company) are often prepared to make a so-called "declaration of subordination" ceding the priority of their claim. For such a declaration to have an effect and thus avert the overindebtedness, the creditor must not only accept that his claims rank behind those of all other creditors, but must also explicitly refrain from raising his claim (and any interest accruing to it) for as long as the state of overindebtedness continues. Such a declaration is thus merely a moratorium and not a waiver of outstanding debts; the company remains in debt and can in no way delete the outstanding obligation from the borrowed capital.

173 If there is a prospect of restructuring, the court may defer the announcement of insolvency in response to an application by the board of directors or a creditor, but not, however, by a shareholder. In this event, it has to undertake measures for the preservation of assets (CO 725a I). In particular, the court may appoint a commissioner and either deprive the board of directors of its power

53

25 For reductions designed to eliminate a balance sheet deficit, the law provides for a simplified procedure: the call on creditors and the satisfaction or securing of their claims are dispensed with (CO 735).

26 Normally, a valuation of the assets based on the going concern values yields a higher amount. By way of exception, however, a valuation at liquidation value can be higher if the company possesses considerable hidden reserves (*e.g.* operating premises).

27 A prior notification to the general meeting is not required. If the board of directors does not act and the overindebtedness is obvious, the auditor is required to make a report to the court (CO 729b II). Shareholders and creditors, on the other hand, are not authorised to notify the court.

to act for the company or make its resolutions subject to the consent of the commissioner (CO 725a II). Only if it is necessary for the protection of third parties (normally creditors), public notice of a deferral of bankruptcy must be given (CO 725a III). The deferral of bankruptcy under company law results in the suspension of proceedings brought by the creditors (BGE 101 III 99; BGE 104 III 20); it does not, however, delay either limitation periods or the due date for claims and the accrual of interest. It creates a breathing space that raises somewhat the chances for an out-of-court settlement. The deferral of bankruptcy ends either when it is revoked by the court following successful restructuring or with the commencement of bankruptcy proceedings by the court on the expiry of the postponement (which may have been extended) or the final disappearance of any prospects for restructuring[28].

3.2 Shares

3.2.1 Definitions

174 The term "share" has various meanings reflecting its different functions.

175 In its legal definition, the law refers to the share as a partial sum of share capital to be determined and announced in advance (CO 620 I). The share is thus primarily a share in the company capital. It must amount to a certain value (called "nominal value") which must be at least one Swiss centime (CO 622 IV)[29]. Shares without a nominal value or which merely quote a certain fraction of the nominal capital ("shares of no par value") are unlawful. The sum of the total nominal values of the shares yields the share capital, and it is open to the company limited by shares to issue shares with different nominal values. The participation of a shareholder is in consequence always measured according to the relationship of the nominal value of the shares that he holds to the total share capital. The economic value of this capital share is measured, however, not according to nominal value, but either according to the market value of the share, *i.e.* stock exchange value or the value deriving from a dealing price agreed between a shareholder willing to sell and a potential purchaser, or, where necessary, according to the "true" or "intrinsic" value specified by a

court (CO 685b V)[30]. This intrinsic internal value is determined on the basis of established evaluation methods. Special consideration is given to the underlying value of the company, *i.e.* the book value of its total assets under deduction of its debts, and of its potential yield value, *i.e.* the profits of the preceding financial years capitalised at customary market interest rates[31].

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28 The deferral of bankruptcy can also end if the company on own application or that of a creditor is granted a legal moratorium of debt enforcement (DCBA 293 et seq.).

29 This minimum nominal value has been applicable since 1 May 2001. This reduction in the minimum nominal value came about on practical grounds, in particular in the interests of publicly traded companies whose shares had become too heavy for the stock market.

30 In addition, the law speaks of "real value" in connection with the (exceptional) revaluation of real estate and shareholdings without, however, defining the term (CO 670 I). If there is a market for the object to be valued (real estate and shareholdings), the real value could be the market value; otherwise the value would depend on the prevailing conditions determining it.

31 In practice, valuation has increasingly been carried out by the discounted cash flow method ("DCF-method") as opposed to the so-called "practitioner's method". This latter takes the average between the value on a capitalised income (which can if necessary be weighted by multiplying by two or three) and the material asset value as company value. In contrast, the company value based on the DCF-method consists of the sum of the future free cash flows, *i.e.* the future revenues, and these are normally discounted on their current value by the weighted average cost of capital (WACC). *Cf. Carl Helbling*, Unternehmensbewertung und Steuern, 9th ed., Düsseldorf 1998, pp. 105 et seq. and 135 et seq.

176 In addition to this meaning as a share in capital, the share is also the embodiment of all the rights and obligations of the shareholder of the company limited by shares[32]. He acquires these either via his original subscription to the shares on incorporation or capital increase or derives them through transfer from a previous shareholder.

177 Finally, the share is the designation of a certificate that attests to the rights of the shareholder (CO 622 V).The tradability of the member's position is a central structural feature of the company limited by shares that is enhanced through the documentation of the share. Shares issued as physical documents are held in legal terms to be securities (CO 965 et seq.), and they provide everyone who can show his entitlement to them the financial and membership rights which they embody *vis-à-vis* the company[33]. The documentation in the form of a printed security does not, however, represent an absolute requirement for the legal justification, pursuit and transfer of shareholders' rights (BGE 83 II 454)[34]. In the case of private companies limited by shares with a small number of shareholders, physical share certificates tend rather to be the exception, either because the issue is deemed to be superfluous or because it is overlooked[35].

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Publicly traded companies also regularly no longer distribute share certificates. In the course of the general movement towards paperless stock exchange transactions, they have mostly included in their articles of association a reference to so-called "registered shares to be printed at a later date"[36]. Later the registered shares will be supplied only at the express request of a shareholder. As long as this does not happen, trading proceeds in a paperless manner and is effected not through physical transfer but only via electronic entries at the Swiss clearing centre SegaInterSettle AG (using the facility of its associated custodian bank), at the custodian bank (in the sub-register for the customer) and at the company in its share register. In recent times, publicly traded companies have been going still further in that their articles of association make no mention of printing and delivering registered shares, but simply grant to the shareholders the right to demand at any time an attestation as to their holding of shares, but no longer any claim for the printing and delivery of it. As a result of the SIS-system the transfer of such shares can only be effected with the collaboration of a custodian bank affiliated to the SIS and is subject to the requirement that the request be made in writing (CO 165 I).

32 For the legal status of the shareholder *cf.* N 272 et seq. below.

33 A certain number of shares can also be covered by a single share certificate. Legally share certificates are the same as the corresponding individual titles and do likewise qualify as securities (BGE 86 II 95).

34 The share is merely a declaratory security. This means that the rights it attests to exist regardless of their embodiment in the security. The principle of securities law, according to which a debtor is required to contribute only in return for the handing out of a certified security (CO 966 I), is consequently not applicable.

35 The refusal to issue share certificates does not always have to be a disadvantage because in a small circle of shareholders known to each other personally share certificates are regarded as a formality rather than as securities that must be carefully preserved. They are often misplaced and must then, for example in connection with a sale, be declared by the court to be null and void in a costly procedure (CO 977; 981 et seq.).

36 In collaboration with the SWX Swiss Exchange, the Swiss Bankers Association and the SIS SegaInter-Settle AG, a set of regulations has been developed that guarantees the tradability of registered shares (including shares with restrictions on the transferability). *Cf.* the SWX directive on tradability of registered shares of 1 June 1998. For listed registered shares the SIS system is now mandatory. Listed bearer shares are given to SIS SegaInterSettle AG for safekeeping in a group deposit. Here too, there is no physical delivery, and the transfer from seller to purchaser goes ahead purely in accordance with book entries.

3.2.2 Types of shares

178 Shares are always either registered shares or bearer shares (CO 622 I)[37]. The main difference between the two types is the way they are transferred. Beyond this, shares are distinguished among themselves according to whether they confer preferential rights (preference shares, voting shares) or not (common shares).

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3.2.2.1 Bearer shares

179 A bearer share is a security paper in which the company limited by shares declares that it recognises and treats the bearer as a shareholder. The bearer can exercise his rights by presenting his shares (CO 689a II). Bearer shares are qualified as actual bearer certificates in the terms of the general legislation on securities (CO 978 I). They may only be issued on payment of the full nominal value (CO 683 I). Bearer shares issued before payment has been made in full are null and void (CO 683 II; *cf.* BGE 86 II 89; BGE 112 II 356).

180 The transfer of bearer shares ensues through a simple handing over of property, the legal effect of which is essentially measured in accordance with the principles of property law[38]. This transfer cannot be restricted by the articles of association (CO 685a I). Bearer shares can thus be traded simply and anonymously, and the company has no right to know the identity of the shareholders[39]. In addition, bearer shares cannot be designated to be voting shares (CO 693 II).

3.2.2.2 Registered shares (and the share register)

181 The company limited by shares can also certify the status of the shareholders by means of securities that are not bearer shares, but certificates carrying the name of a particular person (CO 622 I). Registered shares must be paid to an amount of at least 20 percent of their nominal value (CO 632 I); they represent transferable order papers created by law (CO 684 II; 1145 et seq.). For the transfer of registered shares it is accordingly necessary both to hand over the certificate and to endorse it, *i.e.* with an explicit declaration of transfer on the share (CO 684 II; 967)[40]. Consequently, the acquirer of a registered share (the endorsee) must identify himself as a shareholder *vis-à-vis* the company by producing his share certificate, which leads to his registration in the share register. Like bearer shares, registered shares are in principle transferable without restriction (CO 684 I). In the case of registered shares, however, the principle of

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37 The choice between registered or bearer shares must of necessity be regulated in the articles of association (CO 626 Sec. 4). Provided their relationship to each other is established, the articles of association can also provide for the issue of both types of share (CO 622 II). The articles of association can also provide for the possibility of converting each of the two types into the other (CO 622 III).

38 The conditions are: (i) the conclusion of a valid basic transaction (normally a share purchase agreement); (ii) the transfer of ownership of the share paper or execution of a surrogate transfer; and (iii) the seller's right of disposal or failing this - the acquirer's good faith in respect of the seller's legal standing.

39 According to prevalent expert opinion, the owner of bearer shares is not required to divulge his identity even when he exercises his rights at the general meeting. As a result of the obligation to disclose major shareholdings, however, the principle of anonymity applies only to a limited extent in the case of listed companies (CO 663c; SESTA 20), groups (CO 663b Sec. 7, 663e II Sec. 3) and banks (BankA 6 V together with BankO 25c I Sec. 3.10.2; *cf.* also BGE 124 II 581).

40 *Cf.* N 272 below.

free transferability can be restricted under law or by the articles of association (so-called "Vinkulierung"; *cf.* CO 684 I; 685-685g)[41].

182 The issue of registered shares is inseparably linked to the existence of a share register: for registered shares the board of directors of the company is required to keep a share register in which the owners and usufructuaries are listed with their names and addresses (CO 686 I)[42]. It confirms the legitimacy of the shareholders, for in relation to the company only those registered in the share register are regarded as shareholders (CO 686 IV).The company must in addition certify the registration on the share certificate (CO 686 III). The shareholder is also entitled to see the details of his own entry in the share register[43]. The registration in the share register, however, has only a declaratory effect; it substantiates the (rebuttable) assumption that the person registered in the share register is a shareholder of the company (BGE 124 III 354). The registration therefore does not bring about the legal transfer of the share as such. Its purpose is rather an indication of the acquisition of the share as property (*i.e.* ownership and seamless endorsement sequence) or the legal establishment of a usufruct (CO 686 II). If the entries derive from false details given by the acquirer, the company can delete the entries in the share register following a hearing of the person affected. This person must, however, be informed without delay of the deletion (CO 686a).

183 In corporate practice, registered shares are accorded a greater importance than bearer shares. For the company in particular, registered shares have the advantage that it always knows who its shareholders are[44]. This does not merely provide greater control of the shareholders, but is also convenient in administrative ways. In particular, invitations to the general meeting (CO 700 I) can go out by simple letter and are not required to be publicised through advertisements in the media. If, however, the transfer of registered shares is subject to restrictions contained in the articles of association, registered shares can be disadvantageous for shareholders wanting to sell.

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3.2.2.3 Voting shares

184 The shareholders' voting rights are in principle not dependent on the number of shares they hold, but according to the nominal share value their shares represent (CO 692 I)[45]. The voting rights can, however, be specified by a provision in the articles of association to be irrespective of the nominal value resulting from the number of shares belonging to each shareholder such that each share carries one vote (CO 693 I).The issue of voting shares must be based on a provision in the articles of association. The introduction of such a provision into the articles of association is also possible at a later time, but then it does require a qualified majority as is provided for by law for certain "important resolutions" (CO 704 I Sec. 2). These shares designated as voting shares that have a lower nominal value than other shares issued by the company can moreover only be issued as registered shares and must be paid up in full. In addition, the nominal

41 For more on restricting transferability of registered shares, *cf.* N 202 et seq. below.

42 In respect of the nature of the share register, the most diverse types of written directories are possible and customary. It can be kept as an actual book; small "private" companies especially restrict themselves to collected single sheets in a file. Publicly traded companies have their ledger organised in electronic form by their share office or by a specialist company.

43 Subject to the reservation of CO 697, however, the shareholder has no right of access to the share register in respect of the entries of the other shareholders. He is not permitted, for instance, to find out the names and addresses of his fellow-shareholders in the run up to a general meeting, in order to win them over to his views or even to grant proxies (something the board of directors can do). Third parties, notably creditors, have no right to inspect the share register.

44 Registered shareholders can however renounce the entry in the share register and thus keep their anonymity. For more on such "Dispo-Shareholders", *cf.* N 210; N 213; N 282 below.

45 The voting right is accordingly measured irrespective of the actual payment in full having been made; unlike the right to dividends and share in the proceeds of liquidation (*cf.* CO 661).

value of the other shares may not exceed ten times the nominal value of the voting shares (CO 693 II)[46]. With the same investment of capital it is therefore possible to obtain ten times the number of votes.

185 The voting privilege, however, does not apply without limitation; it is not applicable to business connected to the exercise of shareholders' supervision rights, namely:

186 (i) the election of the auditors (CO 693 III Sec. 1);

187 (ii) the appointment of experts to review management or individual parts thereof (CO 693 III Sec. 2);

188 (iii) a resolution on initiating a special audit (CO 693 III Sec. 3); and

189 (iv) a resolution on raising an action of accountability (CO 693 Sec. 4).

190 In addition, the influence of voting shares in relation to "important resolutions" is restricted by the legally mandatory double hurdle requiring that such resolutions must be passed by a minimum of two thirds of the votes represented combined with an absolute majority of the nominal share capital represented (*cf.* CO 704 I)[47].

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3.2.2.4 Preference shares

191 The property rights of the shareholder, in particular his right to dividends and a share in the proceeds of liquidation, are determined in principle according to the extent to which he has made full payment for the shares he holds (CO 661). The company can however deviate from this principle and issue preference shares, which are privileged *vis-à-vis* common shares in respect of their financial entitlements (*cf.* CO 654/656). Like voting shares, the issue of preference shares must derive from a provision in the articles of association. In contrast to voting shares, however, they need not be in the form of registered shares or be fully paid up; in addition, no qualified majority is required for the retroactive introduction of preference shares. The cancellation or amendment of preference shares requires both a resolution of the general meeting and a majority of the preference shareholders voting at a separate meeting (CO 654 II and III).

192 In content, the preference can relate in particular to the nature and size of the dividend and participation in liquidation surplus as well as to the pre-emption rights on the issue of new shares occasioned by an increase in capital (CO 656 II). Especially in the case of a restructuring, the issue of preference shares is a suitable means of either gaining new investors for the ailing company or of inducing existing shareholders to dispense with their current investment in a reduction in capital. Preference shares are also issued in family firms in order to reward deserving founder members and employees as well as, if possible, to secure a certain return on their investment to shareholders not active in the business[48].

3.2.3 Participation certificate and profit-sharing certificate

193 Apart from shares, the company limited by shares recognises two further equity securities, the participation certificate and the profit-sharing certificate:

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46 In this context we refer to "concealed voting shares"; in contrast to the "open voting shares" not permitted under Swiss law, which provide multiple voting rights for the same nominal value.

47 For more on the qualified quorum for "important resolutions" *cf.* also N 420 et seq. below.

48 In practice, the enterprising shareholders in exchange not infrequently obtain the majority of the votes.

3.2.3.1 Participation certificate (PC)

194 Although company law does not formally make participation certificates (PCs) into a type of share, it regulates them in almost every respect in accordance with the guiding principles of the non-voting share (*cf.* CO 656a-656g). Fundamentally, the participant has the same property rights as the shareholder (CO 656f), but not the right to vote and the associated rights of participation (CO 656a I; 656c).

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195 In order to avert too wide a gap between voting rights and risk, the participation certificate capital may not exceed twice the amount of the share capital (CO 656b I)[49]. Participation certificate capital forms an independent section of the company's shareholders' equity and must be identified separately in the balance sheet; however, for calculating limits imposed under law on the creation of reserves (CO 671), for the acquisition of own shares (CO 659), the initiation of a special audit (CO 697b) and for ascertaining a loss of capital (CO 725), the participation certificate capital must be included with the share capital and constitutes together with this the relevant figure (CO 656b III).

196 Participation certificates are in principle subject to the same requirements as shares, provided no special regulation has been passed (CO 656a II). Like shares, they are created on incorporation or at a later date in accordance with the regulations on increase in capital, and they function like shares during their existence and are eliminated in the same way as shares, *i.e.* through reduction in capital or in the dissolution of the company. Like shares, participation certificates are securities and can be issued in bearer form or as transferable or non-transferable registered participation certificates and can be provided with preferential rights.

197 In relation to property rights, participation certificates must at the minimum be on equal terms with the share category assigned the fewest privileges (CO 656f II and III). Since the participants have no voting rights or co-management rights and cannot serve on the board of directors, the law also provides a range of protective measures to prevent them from being misused or exploited by voting shareholders: the participants must in particular receive notice of the convening of a general meeting and the motions of the board of directors (CO 656d I); they also have the right to present in writing for the attention of the general meeting requests for information and inspection and for initiating a special audit (CO 656c III) and to be informed of all resolutions passed by the general meeting (CO 656d II). In addition, any preferential and participation rights of the participants in the articles of association can be amended at a later date only with the consent of a special meeting of the affected participants (CO 656f IV). Following from the equality of treatment with the shareholders, finally, each participant has the right to challenge resolutions of the general meeting that infringe the law or the articles of association (CO 706 I) as well as

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the right to initiate proceedings for the corporate bodies of the company to be brought to account (CO 752 et seq.)[50].

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49 In practice, the participation certificate, which was first regulated in the revision of 1991, has lost much of its importance. The non-voting participation certificate in particular stands in sharp contrast to the principles of "good corporate governance", which *inter alia* aim for a balanced relationship between management and supervision by the capital owners. *Cf.* N 682 et seq. and N 769 below.

50 Further protective provisions in favour of the participants can be provided for in the articles of association.

3.2.3.2 Profit-sharing certificate

198 A company limited by shares may be authorised by its articles of association to distribute profit-sharing certificates to persons linked with the company through a previous participation in capital or as a shareholder, creditor, employee or in a similar way (CO 657 I)[51]. These profit-sharing certificates provide the holders rights to a share of the balance sheet profit or the proceeds of liquidation, as well as rights to subscribe for new shares (CO 657 II). They thus procure only rights to assets and no membership rights. The profit-sharing certificate is neither a type of share nor a participation certificate nor does it represent a share in company capital or possess a nominal value, and it is not distributed in return for a capital contribution either (CO 657 III)[52].

3.2.4 Debentures, convertible bonds and option bonds

199 Shares, profit-sharing certificates and participation certificates attest to participation in the company, and the capital contributions made by shareholders and participants form the shareholders' equity in the company. For the procurement of borrowed capital, on the other hand, especially for large, economically important companies, there is the possibility of issuing bonds (*cf.* CO 1156-1186). These are normally fixed interest credit demands, predominantly issued publicly in series and at the same conditions as securities on the occasion of a mostly long-term loan. In the case of a public issue, it is mandatory to provide a prospectus (CO 1156), and the creditors constitute by law a body of creditors (CO 1157 et seq.).

200 In the capital market there are various special types of bonds including convertible and option bonds. These forms of capital investment consist of combinations of (mostly fixed) interest bonds with a right to subscribe to shares (in some circumstances to participation certificates as well). The inclusion of these rights can vary: with options the investor retains his bond and has the opportunity to acquire at certain conditions (normally at the end of the term) shares or participation certificates additionally. In contrast to this, the owner

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of convertible bonds has the right within a certain period or at a given time (normally at the end of the term) to trade in the bond for one or several shares or participation certificates.

201 Company law simplifies the supply of the shares necessary for carrying out conversion and option rights though the mechanism of a conditional increase in capital (CO 653-653i)[53]. In favour of the conversion and option rights, the law also provides for a mandatory safeguard against dilution of holdings, provided the same restriction does not affect the shareholders (CO 653d II). Nor can regulations on restrictions of the transferability be brought into play when shares are obtained through the exercise of conversion or option rights unless this possibility is reserved in the articles of association and in the prospectus (CO 653d I). It should be noted though that this is in fact what usually happens in practice.

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51 Profit-sharing certificates may be created in favour of incorporators only on the basis of a provision in the original articles of association (CO 657 V).

52 Those entitled to profit-sharing certificates form by law a group which by analogy are covered by the provisions applicable to a group of creditors in the case of bonds (CO 657 IV; *cf.* also CO 1157 et seq.).

53 For more on the conditional increase in capital *cf.* N 249 et seq. below.

3.2.5 Restrictions on the transferability of registered shares

3.2.5.1 General remarks

202 The unrestricted transferability of membership and of the share is typical of the company limited by shares (*cf.* CO 683 et seq.). This is because it should be irrelevant to whom membership of the company passes since the person of the shareholder is unimportant. This free transferability, however, can be undesirable for (atypical) companies limited by shares with powerful personal elements; in such cases, it may be more desirable to seek to influence the composition of the circle of shareholders. In order to make hostile takeovers more difficult moreover, publicly traded companies may have an interest in limiting the number of shares held by one person. To a limited extent these goals can be achieved through restrictions on the transferability (the so-called *Vinkulierung)* by including in the articles of association a provison that makes the valid transfer of membership dependent on the approval of the company (*cf.* CO 685a-685g)[54].

203 Without this provison, the company limited by shares has no way of restricting the transfer of its shares. It is simply required to accept an acquirer without further ado as a shareholder (CO 684 I). A restrictive provison today tends nevertheless to be the exception and is only possible with registered shares (CO

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685a I). Bearer shares cannot be restricted in this way. Apart from the special case of the statutory restriction of partially paid up registered shares (CO 685), restrictions must always be provided for in the articles of association (CO 685a et seq.). It can be introduced at a later date, but only with the qualified majority of two thirds of the votes represented and the absolute majority of the shares represented required for important resolutions (CO 704 I Sec. 3). In respect of restrictions in the articles of association though, the law makes a distinction between those registered shares listed on the stock exchange and those that are not. In the case of listed shares, the opportunities for restricting transferability are severely limited so as not to impede the trading of shares in too excessive a manner (CO 685d). In every case, the restrictions on transfer apply only to acquisition through legal transaction, but do not apply, or apply only in part, to acquisition due to inheritance, marriage or debt enforcement proceedings (CO 685 I; 685b IV; 685d III).

3.2.5.2 Statutory restrictions on the transferability

204 Registered shares that are not fully paid up may be transferred only with the consent of the company unless they are acquired by inheritance or distribution of an estate or under matrimonial property law or debt enforcement proceedings (CO 685 I). The justification for this regulation lies in the fact that the seller of the partly paid up registered shares who is not a subscriber is freed from his obligation to pay in full (CO 687 III)[55]. The company may, however, withhold its consent only if there is doubt as to the solvency of the acquirer and the security requested by the company is not provided (CO 685 II). As soon as the acquirer of registered shares that are not fully paid up is

[54] The approval of the transfer is within the competence of the board of directors (CO 716 I). By the articles of association, this competence can also be transferred to the general meeting, and this can - in some circumstances - make sense for "private" companies limited by shares. Due to the 20-day refusal period for shares listed on a stock exchange (CO 685g), however, such a competence of approval of the general meeting is conceivable for unlisted shares only (*cf.* also CO 685c III).

[55] If the subscriber sells the share, he may be required to pay the non paid-up amount if the company goes into bankruptcy within two years of its registration in the commercial register and the rights of his legal successor arising from the share have been declared forfeited (CO 687 II).

recognised as a shareholder and entered in the share register, he is obliged to make payment to the company (CO 687 I).

3.2.5.3 Restrictions on the transferability of listed registered shares in the articles of association

205 For listed shares, *i.e.* shares that are listed on a Swiss or foreign stock exchange in a main or other segment, only the following possibilities for restricting transferability exist[56]:

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206 (i) *Percentage clause*: The articles of association can provide for a percentage limit of registered shares (CO 685d I)[57]. Although a company limited by shares cannot prevent the sale of shares above this percentage which are freely available on the stock market, it can prevent the acquisition of the voting rights that go with them. If the articles of association contain, for example, a percentage hurdle of 3 percent, a shareholder can certainly purchase 10 percent of all shares, but will be registered in the share register as a voting shareholder only in respect of 3 percent of the shares. For shares exceeding the percentage limit, the voting rights lie dormant, but not the property rights (in particular the right to a dividend; CO 660 I). For these shares, the acquirer is entered into the share register as a shareholder without the voting rights. Such provisions in the articles of association are designed in particular to make hostile takeovers of the company more difficult. Since the percentage limit can easily be evaded by persons working together as a group and dividing up the share package exceeding the limit, the articles of association normally contain further provisions covering the different cases in which several persons can be deemed to be shareholders (so-called "group clauses").

207 (ii) *Fiduciary clause*: The company can furthermore refuse registration in the share register if the acquirer at its request does not explicitly declare that he has acquired the shares in his own name and for his own account (CO 685d II). This declaration is also designated a "fiduciary declaration" and is meant to prevent the circumventing of the limit imposed on shares carrying voting rights. If the declaration is not given, the acquirer is entered into the share register only as a shareholder without voting rights.

208 (iii) *Foreigner clause*: A registration in the share register constituting a violation of a Federal Act limiting the circle of shareholders can be refused. This regulation was introduced to cover cases where foreign persons buy shares of Swiss companies that by law must remain predominantly in Swiss hands. Examples of this can (still) be found in the Federal Act on the Acquisition of Real Estate in Switzerland by Non-Residents (the so-called

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56 If registered shares listed on a stock exchange are acquired through inheritance or distribution of an estate or under matrimonial property law, the company cannot reject the acquirer in any circumstances (CO 685d III). Unlike the statutory restrictions on the transferability (CO 685 I), however, here the transfer by debt enforcement proceedings is not exempted from being restricted.

57 Such provisions in the articles of association can be formulated as a potential regulation that gives the board of directors the possibility - provided the principle of equal treatment is respected (CO 717 II) - of also recognising shareholders whose holdings of shares exceed the percentage limits set down in the articles of association.

"Lex Koller") or in banking legislation[58]. This provision known as the "foreigner clause" is increasingly losing its force, mostly on account of the growing ties with the European Union; its practical importance is at present already very limited.

209 In respect of the transfer of voting rights, the law makes a distinction according to whether registered shares listed on the stock exchange are acquired on the stock market or off-exchange:

210 (i) *Stock market acquisition*: If quoted registered shares are sold on the stock exchange, the selling bank informs the company without delay of the name of the seller and the number of shares sold (CO 685e). Subsequently, the company deletes the seller as a shareholder from its share register. The seller's rights as shareholder thus disappear. The property and other rights are transferred to the acquirer with the transfer of the shares (CO 685f I). Until the acquirer is recognised by the company, he can neither exercise the voting rights nor any other rights to which he is entitled by the shares. In the exercise of all other shareholders' rights, in particular the pre-emption right (*cf.* CO 652b), however, the acquirer is not restricted (CO 685f II). If the acquirer is not recognised on account of restrictions on the transferability, he remains the owner of the shares and is entered into the share register as a shareholder without voting rights who does, however, have all property rights. The shares involved are regarded as not represented at the general meeting (CO 685f III). It is not uncommon for acquirers of shares to refrain from requesting to be registered in the company share register. They restrict themselves to drawing the dividends via their custodian bank, *i.e. de facto* anonymously. Such shareholders are referred to in Switzerland as "Dispo-Shareholders". Their presence, which breaks the link between risk and co-determination, not uncommonly amounts to up to 50 percent in Swiss publicly traded companies, and this state of affairs is undesirable in both legal and economic terms[59].

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211 (ii) *Off-exchange acquisition*: If listed registered shares are acquired off-exchange, the property and property rights pass on to the acquirer as soon as he has submitted his request to the company to acknowledge him as a shareholder (CO 685f I). The voting rights in this case as well lie dormant until the recognition of the shareholder (CO 685f II).

212 Both in the case of stock exchange and off-exchange acquisitions, the acquirer's request for recognition, *i.e.* for registration as "shareholder with voting rights" in the share register, must be rejected by the company within a period of 20 days following receipt; if the company fails to do this, the acquirer is deemed to be a shareholder with voting rights (CO 685g).

213 From the point of view of the company there can therefore be four types of shareholders with registered shares listed on the stock exchange: (i) shareholders registered in the share register with voting rights; (ii) shareholders registered in the share register without voting rights; (iii) shareholders who have acquired shares, but have not made themselves known to the company (the so-called "Dispo-Shareholders"); and (iv) shareholders who are registered in the share register, but have

58 The "Lex Koller" was relaxed considerably in several revisions, most recently as of 1 April 2005. On 4 July 2007, the Federal Council announced its intention to repeal the "Lex Koller" and thus allow foreigners to also acquire land for housing purposes in Switzerland. The repeal shall, however, not take place before a period of three years in order to give cantons and communes enough time to implement accompanying measures to avoid the negative effects of a boom in the construction of holiday homes.

59 As a corrective aimed to solve the problem of "Dispo-Shares", there exists the possibility of an active effort by the intermediaries (*i.e.* buyer banks) to ensure the registration of their clients, or there are nominee solutions as is customary in the USA for example, *i.e.* the registration of registration companies acting openly as fiduciary institutions in the place of individual shareholders. The articles of association of numerous Swiss publicly traded companies partly admit nominee contingents, and register them up to a certain upper limit without verifying their status as shareholders with voting rights.

sold their shares off-exchange without the acquirer informing the company. Despite restrictions on the transferability, companies can thus have no complete overview of their registered shares owners and the prevailing power relationships, especially since the "Dispo-shareholders" can in most cases gain the voting rights at any time by declaring their holdings for registration in the company ledger.

3.2.5.4 Restrictions on the transferability of unlisted registered shares in the articles of association

214 For restrictions on the transferability of unlisted registered shares, *i.e.* covering "private" companies limited by shares, the law grants a greater degree of latitude (CO 685b et seq.). In contrast to restrictions on the transferability of listed registered shares, an unlisted company limited by shares can impose restricted transferability on its registered shares in the course of acquisitions through legal transaction by preventing the transfer as such and not just the transfer of voting rights. The ownership of the shares and all associated rights remain in such cases with the seller (CO 685c I).

215 In the case of unlisted registered shares, the following possibilities for restricting transferability are permissible, but must always be specified in the articles of association:

216 (i) *Good cause*: The company can reject an application for registration provided it gives an important reason ("good cause") as specified in the articles

67

of association (CO 685b I)[60]. The law makes reference to two states of affairs in particular that constitute good cause, but they must both be named explicitly in the articles of association (CO 685b II):

217 A restriction on the transferability of shares can primarily serve to maintain economic independence. Thus, the permission to transfer the shares can be refused if there is a rival behind the purchase or if there is generally a specific suspicion that the purchase of the shares is connected with a takeover of the company or a change in control. As with registered shares listed on the stock exchange (*cf.* CO 685d I), a percentage limitation on the acquisition of shares is also possible here.

218 As a means of limiting the circle of shareholders with the view of attaining the company objective, it is also possible to restrict transferability. A company limited by shares can, for instance, allow shareholders only of a certain profession or industry.

219 (ii) *Takeover bid*: The application for consent can also be refused by the company if it offers to take the shares from the seller, but not from the buyer, for its own account, for the account of other shareholders or for third parties at the "true value" at the time of the application (CO 685b I)[61]. This possibility allows "private" companies to bar third parties from membership on any grounds at all and thus borders on arbitrariness, but only if the shares are bought from the shareholder willing to leave at their "true value". This "true" or "intrinsic" value is determined on the basis of the company value in terms of underlying assets and earnings value (BGE 120 II 259)[62]. The offer to buy the shares must be submitted to the seller within three months following receipt of the

60 The criterion of good cause could well be identical here with "important material grounds" established in expert opinion and practice that are required for the withdrawal of the pre-emption right (CO 652b II; *cf.* BGE 121 III 219). *Cf.* also N 244 below.

61 This provision is also referred to as an "escape clause" because it enables the shareholder willing to sell to leave the company even in cases where the buyer is rejected. The company can aquire up to 20 percent of its own share capital in the context of this "escape clause" for its own account. The acquired own registered shares in excess of 10 percent, however, must be sold within two years or cancelled through a reduction in capital (CO 659 II). *Cf.* N 158 et seq. above.

62 *Cf.* also N 175 et seq. above.

acquirer's application for recognition by the company (CO 685c III). If the seller declines the offer, the transfer does not take place and he remains a

68

shareholder. In no circumstances does the acquirer obtain ownership or shareholders' rights from the share(s)[63].

220 (iii) *Fiduciary clause*: The company limited by shares can - as in the case of listed shares (*cf.* CO 685d II) - additionally refuse registration in the share register if the acquirer does not explicitly declare that he has acquired the shares in his own name and for his own account (CO 685b III).

221 As long as the board of directors withholds its consent for the transfer of restricted shares, the ownership and all associated rights remain with the seller. Not until the approval has been given do these rights pass on to the acquirer (CO 685 c I). Nonetheless, the company limited by shares or its board of directors has to decide on the acquirer's application for registration in the share register within three months; if the board of directors does not reject the application within this time period, consent is deemed to have been given (CO 685c III)[64]. If, however, the shares have been acquired by inheritance or distribution of an estate or under matrimonial property law or debt enforcement proceedings, the company may reject a request for consent only if it makes an offer to the acquirer to acquire the shares at their true value (CO 685b IV). In the case of these special forms of acquisition there is thus no cost-free refusal available. In these cases there is also a splitting of the shareholders' rights: the ownership of the registered shares and their associated property rights (in particular the right to dividends; *cf.* CO 660 I) are transferred to the acquirer immediately, the rights of participation on the other hand are not passed on until the company has given its consent (CO 685c II).

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63 The acquirer as well as the shareholder who is selling can demand that the "true value" be determined by the court in whose jurisdiction the company's registered office is located. The valuation costs are borne by the company (CO 685b V). If the seller (or, in case of a statutory transfer, the acquirer) does not reject the takeover offer within a month of becoming aware of the true value, the offer is regarded as accepted (CO 685b VI).

64 By means of a provision in the articles of association, the general meeting can also be given the power to approve the application for consent to the transfer of registered shares (*cf.* CO 716 I).