Contents:

The New Limited Liability Company Law

On December 16, 2005 the Swiss Parliament adopted the new Limited Liability Company Law ("LLC Law"), together with some further legislative changes in the area of Swiss Company and Commercial Law (see the following article of this newsletter). Various weaknesses of the Limited Liability Company Law of 1936 were eliminated and significant improvements were introduced. Many of the new optional norms under the LLC Law provide suitable flexibility to the shareholders (Gesellschafter). The revised LLC Law will enter into force at the beginning of 2008.

In the future a **limited liability company** ("LLC") **may be formed** as a *single shareholder company* by a natural or juridical person, whereas under the current law at least two persons are necessary. In addition the LLC will also be allowed to pursue *non-economic purposes*. The minimum amount of CHF 20'000 for the *nominal capital* will be retained but the current ceiling of CHF 2'000'000 will no longer apply. Since the *company shares must now be paid in full* the subsidiary joint and several liability of the shareholders is abolished. With the elimination of this joint and several liability an individual shareholder no longer assumes the risk of liability for the unpaid shares of another shareholder in connection with a capital increase. The bankruptcy of a shareholder cannot any longer lead to the dissolution of the company. In case of a capital increase a simple majority of votes of a shareholder meeting will suffice. The requirement of a unanimous decision will cease to apply.

The provisions relating to the **company shares** were revised completely. In future, a shareholder may own more than one company share. Furthermore, the *minimum nominal value* will be reduced from CHF 1'000 to CHF 100. The *transfer or assignment of company shares* will no longer have to be registered in a public deed – written form will suffice. On the other hand the rules on the contents of a transfer agreement (assignment) have been tightened. As in the subscription deed such transfer agreement must make a reference to provisions in the articles of association. In particular such references must be made with relation to an obligation to make further capital contributions or to perform additional services as well as to the existence of non-competition clauses, pre-emplion rights of shareholders or contractual penalty clauses. The duty to submit each year a list of the shareholders has been eliminated. The new rule abolishes the mandatory consent of 3/4's of the shareholders to the *assignment of a company share* and only provides for this as optional law. This means that the articles of association may limit or even abolish the requirement of consent. It follows that the articles of asso-ciation may also completely restrict any transfer of company shares. A shareholder willing to assign his shares must therefore attain the consent of his co-shareholders as required by law or the articles of association. If he fails his only remaining option will be to sue in court and require a right to withdraw based on valid reasons. More extensive reasons for withdrawal or expulsion of shareholders must be defined in detail in the articles of association.

The withdrawal of a shareholder based on such valid reasons will give him a right to an **indemnification** corresponding with the intrinsic value of his share in the company. If a withdrawal or an expulsion is based upon provisions of the articles of association the calculation of the indemnity may be modified. Any such indemnification will become due for payment only if and when the company disposes of freely available share capital. Alternatively the shares of the leaving shareholder may be sold or the nominal share capital of the company may be reduced if and to the extent this procedure is in compliance with the corresponding provisions. As long as the leaving shareholder has not been indemnified in full he is entitled to demand that the company appoints an auditor.

Presently the ability of a LLC to hold **its own shares** was not restricted if such shares were fully paid in. The new law restricts the acquisition of such own shares to 10% of the nominal capital and follows the general provisions in the corporation law. In connection with transfer restrictions or the withdrawal or expulsion of a shareholder the company may acquire up to 35% of its shares provided however that within two years this quota will be reduced again to 10% or that the capital of the company is accordingly reduced.

The revision clarified also the hitherto disputed issue of **the admissibility of participation and/or profit sharing certificates**. With regard to the profit sharing certificates the new law refers to the corporation law, whereas participation certificates will not be allowed anymore in the future. Insofar as such certificates exist they will be converted within a period of transition into ordinary shares with the same pecuniary rights as all other ordinary shares.

The revised law maintains the possibility to oblige shareholders by provisions of the articles of association to make **supplementary contributions** and/or to perform **additional services** to the company. In the future such supplementary contributions will be limited to twice the value of a company share. Supplementary contributions may be called by the manager only if the balance sheet shows a deficit and/or if the company cannot continue its business without additional funds or if the need for further share capital is defined in the articles of association. The obligation to perform additional services may only be enforced in order to serve the purpose of the company to maintain the independity of the company or to secure the composition of the shareholders. Any obligation to make supplementary contributions to the company which exceeds the nominal capital by a factor of two may be reduced only in accordance with the rules of the revised law even after the expiration of the transitional period of two years.

Under the new laws the company may dispose of the compulsory appointment of an **audit company** only under certain conditions. The existence of such conditions must be proven to the commercial registry office. When the new law has come into force it has to be assumed that each LLC must appoint an audit company. Any waiver of the shareholders to appoint an auditor which is not notified to the commercial registry office will lead to the assumption that the company suffers from a organisational deficit, which will lead to corresponding steps on the part of the registrar of the commercial register (see also in this regard the following article with respect to organisational deficiencies).

In future, each shareholder will be able to request from the managers information concerning all affairs of the company. If the company does not have any auditor, the shareholder furthermore has an unlimited right to inspect the books and records himself. If an auditor has been appointed, the shareholder must, for the enforcement of this inspection right, show a justified interest in the course of such an inspection. Shareholders must observe the duty of loyalty. The managers, however, may refuse the **right of information and inspection** if a danger exists that the shareholder will use the knowledge obtained to the detriment of the company or for purposes unrelated to the company.

As in the case of a corporation, the LLC must be represented by a person domiciled in Switzerland. This requirement may be fulfilled by a manager or, in future, also by an executive director. As in the corporation law the allocation of competences between the **managers** and the **shareholders** has been restricted by rules, which restrict the delegation of certain powers. The new law also allows to request in the articles of association that the managers must present certain matters to the shareholders meeting for approval. To specify such a request in the articles of association it makes sense particularly if a daughter company in the form of a LLC is to be managed in conformity with the rules of a parent company. By reserving the right of consent in certain matters the parent company secures the ability to intervene directly into the affairs of this subsidiary. It is yet unclear what influence the reservation of consent will have on the liability of the managers and/or the shareholders.

Under the new law the articles of association may introduce a **veto right** to individual shareholders of the LLC and thus make such a company to an interesting tool in estate planning. Until now, a veto right could only be achieved on a de facto basis, through a varying allocation of the voting rights per company share. This latter option is possible under the revised law but only to a limited extent. If the articles of association stipulate that the voting right is one vote per share, the relationship between the smallest and the largest nominal value is not permitted to be greater than 1 to 10 regardless of the nominal value. Existing company shares with differing voting rights will continue to remain valid following the effective date of the LLC Law.

The **terms and conditions of the law applying to the transition period** between the old and the new law will be outlined in the following article on the revision of the corporation law. In this context it is sufficient to state that the adaption of the articles of association and the subscription of unpaid nominal capital must take place within two years after the new law has been put into force (i.c. until the end of 2010).

The harmonization between the corporation law and the LLC Law has developed to an extent that leads to an increased numbers of cross references in the new LLC Law (inter alia with respect to contributions in kind, pre-emptive rights, loss of capital). Consequently some differencies in language had to be corrected.

The adjustments made to the new LLC bring a genuine relief and will make this kind of company to genuine alternative to corporations. This includes in particular the possibility to create subsidiaries for groups of companies. The legal form of the LLC is still structured as a person-oriented company limited by shares and leaves leeway to adapt the international structure to the needs of the persons involved.

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PS. Dr. Hans-Rudolf Staiger, Partner of Staiger, Schwald & Partner, has published an article on the LLC Law of Switzerland in the "Handbuch des internationalen GmbH-Rechts", p. 1385 ff., edited by Dr. Rembert Süss, Attorney-at-Law, and Thomas Wachter, Notary, published by zerb Verlag GmbH, D-Angelbachtal, 2006. ISBN 10: 3-935079-31-1, ISBN 13: 978-3-935079-31-0

The "Minor Revision of the Corporation Law"

In the course of the LLC revision, numerous commercial law provisions have been adapted or fundamentally changed for reasons of harmonization or practicality. Numerous changes run crosswise through the entire Corporation Law - from the incorporation to the establishment of a company name to the liquidation and to the provisions concerning the auditor.

As in the case of LLCs, the new provisions intend to facilitate for corporations, the **formation** of *single-shareholder companies*. The new rules further clarify who may be a founding shareholder. The corporation may be incorporated by one or more natural or juridical persons or other commercial companies. The requirement of at least three founders no longer applies. This new provision provides relief in situations where groups of companies are involved.

The **intention to acquire a contribution** in kind in connection with the foundation (or capital increase) will have to be disclosed only if such an asset is contributed by a shareholder or a person closely associated with a shareholder.

The **establishment of a company name** will now be governed in uniform fashion for all commercial companies. In future, corporations, LLCs and cooperatives must *indicate the legal form* in *the company name*. Logos and other logotypes may continue to be used by way of supplement even if they do not contain any additional specification as to legal form. Companies that are already registered must adapt their company name to the provisions of the new law within two years after the new law becomes effective.

The use of company names that do not correspond with the wording that is entered in the commercial register *and* may be misleading is subject to sanctions. The company name registered in the commercial register must be indicated in full and in unaltered fashion in the business correspondence, on order forms and invoices as well as in public announcements. The **registered company name** must also be used in the Internet in a manner in conformity with law. Evidently, abbreviated names, logos, business names, company signs and similar particulars may continue to be used in future as well.

The signing of the **notification of entries in the commercial register** will in future be governed in a single provision for all legal entities. The *supreme direction and management body* is responsible for the notification of any entry in the commercial register. In the case of *corporations*, the notification must be signed by two members of the board of directors or by one member with single signatory power.

In accordance with a desire for simplification, the requirement that the members of the board of directors must be shareholders of the company will be dispensed with. Accordingly, *no* **mandatory or qualifying share for board members** will be necessary any more. As a consequence, an express right on the part of the board members to participate and submit motions at the shareholders' meeting will now be stipulated. In this regard, however, the question arises as to how in future the provision on the universal meeting, pursuant to which all shareholders may hold such a meeting without adhering to the requirements as to form for the calling of the meeting, is to be interpreted.

Similarly, the **requirements as to domicile and nationality** for the members of the board of directors will also be relaxed considerably. In future, the company must be represented by a person domiciled in Switzerland, although this requirement may be fulfilled by a member of the board of directors or an executive director. It will thus be possible in future that none of the board members is domiciled in Switzerland. With the elimination of the domicile requirement, it will become more difficult to sue a board member who has engaged in misconduct based on liability.

In connection with the redemption of shares, the **shareholder rights** are subject to a new rule in the event of a reduction in the company's capital. If the capital of the company is reduced to zero and subsequently paid in again in the full amount the shareholders retain under the present law their position as shareholder including a minimal voting right. irrespective of the cancellation of their shares and even if they do not participate in the subsequent restitution of the share capital. Under the new law the shareholders rights – including the voting right – will cease to exist. In connection with the restitution of the share capital the former shareholder is nevertheless entitled to an unconditional and non-deprivable preemptive right.

The procedures with regard to the restructuring of a company in case of **deficiencies in its organization** have undergone a complete modification. If a company lacks one of the executive bodies that is prescribed or if one of the prescribed bodies is not duly constituted, a shareholder, a creditor or even the registrar of the commercial register will be able to request the court to take the *required measures*. It is then the responsibility of the court to take the appropriate measures to enforce the provisions of law.

The **deletion of members of executive bodies and powers of representation** in the commercial register is also subject to a new rule. It is basically the responsibility of the company to promptly delete persons entered in the commercial register as members of executive bodies when such persons withdraw from office. However, because the mandate of members of executive bodies will terminate in each case in peremptory fashion upon their withdrawal, both the resigning persons as well as third parties have a relevant interest in an immediate correction of the commercial register entry. Thus mistakes through entries that have become incorrect and possible consequences in terms of liability are avoided. In future, withdrawing persons may therefore also effect their deletion *themselves, immediately* – without the 30-day period. Based on the definition of the member of a executive body as an organ of the company, the liability must cease at the point in time in which the ability to influence decisions of the company ceases to exist. The liability continues to exist only if the relevant executive body fails itself to ensure that the entry in the commercial register is immediately deleted.

In future, the **dissolution of the company, with liquidation**, is deemed to be an "essential decision" of the shareholders' meeting and, therefore, requires a *qualified quorum*.

The duty of the corporation to appoint an **auditor** will in future depend on certain requirements. These requirements apply not only to corporations but also, by means of cross-references, to LLCs and cooperatives. Similar provisions will in future also apply to associations and foundations. Through this new rule, the legislators wish to do justice to the varying auditing needs of small and large enterprises. The duty to have accounts audited will no longer be determined by the legal form of the relevant company but will generally be determined for *all commercial companies* based on their size and *economic importance* (public company, larger and smaller enterprises). In this regard, a distinction will be made between the ordinary and *limited audit*. This distinction is drawn, on the one hand, based on the *content, intensity* and *volume of the audit* and, on the other hand, based on the technical requirements or qualification criteria of the auditor. The *ordinary audit* is required for all public companies, all companies that fulfill two of the following criterias - balance sheet total of CHF 10 million, sales revenue of CHF 20 million, 50 full-time employment positions – and all companies that are subject to a duty to prepare consolidated financial statements. An ordinary audit must also be conducted if requested by representatives of 10% of the capital or if the articles of incorporation stipulate such an audit. The ordinary audit foresees a comprehensive report to the board of directors and a summary audit report to the shareholders' meeting. The tasks of the ordinary audit are now specified by law. In future, enterprises must also demonstrate the existence of an internal controls system (ICS). The ICS relates to all procedures, methods and measures introduced by company management to ensure a proper course of operative events. If the requirements for an ordinary audit are not fulfilled, the annual financial statements must be subject to a limited audit. The *limited audit*, the so-called *review*, will introduce a new form of annual audit into Swiss company law, which will merely consist of a summary audit report to the shareholders' meeting. The report includes interviews with management, appropriate detailed examination and analytical audit operations. With the consent of all shareholders, even the limited audit may be waived if no more than ten full-time employment positions exist. In general, numerous uncertainties still exist in terms of the structuring and implementation of the new audit duty.

According to the **transitional provisions**, the new law is directly applicable to existing companies as from its effective date. If the current organization of the company does not comply with the revised provisions of law, an adaptation period of two years as from the effective date of the law will apply. The auditor – where required – is to be appointed as from the first fiscal year that begins on or after the effective date of the law.

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