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Revised Swiss Insider Rules—A Change of Paradigm

Reference: CapLaw-2009-1

Rules on criminal insider trading have been introduced in the Swiss Penal Code more than 20 years ago, but only very few persons have actually been convicted. This situation is likely to change following a recent amendment of the law by which the term (price sensitive) 'fact' has been expanded significantly. Indeed, although barely noticed by the wider public, the revised law has led to a change of paradigm in Swiss insider legislation. The amendment is likely to have implications on regulatory as well as self-regulatory rules. This article will shed some light on the amendment as well as the Swiss regulatory regime on insider trading and market abuse in general.

By Philippe Weber / Petra Ginter / Gian-Andrea Caprez

1) The Regulatory Regime on Insider Trading

Switzerland is not a member of the EU or the EEA and, hence, generally not bound by EU regulations on insider trading. The various standards addressing insider trading and fair market conduct are set out in various statutory provisions as well as regulatory rules ranging from criminal provisions to regulatory and self-regulatory rules. The most important provision, however, is article 161 of the Swiss Penal Code (PC).

a) Insider Trading under Criminal Law (article 161 PC)

What is insider trading: Article 161 PC incriminates, in essence, the misuse of privileged material non-public information. Article 161 (1) PC states that any person who, as a member of the board of directors, the management, the auditors or as agents of a company or its subsidiary or its parent company, as member of a government agency or as a public servant, or as auxiliary person of the afore-said, enriches itself or any other person (i) by taking advantage of the knowledge of material non-public facts whose disclosure will, in a foreseeable way, substantially influence the price of stock or other securities of a company or options thereon which are listed or pre-listed on an exchange in Switzerland, or (ii) by directing such material non-public facts to any third party, shall be punished with imprisonment up to three years or fine.

Who can be punished as primary insider: Importantly, only the type of persons expressly mentioned in article 161 (1) PC who have access to material, non-public information due to a privileged position *(Sonderdelikt)* qualify as ***primary insiders*** and, thus, can be punished under article 161 (1) PC. Accordingly, unlike in many other jurisdictions, shareholders who, by holding a sufficient amount of stock, have access to confidential information of the company are not listed in article 161 (1) PC. A shareholder would, nevertheless, become an insider if, due to its effective influence on the company, it qualified as a *de facto* officer.

Can tippees be punished: In addition to primary insiders, according to article 161 (2) PC, so-called ***tippees*** can be punished with imprisonment up to one year or a fine, if they receive the insider information (directly or indirectly) from a primary insider and enrich themselves or a third party by use of such information.

Significantly broadened definition of the term 'fact' under the revised law: As per 1 October 2008, the Swiss legislator expanded the scope of application of the insider trading provision by ***deleting para. 3 of article 161 PC.*** Para. 3 held that only upcoming initial public offerings, mergers and acquisitions or similar facts with comparable consequences were considered as facts that constituted privileged information the misuse of which could potentially lead to criminal sanctions against an insider. Under the revised law, the misuse of privileged information is no longer tied to a prescribed list of material facts.

Upon the deletion of the material list of relevant events, potentially ***all facts*** within the issuer which will significantly affect the market price of the securities in a foreseeable manner (both as regards materiality and direction), are considered relevant. This important development leads to a ***change of paradigm in Swiss insider law.*** For example, under the old law, financial information (*e.g.,* such triggering profit warnings) or results of clinical trials were, in principle, not covered by article 161 PC. The scope of (criminal) insider trading was hence extremely narrow and limited to material M&A and related activities.

Consequently, the question arises what ***'fact'*** means under the revised law. First of all, it can be assumed that the facts as explicitly named in the former para. 3 of article 161 PC, continue to fall within the scope of the law. Furthermore, material financial information will most likely be considered relevant facts under article 161 PC. The same applies to material business developments (*e.g.* important results of a clinical trial) or changes in financial results (e.g. profit warnings). As a rule of thumb, the term 'fact' will have to be interpreted in the same manner as for purposes of ad hoc publicity disclosure rules of the SIX Swiss Exchange (SIX; see below); however, this rule should be applied with caution, *inter alia,* because of the different nature of SIX regulations and criminal law.

Under the new law, the management of a Swiss listed issuer is under the constant risk of infringing article 161 PC because, by definition, management is permanently involved in confidential planning and financial review of the issuer. Thus, at what stage ***plans or projects*** of the issuer can be considered a 'fact' within the meaning of the revised law? Under the former law, the majority of Swiss doctrine held that plans can constitute facts within the meaning of article 161 PC, irrespective of how likely the execution is. In our view, however, the revised law calls for a more ***restrictive interpretation*** whereby the practice of the SIX regarding ad hoc publicity provides useful guidance. According thereto, mere rumours, ideas, planning alternatives and intentions do not trigger ad hoc publicity disclosure obligations. In line therewith and based on the general principle of *'nulla poena sine lege'*, a plan or project should be in a status of having a reasonable chance of being executed to constitute a 'fact' within the meaning of article 161 PC.

b) Other Relevant Rules

Market Manipulation under Criminal Law (article 161bis PC): A person undertaking to *manipulate* a security's price by communicating or distributing 'false' information to the public is not considered to be an insider pursuant to article 161 PC. However, subject to certain conditions being met, such person can be punished for market manipulation pursuant to article 161bis PC.

Ad Hoc Publicity Rules of SIX: Article 72 of the SIX Listing Rules sets out ad hoc disclosure duties for companies whose securities are traded on SIX. Special rules apply to Swiss issuers whose shares are traded on SWX Europe in London. However, due to the planned relocation of trading to SIX in Zurich mid-2009, the respective differences are likely to disappear soon. A breach of ad hoc disclosure duties may result in sanctions by SIX against the issuer. Under SIX Listing Rules, the issuer must inform the market of any price sensitive fact which has arisen in its sphere of activity and is not publicly known. Price sensitive facts are facts which are capable of triggering a significant price change (for further details, see: *http://www.six-swiss-exchange.com/admission/being_public/publicity_en.html*).

FINMA 2008/38 Circular on Market Abuse: Finally, the Swiss Financial Market Supervisory Authority (FINMA) circular 08/38 of 20 November 2008 (FINMA Circular 08/38; *http://www.finma.ch/d/regulierung/Documents/finma-rs-2008-38.pdf*) contains detailed regulations on the use and dissemination of price sensitive information, including examples of permitted and prohibited activities. The circular only applies to certain kinds of entities supervised by FINMA, *i.e.* licensed securities dealers and, within certain limitations, also to banks without securities dealer license and licensed institutions under the Collective Investment Schemes Act. The circular in part goes beyond arts. 161 and 161bis PC and, *inter alia,* intends to close certain gaps between Swiss law and the standards under the Market Abuse Directive of the EU (MAD).

2) Material Implications of the revised Article 161 PC

a) Implications for the Issuer: Organisational Matters/ Share Based Compensation

The provisions of the Penal Code on the ***criminal liability of enterprises are likely to become more relevant*** within the context of insider trading. According to article 102 (1) PC, a crime or offence shall be attributed to the enterprise if committed while it exercises a business activity within the scope of the enterprise and if such act cannot be attributed to a natural person ***due to the deficient organisation of that enterprise.*** In such case, the enterprise can be punished with a fine up to five million Swiss Francs, leaving aside the potential adverse effect in terms of reputation.

This general rule being applied to the above discussed insider situation means that if a criminal offence described in article 161 (1) PC cannot be attributed to a specific insider because of the deficient organisational structure of the issuer, the latter can be punished subsidiarily. In order to avoid such punishment, a company should take the necessary organisational measures which enable it to identify suspects of insider trading offences. In the light of the broadened scope of article 161 PC, issuers of Swiss listed securities should, therefore, consider a ***review of their internal organisation and procedures in terms of (protection against) insider trading.*** Such review could, amongst others, cover the following aspects: (i) Status of existing internal insider policies and organisational regulations, (ii) possibility of blocked or supervised safe custody accounts of employees, (iii) maintenance of insider lists (note: different to article 6 (3) MAD, insider lists are not mandatory under Swiss law), and (iv) appointment of a Compliance Officer to implement, coordinate and supervise all measures to prevent insider trading.

Partly connected therewith, issuers may also have to review their existing procedures for setting-up, structuring and executing ***share based compensation*** schemes. For example, stock option plans as well as allocation and conditions of exercise of related options may (have to) be structured in a different manner in order to reduce the risk of potential insider trading issues.

b) Implications for Planned Transactions

With the broader term 'fact' under the revised article 161 PC, parties involved in transactions of listed companies or relevant Swiss listed securities, more than ever, must consider Swiss insider law implications. *E.g.,* if a party is offered access to information of a Swiss listed company in a due diligence process, the information gained therein may qualify as a fact under article 161 PC. From a Swiss criminal law perspective, this was much less of an issue under the former law where, *e.g.,* financial information or clinical data, was not covered by article 161 PC (see above) and the fact of the transaction as such may even have been exempted from article 161 PC based on the principle that 'nobody can be his own insider'.

The principle of ***'nobody can be his own insider'*** has been developed by Swiss doctrine. It concerns, inter alia, the question of whether, in a takeover situation, an acquirer of shares can be considered an insider or tippee, respectively, pursuant to article 161 PC. A not yet public, however likely to be executed, takeover plan may presumably be qualified as privileged material confidential information in the sense of article 161 PC. Nonetheless, the prevailing doctrine holds that the acquirer does not qualify as an insider, or tippee respectively, in the case of a planned takeover because such plan is built in its own 'mind' and based on its own decision. *E.g.*, the above mentioned FINMA Circular 08/38 lists amongst permitted activities the purchase of securities of the target company by the potential acquirer itself, or by appointed third parties on account of the former, in preparation of a takeover. The circular also explicitly permits the repurchase of own securities within the framework of a share buy-back program pursuant to Release No. 1 of the Swiss Takeover Board regarding Equity Security Repurchases. It should be noted, however, that also Release No. 1 defines certain periods during which buy-backs must be suspended taking into account potential insider issues.

The rule that 'nobody can be his own insider' may no longer protect a party if such party acts based on ***price sensitive information which is not (clearly) related to the transaction*** in question. The issue is of particular importance in difficult market circumstances in which a potential counterparty to a listed company may no longer be able or willing to solely rely on publicly available information about the listed company before entering into a transaction.

Consequently, ***under the revised law, parties to a potential transaction will increasingly have to consider means to mitigate the risks of insider trading*** whereby traditional measures, such as the execution of confidentiality and standstill agreements and the keeping of insider lists, may not suffice in all circumstances.

SIX Swiss Exchange: Changes effective as of 1 January 2009 (or as indicated below)

Reference: CapLaw-2009-2

By Andrea Huber

Disclosure of shareholdings pursuant to article 20 Stock Exchange Act (SESTA) will have to be published by the issuer via the electronic publication platform operated by the SIX Disclosure Office (DO Publication Platform): The obligation to publish the notification in the Swiss Official Gazette of Commerce and in one of the main electronic media publishing stock market information has become obsolete. The Directive on Electronic Publication and Reporting Platforms issued by the SIX Admission Board provides technical details as well as the conditions how to use the DO Publication Platform (for further details see *http://www.six-swiss-exchange.com/admission/being_public/disclosure_en.html*).

SIX Group decides to reorganize securities market regulation and supervision of issuers and exchange trading: Regulatory and supervisory functions will be organizationally segregated from the operative business of the exchange. Moreover, the separation of powers of rule-making, rule-enforcement and adjudicative bodies shall be reinforced. Going forward, the former Admission Board will be known as the Regulatory Board and will be responsible for enacting rules governing issuers as well as market participants. The SIX Exchange Regulation division will be responsible for the enforcement of the rules and regulations. It will combine the Listing & Enforcement function for issuers as well as the Surveillance & Enforcement function for market participants (for further details see *http://www.six-swiss-exchange.com/media_releases/online/media_release_200901071100_en.pdf*).

SIX Swiss Exchange decides to reunify share trading in Zurich by mid-2009, thereby achieving a harmonised regulatory environment for all Swiss stocks. Consequently, trading in the 32 Swiss blue chip stocks (*i.e.*, the shares included in the Swiss Market Index and Swiss Leader Index), which today is conducted on SWX Europe in London, will be relocated to SIX Swiss Exchange in Zurich and be subject to Swiss regulation and supervision only (for further details see *http://www.six-swiss-exchange.com/media_releases/online/media_release_200811110655_en.pdf*).

New Timetable for general revision of SIX Listing Rules/Duty to Publish Listing Notices for Debt Securities (Bond and Derivatives) abolished as per 1 January 2009: The concentration of share trading in Zurich (see above) also has an impact on the almost completed revision of the SIX Listing Rules. Given the new circumstances, the SIX Admission Board has decided to integrate the changes resulting from the concentration of share trading in Zurich into the ongoing revision and to postpone the entry into force of the overall revised regulations until mid-2009. However, the obligation to publish a listing notice in connection with listing of bonds and derivatives will be repealed already with effect as of 1 January 2009 (for further details see *http://www.six-swiss-exchange.com/download/admission/regulation/notices/2008/notice_200811_en.pdf;* full report on revision of SIX Listing Rules to follow in later edition of CapLaw).

New Disclosure Obligations under SESTO-FINMA

Reference: CapLaw-2009-3

By Philipp Candreia

In the course of the reorganization of the supervision of the Swiss financial market under the umbrella of a single financial markets supervisory authority (FINMA; for further details see the article *The New Swiss Financial Market Supervisory Authority and Other Regulatory Features, by René Bösch/Benjamin Leisinger* in this edition of CapLaw), also new disclosure obligations with respect to shareholdings have been introduced (see *http://www.admin.ch/ch/d/sr/c954_193.html*). The new FINMA Stock Exchange Ordinance (SESTO-FINMA) adopts the existing regulations under the former SESTO-

FBC but also contains material new regulations regarding disclosure effective as of 1 January 2009. In brief, noteworthy amendments and clarifications include the following:

Use of E-mails and Telefax/Calculation of Periods: Notifications, applications and other correspondences may also be made by telefax and e-mail. Further, the calculation of the statutory periods (article 8 SESTO-FINMA) and the regulation of the proceedings, including the requirements for an application (article 26 SESTO-FINMA), have been clarified.

Time of Notification (article 11 SESTO-FINMA): If a threshold is exceeded by way of an increase, decrease or restructuring of the share capital, the notification duty is now uniformly triggered by the publication of such changed share capital in the Swiss Official Gazette of Commerce, irrespective of whether the notification is to be made by the company itself or another shareholder.

Calculation of Thresholds (article 12 SESTO-FINMA): The new ordinance clarifies that purchase and sale positions are each to be calculated separately and independently and must be notified simultaneously. The thresholds are to be calculated on the basis of the voting rights pursuant to the entry in the commercial register.

Securities Lending and Similar Transactions (article 14 SESTO-FINMA): If a disclosure threshold is touched in connection with securities lending and similar transactions, such as repurchase transactions, or a transfer of ownership by way of security, the new ordinance explicitly states that disclosure must be made by the acquirer of the securities only (irrespective of which party will exercise the voting rights). Standardised securities lending and repurchase transactions are exempted if made via trading platforms for purposes of liquidity management.

Financial Instruments: Article 15 SESTO-FINMA contains more detailed rules on the disclosure of financial instruments, including such allowing for cash settlement and margin transactions (*e.g.,* contracts for difference or financial futures)

Changes in Relationship between Direct and Beneficial Owner (article 16 (b) SESTO-FINMA): Changes in the relationship between the direct purchaser, indirect purchaser and beneficial owner are explicitly subject to a notification duty.

Tender Offer (article 19 SESTO-FINMA): Different from past practice, during the term of a tender offer the offeror and the persons acting in concert with the offeror only have to comply with the special disclosure of shareholding duties under article 31 SESTA while the general disclosure obligations pursuant to article 20 SESTA are suspended.

Substitute Publication by Disclosure Office (article 23 (4) SESTO-FINMA): If a company fails to publish a notification or publishes an incorrect or incomplete notification, the SIX Disclosure Office may immediately make the necessary publication, at the costs of the company.

Time of Filing for Exemptions (article 24 (3) SESTO-FINMA): The new ordinance explicitly states that applications for exemptions from disclosure duties may, under exceptional circumstances, also be made ex post, after entry into an agreement.

Transitional Rules: Until 30 June 2009 notifications may also be made pursuant to the former regulations under the SESTO-FBC if specifically indicated in the notification and the publication (article 48 SESTO-FINMA).

Swiss Takeover Regime Overhauled

Reference: CapLaw-2009-4

The regulatory framework for public takeover offers in Switzerland has been overhauled as of 1 January 2009. Some changes are due to a codification of rulings previously passed by the national regulator, the Swiss Takeover Board (TOB). Others introduce significant substantive amendments. This article provides an overview of the main changes.

By Thomas Reutter

The regulatory framework for public takeovers in Switzerland consists of the Federal Securities and Stock Exchange Act (SESTA), the Securities and Stock Exchange Ordinance of the Swiss Financial Markets Supervisory Authority (SESTO-FINMA, former SESTO-FBC) and the Ordinance on Public Takeovers Offers of the Takeover Board (TOO). All three acts have been amended as of 1 January 2009.

Bidders

Bidders (Offerors) will have to face a restriction as to the permissible offer consideration in mandatory bids. An exclusive share exchange offer is no longer permissible. Instead, bidders must offer a cash alternative for mandatory bids as of 1 January 2009 (article 43 (2) SESTO-FINMA). It is currently unclear, if the TOB will apply this rule to voluntary offers which, upon consummation, would trigger a mandatory bid obligation. This is generally the case for voluntary offers relating to more than one third of the target company's shares unless the target company has opted out of the mandatory bid regime. Market participants expect the TOB and its supervisor, the Financial Markets Supervisory Authority (FINMA) not to expand the scope of the regime as this would impose unnecessary burdens on voluntary takeover offers unknown in other major jurisdictions.

In addition, bidders will also have to comply with ***additional disclosure requirements in case of exchange offers.*** Article 24 (5) TOO requires the prospectus to contain information about the anticipated effects of a successful offer on the assets and liabilities, financial position and earnings of the company, whose securities are being offered in exchange (usually the offeror). This wording sparked some confusion as to whether—apart from a condensed narrative—also pro forma financial statements would have to be prepared by a bidder of an exchange offer. Given the unduly onerous and sometimes impossible nature of such an undertaking I expect the TOB not to adopt such an approach.

Finally, potential bidders will have to be cautious with public statements under the revised takeover regime. ***A new 'put up or shut up' rule is introduced*** for persons who publicly announce that they consider launching a public takeover offer without complying with the requirements of a formal pre-announcement (which triggers the duty to submit an offer). As of 1 January 2009 the TOB may require such persons to either submit an offer within a certain period or require them to publicly declare that they will neither launch a public takeover offer nor exceed a threshold triggering the obligation to launch an offer within six months (article 53 TOO).

Board of Directors of Target Company

The board of directors of the target company must publish a report in relation to the offer. It can either recommend acceptance or rejection of the offer or remain neutral highlighting the pros and cons of the offer to its shareholders. As of 1 January 2009 such ***board reports will also have to disclose the number of votes cast for and against the decision*** adopted in respect of the offer (article 30 (4) TOO). In addition and with a view to avoiding an unfair promotion of the board of directors' own agenda, any disclosed expected results of the target company must be accompanied by an explanation of the principles governing the disclosed information and the assumptions on which forecasts are based (article 30 (2) TOO).

As of 1 January 2009, the Board of Directors faces a ***further restriction as to defense measures*** in an unfriendly takeover scenario. The list of defense measures that need the prior approval of the shareholder meeting has been expanded (article 36 (2) TOO). For example, it may not acquire or sell assets exceeding ten percent of the earnings power of the target company. It remains unclear whether the notion of the 'earning power' ***(Ertragskraft, rentabilité)*** relates to profit, EBIT or any other financial figure. Moreover, it may not buy or sell its equity securities or the securities offered in exchange, if any and may not grant any options or conversion rights without the prior shareholder approval.

Shareholders

In contrast to the rights of bidders and the board of directors of the target, the rights of the shareholders of the target company have been bolstered under the revised takeover law regime. As of 1 January 2009 ***shareholders holding two percent or more of the voting rights of the target company may request to be admitted as a party*** in the takeover proceedings (article 56 (3) TOO). The 'party status' may be applied for both an ongoing takeover procedure as well as an application for exemption from a mandatory offer. Thus, shareholders may now challenge takeover offers on the basis of disclosure and in certain limited cases also with respect to the terms of the offer. As a result, takeover offers are now subject to increased legal uncertainty and potential delays. A more detailed analysis of the new shareholder rights will be included in the next issue of CapLaw.

Competitors

Competing bidders will be subject to certain formal changes as to the timing of the competing offer, its impact on the initial offer and any amendments to both offers (article 50 et seq. TOO). In particular, ***the initial offer can no longer be withdrawn in case of a competing offer.*** Moreover, the revised TOO now clarifies that the minimum price applicable to any competing offer is the same price that would be applicable to the preceding offer provided the competing offer is subject to the minimum pricing rules (article 48 (3) TOO).

Offer Mechanics

Instead of a lengthy publication in a printed newspaper in both German and French, the offeror now has ***the option to merely publish an offer notice including some minimum details in a printed newspaper,*** provided the full offer prospectus is available on the internet and may be obtained free of charge. The offer prospectus and the offer notice must also be released to the TOB and at least two news providers.

As an additional change to the offer mechanics the new regime ***introduces a mandatory cooling off period of ten trading days after publication of the offer prospectus*** during which the offer may not yet be accepted. This mandatory time window is introduced to settle any objections raised by the shareholders or the target company (in case of an unsolicited offer) against the offer prospectus. Under the old regime, the cooling off period could be dispensed with in a friendly takeover scenario.

Transaction Disclosure

The offeror, persons acting in concert with the offeror, the target company, each other party to the proceedings and—upon order of the TOB—shareholders holding individually or together in a coordinated manner at least 3% of the shares of the target company must disclose on a daily basis all transactions and securities of the target and of any securities offered in exchange, if any (see article 38 et seq. TOO). This notification duty kicks in on the date of the pre-announcement or, absent a pre-announcement, on the date of the offer prospectus and ends upon expiry of the additional acceptance period. The transactions must be disclosed individually and may no longer be notified on an aggregate basis only. Transactions will be published on the website of the TOB. The general rules on disclosure of major shareholdings are suspended during a takeover procedure and replaced by the above more stringent notification duties (article 19 SESTO-FINMA).

Regulatory Proceedings

As of 1 January 2009 the TOB will issue ***legally binding orders*** instead of the non-binding recommendations under the old regime. Decisions by the TOB can be challenged before the FINMA within five trading days. Decisions of the FINMA can be appealed to the Swiss Federal Administrative Court. A further appeal to the Swiss Federal Court is, subject to certain limited exceptions, no longer possible.

The new regime also dispenses with the possibility to obtain an interpretation of takeover laws from the chairman of the TOB ***(Präsidialauskunft; renseignement de la présidence).*** Non binding information as to the interpretation of Swiss takeover law may, however, still be obtained from the secretariat of the TOB.

TOB Clarifies Mandatory Bid Obligation in Case of Share Transfers Among Commonly Controlled Companies

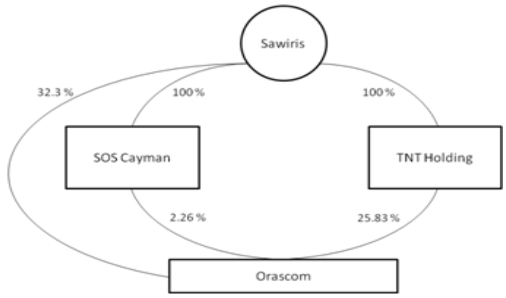
Reference: CapLaw-2009-5

On 3 December 2008, the Swiss Takeover Board (TOB) issued a recommendation regarding Orascom Development Holding AG (Orascom). The TOB ruled that transfers of shares among commonly controlled companies may trigger the obligation to launch an offer for a member of the group holding shares directly—even though the aggregate shareholding of the group or the ultimate beneficial owners is not increased or has not changed—if such direct shareholder exceeds the threshold of 33⅓% of the voting rights. However, in most cases, an exemption (to be formally filed for with the TOB) may be granted.

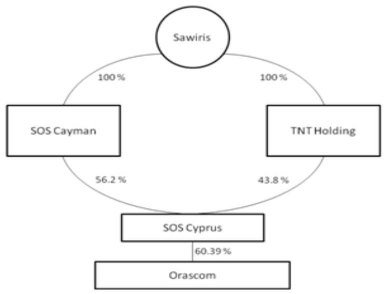
By Frank Gerhard

1) Background

Orascom is a Swiss stock corporation whose shares are listed on the main segment of the SIX Swiss Exchange. Samih O. Sawiris (Mr. Sawiris) holds, directly and indirectly, 60.39% of the voting rights in Orascom: 32.30% are held directly by Mr. Sawiris and 25.83% and 2.26%, respectively, are held indirectly through two wholly-owned holding companies (SOS Holding Ltd. [SOS Cayman] and TNT Holding Ltd., both on the Cayman Islands). The ownership structure is as follows:



Mr. Sawiris intended to reorganize his shareholdings in Orascom by contributing all his directly and indirectly held shares into a newly established SOS Holding Ltd., Cyprus (SOS Cyprus). After the execution of the contemplated transaction, the ownership structure will be as follows:



Mr. Sawiris and SOS Cyprus filed an application with the TOB and asked for (i) a statement that the intended reorganization does not trigger the obligation of Mr. Sawiris and SOS Cyprus to launch a takeover offer and, alternatively, (ii) the granting of an exemption from launching a takeover offer.

2) Considerations of the Swiss Takeover Board

a) Distinction between Beneficial Ownership and Formal Ownership

Pursuant to article 32 (1) of the Stock Exchange Act (SESTA), anyone who directly, indirectly or acting in concert with third parties acquires equity securities, and, by such acquisition, taken together with the equity securities such person already holds, exceeds the threshold of 33⅓% of the voting rights of a target company must submit an offer for all listed equity securities of such a company.

In the present case, the applicants argued that only the acquisition by the ultimate *beneficial owner* of SOS Cyprus—Mr. Sawiris—was relevant for determining the mandatory offer obligation. Consequently, they argued that SOS Cyprus was not obliged to launch an offer, even though its own shareholding was to exceed the threshold of 33⅓% post-transaction. Mr. Sawiris himself would not be subject to a mandatory offer because he already exceeded the threshold on its own prior to the transaction.

The TOB acknowledged—in line with the doctrine—the principle of referring to the economical entitlement for determining the obligation to launch an offer. However, it newly introduced an important distinction: While the mere formal ownership, *i.e.* the holding of shares on behalf of a third party who is also entitled to the rights attached to such shares, does not trigger the obligation to launch an offer, the view of the applicants that in a group of companies, the beneficial owner is the ultimate parent *only* and the shareholding of the subsidiary is of a mere formal nature, was *refused.* According to the TOB, such a conclusion could lead to unwanted consequences: if, for instance, the Swiss subsidiary of a US parent acquired in its own name and on its own account more than 33⅓% of a Swiss listed company, only the US parent would be obliged to launch a takeover offer. This would also be true, if such US parent went bankrupt, because the Swiss subsidiary would then not be obliged to launch such offer. Rather, said the TOB, in a group of companies, *both* the parent company and the subsidiary ***are beneficial owners of the shares held by the subsidiary—but in a different manner;*** therefore, *both* are subject to the obligation to launch an offer. Only in the case of a fiduciary shareholding—with a total split between the beneficial ownership of the principal and the formal ownership of the agent—such a cumulative obligation is *not* triggered. In such a case, the obligation only applies to the principal and not to the agent. One reason for this differentiation is that the principal may, in case of bankruptcy of the agent, claim the shares to which the agent has acquired title in its own name but for the account of the principal (article 401 (3) of the Swiss Code of Obligations). This would not be true in a mere parent–subsidiary relationship.

In the present case, this means that the new SOS Cyprus is in principle obliged to launch an offer as a result of the contemplated transaction since its direct shareholding will exceed the threshold of 33⅓% of the voting rights of Orascom.

b) Exemption in case of Exceeding of the Mandatory Offer Threshold by Members of a Group

Consistent with the above explained clarification that the shareholdings of subsidiaries cannot be considered as a mere formal shareholding, the TOB pointed out that all companies of a group with the same ultimate parent are considered a group for purposes of determining the mandatory offer obligation (rather than the approach of some scholars who considered a group with the same ultimate parent to be just *one* beneficial owner). The transfer of the shares currently held by Mr. Sawiris, SOS Cayman and TNT Holding to SOS Cyprus, which is fully controlled by Mr. Sawiris, is therefore effected within a group.

The consequences of the transfer of voting rights within a group have already been decided by the Swiss Federal Court in the matter *Quadrant* (BGE 130 II 530, c. 5.3). The court stated that even though the group as such is not obliged to launch an offer if the group already exceeded the 33⅓% threshold prior to a transaction, single shareholders or sub-groups are subject to the offer obligation if internal transfers lead to their stake exceeding the threshold. However, in that specific case, article 32 (2) (a) SESTA in connection with article 39 (2) (b) SESTO-FINMA entitles the TOB to grant an exemption. Notably, but appropriate in its result, the TOB considered the fact that SOS Cyprus joined an existing group as a *new* member not being an impediment to the application of article 32 (2) (a) SESTA.

c) Conclusion of the TOB and Consequences for the Practitioner

To summarize, the TOB concluded as follows:

– ***No mandatory offer*** triggered by Mr. Sawiris because he already exceeded—indirectly—the threshold of 33⅓% prior to the reorganization through his wholly-owned holding companies and *no mandatory offer* triggered by TNT Holding because it did not exceed—directly or indirectly—the threshold of 33⅓% before nor after the transaction.

– ***Exemption from the mandatory offer*** obligation for SOS Cyprus and SOS Cayman because both exceeded the threshold of 33⅓% either directly or indirectly. Indeed, since the obligation is only triggered by an internal transfer within the group and the change of control has no negative effects on the minority shareholders of Orascom, the TOB granted an exemption according to article 32 (2) (a) SESTA.

From an economic perspective it is disputable whether the distinction of the TOB between mere formal shareholdings and shareholdings in a group of companies with a common shareholder is based on sound reasons. The newly introduced practice might be counter-intuitive in a world where a consolidated approach is easily taken, namely in takeover matters, where the law itself provides for the concept of 'group' and of 'beneficial owner'. In addition, it is not entirely clear why the situation in a bankruptcy shall legitimate a differentiation between a fiduciary shareholding and the holding by a parent company via its subsidiaries (having in mind that a principal may well go bankrupt, too). In its result, however, the decision of the TOB provides a higher degree of legal certainty—which comes with a price: when reorganizing shareholdings within a group, shareholders will have to carefully look at each beneficial owner, either direct or indirect, and assess for each of them whether a mandatory offer is triggered. If any of such beneficial owners exceeds the threshold of 33⅓%—notwithstanding the aggregate stake of the group will not be increased—a mandatory offer is triggered. If so, such shareholder should apply for an exemption *ex ante* with the TOB. The decisive criterion in such cases is whether or not the position of the minority shareholders will be negatively affected by the internal share transfer. In most constellations, such an internal share transfer will not affect the minority shareholders in any way and therefore, an exemption pursuant to article 32 (2) (a) SESTA should be easily granted.

CapLaw
SWISS CAPITAL MARKETS LAW

Acting in Concert and Judicial Review of Takeover Law—Note on a Recent Decision of the Federal Administrative Court

Reference: CapLaw-2009-6

On 22 December 2008, the Federal Administrative Court ruled in the matter of Martin Ebner and Scor SE v. Swiss Federal Banking Commission. Instead of a decision defining what is a concerted action, the opinion focused on procedural issues and eventually held that the matter was moot as the parties no longer had a legal interest to obtain a ruling on the merits. However, the effects of this ruling are far from trivial, but impact directly the effectiveness of the right to judicial review of parties allegedly acting in concert in view of a takeover.

By Rashid Bahar

It is commonplace to say that tough cases make bad law, but, in the matter of Ebner and Scor SE v. Swiss Federal Banking Commission (now FINMA), the outcome is a strange precedent. The Decision of the Federal Administrative Court B-6110/2007 of 22 December 2008 is an epilogue to the takeover of Converium AG by Scor SE where the Swiss Takeover Board and then the Swiss Federal Banking Commission formally declared that Scor SE and the Swiss financier Martin Ebner, notwithstanding their objections, were acting in concert. Observers who expected a precedent that would clarify what makes a concerted action or a discussion of the evidentiary requirements will be disappointed: as far as substantive takeover law goes, the forty page opinion does little more than confirm the well established principle that regulators and courts ought to show more restraint in holding that parties are acting in concert under takeover rules than when they are applying the rules on the disclosure of substantial shareholdings. Instead, the bulk of the holdings focus on procedural issues, standing to appeal and the conditions to pronounce a declaratory ruling. In other words, this case is a testament to the fact that long gone are the times when takeover proceedings were simple and informal.

First, the Federal Administrative Court held that Martin Ebner and Scor had standing to appeal. It ruled against the Swiss Takeover Board who pleaded that, as the offer was completed and that it was proven that they had complied with their duties under Swiss takeover law, they had no actual legitimate interest to seek the reversal of the decision of the Swiss Federal Banking Commission. The administrative jurisdiction refuted this argument and considered that the appellants had an interest to appeal because their honour and reputation was negatively impacted by the decision and the media coverage of the whole matter (Decision B-6110/2007, c. 1.2).

From there, the Federal Administrative Court went on to hold that a declaratory ruling was admissible under Swiss administrative procedure (Decision B-6110/2007, consid. 2). It opined that the very task of the financial market authorities is to monitor compliance with Swiss laws and regulations governing takeovers and that, in the interest of all market participants, it had to ensure that takeovers take place in a transparent and legally certain environment. Therefore, the supervisory authorities had, by virtue of their statutory mission, an obvious interest to pronounce declaratory rulings. This conclusion holds on the more for the Federal Administrative Court as issuing a declaratory ruling is a far more effective process than ordering the alleged concert parties to comply with a long list of substantive obligations or to wait for a breach before acting.

Having overcome these procedural hurdles, the federal administrative jurisdiction, finally, moved closer to the merits but then held that, insofar the offer was successful and the parties had complied with all their duties as offerors, they no longer had an actual legal interest to solve the controversy (Decision B-6110/2007, c. 3.3.1 to 3.3.4). The case was thus moot and there was no need to decide on the merits of the matter. The Federal Administrative Court grounded this conclusion by the distinguishing between a concert action under takeover law and a concert action under disclosure rules: as these two related parts of Swiss financial markets law have their own definition of when two persons are deemed to act in concert, a ruling under takeover law would have no binding value in a potential administrative or criminal enforcement action regarding a violation of disclosure rules. For the same reason, the Federal Administrative Court held that the alleged damage to the reputation and honour of the appellants could not be remedied through the appellate procedure: the issue was whether they plotted the takeover without disclosing it, thus eventually breaching the rules on the disclosure of substantial shareholdings, but not their obligations under takeover law with which they complied.

Taking one step back, the opinion of the Federal Administrative Court is puzzling: why did the court decide to consider that the parties had a legitimate interest to the proceeding before considering that the controversy was moot and the parties had no legal interest in the matter—which incidentally is usually not required in administrative procedure, as opposed to ordinary civil procedure (Comp. article 6 and 48 of the Federal Act on Administrative Procedure with article 72 of the Federal Act on Federal Civil Procedure)? It is, indeed, odd that the Federal Administrative Court considered that the reputation and honour of the appellants were sufficiently jeopardized by the proceedings to give the appellants standing to sue, while, at the merits, holding that the reputation was not at stake when holding that the parties acted in concert in view of a tender offer. Arguably, the Federal Administrative Court may be applying a two tiered approach: in a first step, it determines whether the appellants have a sufficient interest to give them standing to sue and, in a second, deeper step, it analyses whether the interest really justifies a decision. Nevertheless, the distinction is Byzantine and highly questionable from a pragmatic perspective.

In conclusion, the *Ebner and Scor SE v. Swiss Federal Banking Commission* opinion raises the difficult question of the effectiveness of judicial review in the context of takeover: when administrative agencies declare that parties involved in a takeover are acting in concert, they burden them with cumbersome obligations. Yet, even if they disagree, the parties have hardly any alternative but to comply: the regulatory framework, together with market constraints, limits the timeframe of a tender offer, so waiting for a final judgement on appeal is not a realistic option. Moreover, the consequences of a breach of the duties of an offeror are also such that the alleged concert parties cannot afford to disregard them and gamble for a victory on appeal. An *a posteriori* determination would thus have the advantage of clarifying the matter after the facts for the future. Yet, with this decision, the Federal Administrative Court also closed this avenue to judicial review. Without the shadow of a doubt, the opinion is consistent with the tenets of Swiss administrative procedure, but its practical effects are highly questionable in the light of the constitutional right to judicial review (article 29a of the Federal Constitution).

The New Swiss Financial Market Supervisory Authority and Its Impacts

Reference: CapLaw-2009-7

As per 1 January 2009, the new Swiss Financial Market Authority (FINMA) has taken up its work. Despite not fundamentally affecting the regulatory environment, some changes did come along with the new supervisor. This article serves the purpose of illustrating these new features.

By René Bösch/Benjamin Leisinger

On 1 January 2009, not only the beginning of a new year was celebrated, but also the beginning of a new era of regulatory supervision in Switzerland. As per this date, the Financial Market Supervisory Authority Act (FINMASA) entered into full effect. Formally, on the basis of the Federal Council's Ordinance of 16 January 2008, parts of the FINMASA had already entered into effect on 1 February 2008. This primarily served the purpose of regulating organizational issues and of having a legal basis for the FINMA's beginning with its work.

1) Functions and Organization of the FINMA

As has already been reality in other jurisdictions, the FINMASA merges three supervisory bodies—the Federal Office of Private Insurance (FOPI), the Swiss Federal Banking Commission (SFBC) and the Anti-Money Laundering Control Authority (AML CA) into one supervisory body. In its function of being the sole supervisory authority, supervision regarding banks, insurance companies, stock exchanges, collective investment schemes and securities dealers as well as other financial intermediaries in Switzerland accordingly is now performed by FINMA. The supervision on auditors now also is regulated in a unified way. The new FINMA Financial Market Audit Ordinance since 1 January 2009 uniformly regulates the general requirements for admission of auditors or audit companies in the financial sector, the supervision of auditors and audit companies, coordination between FINMA and the still existing Federal Auditors' Supervisory Agency (RAB), as well as auditing in the financial sector.

Pursuant to the Federal Council's Message to the FINMASA of 1 February 2006 (the Message), the purpose of this reorganization was to benefit from and to fully utilize the existing knowledge and experience of the different regulatory bodies.

In forming FINMA, Switzerland decided to choose the legal status of an independent institution under public law (article 4 (1) FINMASA). As regards the benefits of such a legal form, amongst others, the independence and level of autonomy, the higher flexibility of such a separate entity vis-à-vis the rest of the public administration, or the government's relatively limited liability can be mentioned. In accordance with its legal form, FINMA has a board of directors, an executive board and an external auditor (article 8 FINMASA).

2) Principally Unchanged Banking, Securities Dealers and Insurance Regulation

The goal of the FINMASA was to provide for one single financial markets regulator by implementing a new organizational framework therefor. But the FINMASA was not designed to achieve new or amended substantive financial markets regulation. Thus, regulatory environment is not fundamentally affected by this change. In particular, the specific laws and regulations, *i.e.* the Banking Act, the Collective Investment Schemes Act, the Stock Exchange Act, the Insurance Supervision Act, the Mortgage Bond Act, the Anti-Money Laundering Act or other federal laws and their respective ordinances, are, predominately, only semantically changed. In relation to these existing laws and regulations, the FINMASA applies as a *lex generalis* and in case of a conflict between the FINMASA and specific laws and regulations, the later prevail (article 2 FINMASA). Also the concept of subsidiarity, *i.e.* that regulation should only be introduced where this is necessary, still applies under the new system (article 7 (2) FINMASA). The principle of self-regulation is not affected by the new system, either. This principle is even expressly mentioned in article 7 (3) FINMASA.

3) Changes Caused by the New Regulation

Nevertheless, some new features did result from the new FINMASA.

a) FINMA's Limited Liability

The liability of the FINMA's corporate bodies, personnel or agents is governed by the Liability Act. Here, the FINMASA introduces a first special feature. In addition to the system of contingent liability pursuant to article 19 of the Liability Act with regard to organizations outside the federal administration that perform public functions, article 19 (2) FINMASA states that FINMA and its agents are only liable if they violate fundamental official duties and the damage is not caused by a violation of duties by the supervised financial intermediary itself. The Message states that even the violation of duties of diligence under private law constitutes a violation of duties within the meaning of article 19 (2) (b) FINMASA. The requirements under lit. a and lit. b of article 19 (2) FINMASA are cumulative prerequisites, *i.e.,* only in cases where the damage is due to a fundamental violation of FINMA's official duties and in the absence of any violation of duties by the supervised financial intermediary itself, FINMA would be liable. This limitation of FINMA's liability was introduced because FINMA's duties are rather complex and connected with enormous risks and, in cases where damages in the financial sector were actually to occur, the amount of these damages could be very high. This change certainly is welcomed by persons charged with investigations and restructuring, as well as liquidators appointed by the FINMA, who now also are only personally liable in cases of intentional or grossly negligent behavior. Under the old article 39 (2) Banking Act, which was removed by the FINMASA, such agents were subject to responsibility under the provisions of company law (articles 752–760 of the Code of Obligations) and therefore personally liable even in cases of simple negligence. Some authors, however, criticize this new limited liability. They state that one of the positive side effects of the introduction of a uniform supervisory body also is to strengthen the people's confidence in the financial markets. This side effect, in their view, is reduced by the limitation of the supervisory body's liability in cases of omissions or other violations of their duties.

b) Penal Provisions

Another change is the tightening of the penal provisions for financial markets offences. Pursuant to article 44 FINMASA, whosoever intentionally performs activities that would otherwise require authorization, approval, registration and the like without such authorization, can now be punished with imprisonment of up to three years or a fine. Pursuant to article 44 (1) FINMASA in connection with article 34 (1) and article 34 (2) and article 333 of the Penal Code, this fine can amount to up to CHF 1,080,000 for individuals and up to CHF 5,000,000 for legal entities. In cases of negligence, the punishment is a fine of up to CHF 250,000. In cases where there was a conviction in this regard and the behavior is repeated within a period of five years, the fine is at least 45 day's rates. Similarly, penal offences regulated in other financial market laws were also tightened. The Banking Act (BA), for example, was amended in several ways in relation to the penal provisions. Article 47 BA, providing for the sanctions in cases of violations of the banking secrecy, so far provided for a punishment of imprisonment for not more than six months or by a fine of not more than CHF 50,000; if the act had been committed by negligence, the penalty was a fine not exceeding CHF 30,000. Article 47 BA now provides for a punishment of imprisonment of up to three years and a fine. In cases of negligence, the fine now can be up to CHF 250,000.

Under the Stock Exchange Act (SESTA), to give another example, since 1 January 2009, even negligent failure to disclose shareholdings pursuant to article 20 SESTA is covered by the penal provision of article 41 SESTA, while under the old regime only intentional failure to notify was penalized. It is not entirely clear whether this change also affects a failure to disclose qualified shareholdings in a listed company regarding transactions concluded before 1 January 2009. The characterization of article 41 SESTA as a penal provision, however, should prohibit the application of the new negligence standard on transactions concluded but negligently not notified before 1 January 2009 under the general principle of *'nulla poena sine lege'* and the legal principle that penal measures should not have retroactive effect pursuant to article 1 of the Penal Code. The failure to notify pursuant to article 20 SESTA, in the authors' view, cannot be regarded as being a continuous offence *(Dauerdelikt),* either. Applying the Federal Supreme Court's decisions regarding continuous offences, such an offence only is at hand if the non-disclosure after the conclusion of the transaction and non-disclosure from then on would qualify as one common mischief. In one decision, the Federal Supreme Court came to the conclusion that a continuous offence was not at hand where a woman failed to notify that her financial circumstances had changed and that she, because of this, was no longer entitled to get social welfare. When it comes to the notification requirement under the Stock Exchange Act pursuant to article 20, in the authors' view, the offence is committed in cases of non-disclosure after the lapse of the time-frame of four trading days provided for by article 22 (1) of the FINMA Stock Exchange Ordinance. This view is further supported by the fact that a late notification does not heal the mischief but rather also qualifies as an offence under article 41 SESTA. Consequently, in the authors' view, both the fact leading to the notification requirement and the lapse of the time period must have occurred after 1 January 2009 in order for the new regime to apply.

c) Administrative Sanctions

Another new feature introduced by the FINMASA is the availability of new administrative sanctions. Since 1 January 2009, FINMA can ban individuals from their profession for a period of up to five years (article 33 FINMASA) or can confiscate proceeds that resulted from severe violations of supervisory regulations (article 35 FINMASA). According to the Federal Council's Message, the sanction of confiscation of proceeds primarily was introduced in order to prevent distortion of competition resulting from a violation of regulatory duties.

d) Strengthened Role of the Takeover Board

As a result of the FINMASA and FINMA's new role as a senior supervisory body in some areas, *e.g.,* regarding the supervision of audit companies, the role and competences of other bodies had to be adjusted. The Takeover Board, for example, a federal commission established under the Stock Exchange Act that is competent to issue general rules and ensure compliance with the provisions applicable to public takeover offers, since 1 January 2009 can issue binding orders (article 33a SESTA), rather than only issue recommendations. In order not to prolong the appeal procedure, this order now can only be appealed within 5 trading days in front of the FINMA (article 33c SESTA) and FINMA's decision can be appealed within 10 days in front of the Federal Administrative Court (article 33d SESTA and article 31 et seq. of the Federal Administrative Court Act). The possibility to then file an appeal against the Federal Administrative Court's decision in takeover issues was abolished (article 83 (u) Federal Supreme Court Act). Only in cases of a violation of constitutional rights, the extraordinary subsidiary constitutional complaint pursuant to article 113 et seq. of the Federal Supreme Court Act would be possible.

New Regime Regarding Depositor Protection in Switzerland

Reference: CapLaw-2009-8

Effective as of 20 December 2008, Swiss depositor protection has been improved. The amount of privileged deposits has been increased to CHF 100,000. Moreover, a new system to secure these privileged deposits has been installed by, one the one hand, providing for the banks' requirement to hold domestic security and, on the other hand, by increasing the system-wide protection to CHF 6 billion. Additionally, a flexible approach to satisfy certain claims as quickly as possible outside the schedule of claims was introduced. Finally, the protection of deposits was extended to pension funds of the banks and vested benefits foundations.

By Benjamin Leisinger

The final text regarding a change of the Banking Act (BA) with regard to the protection of bank depositors now adopted by the Swiss Parliament that—due to a resolution to declare the change in the law urgent—entered into force on 20 December 2008, provides for five immediate measures to improve the protection of bank depositors in Switzerland.

Firstly, the ***privileged amount has been increased*** (article 37b (1^{bis}) BA). Under the old law, deposits which were not in bearer form, including medium-term notes *(Kassenobligationen),* and which were deposited with a bank in the name of depositors, up to an amount not exceeding CHF 30,000 per creditor, had been privileged in the bankruptcy of a Swiss bank by being allocated to the second class pursuant to article 219 (4) of the Debt Enforcement and Bankruptcy Act. Under the new provision, an amount of up to CHF 100,000 per creditor is privileged.

Secondly, the system of protection of the bank depositors' assets was improved by installing the banks' obligation in article 37b (5) BA to hold receivables that are ***domestically secured*** or other assets within Switzerland to an extent of 125 per cent. of the amount of privileged deposits. According to the Federal Council's Message, most banks already meet this requirement today.

Thirdly, a ***flexible system of satisfaction of certain claims*** outside the schedule of claims was introduced (article 37a^{bis} BA). Under the existing article 37a BA, insofar as they are contactable, privileged depositors foreseen in Article 37b BA with an aggregate matured claim of CHF 5,000 or less would have been satisfied as quickly as possible outside the schedule of claims and excluding any possibility of set-off. Article 37a^{bis} BA now establishes a more flexible approach. Now, if there are sufficient liquid assets, privileged deposits can be satisfied up to the amount of CHF 100,000 outside the schedule of claims and excluding any possibility of set-off. The amount that is actually to be satisfied pursuant to this fast and simple procedure is to be fixed by the FINMA on a case-by-case basis.

Fourthly, the ***system-wide protection*** was increased (article 37h BA). Under the old regime, the system of self-regulation that ensured that privileged deposits within the meaning of article 37b BA were actually covered only was approved by the Swiss Federal Banking Commission (which together with the Federal Office of Private Insurance and the Anti-Money Laundering Control Authority was merged into one supervisory body, FINMA, on 1 January 2009) provided that it foresaw a maximum amount of 4 billion Swiss francs for the banks' aggregate outstanding contributions due (Swiss bank depositors' protection is financed *ex-post, i.e.* only in case of insolvency of one bank, the other banks' obligation to contribute actually becomes due; the banks, however, are under an obligation to hold liquid funds in an amount of 50 per cent. of their obligation to contribute to the system in addition to their normal legal liquidity). In other words, 4 billion Swiss francs had been protected by the system of self-regulation. Since 20 December 2008, article 37h (3b^{bis}) BA provides for an amount of CHF 6 billion. This amount seems to be sufficient, as the claims to be satisfied by these contributions of the banks only are the difference between the privileged CHF 100,000 and the amount that has already been satisfied outside the schedule of claims pursuant to article 37a^{bis} BA, not the entire privileged amount. The amount was not increased above CHF 6 billion in order not to install a chain-reaction in case of insolvency of one bank.

Fifthly, since 20 December 2008, also ***deposits of pension funds*** *(Vorsorgestiftungen)* of the banks and of so-called ***vested benefits foundations*** *(Freizügigkeitsstiftungen)* are regarded as being the deposits of the insured persons themselves and are—independent from their other deposits with the bank—protected in an amount of up to CHF 100,000 (article 37b (3) BA). This protection, practically, could lead to the consequence that some clients of the respective banks are privileged in an amount of up to CHF 200,000. According to the Federal Council's Message, despite installing this new protection, the system-wide aggregate amount of privileged deposits that would have to be additionally covered is increased by only 5 per cent.

Due to the urgency and the preliminary nature of these changes, the new system will be thoroughly analyzed and, if necessary, improved. In advance of the discussions in and adoption by the Swiss Parliament, however, the Swiss Federal Banking Commission (now FINMA), the Swiss National Bank as well as the Swiss Banking Association have already been consulted. The Swiss Banking Association had criticized that the new requirement to hold receivables that are domestically secured or to hold other assets within Switzerland to an extent of 125 per cent. of the privileged deposits is not appropriate for every bank. This critique led to article 37b (5) BA's wording that the FINMA can grant exceptions from this requirement. Due to this advance consultation, it can be expected that the changes will be upheld and confirmed in the normal legislative process.

FINMA Introduces New Special Capital Adequacy Requirements on UBS and Credit Suisse

Reference: CapLaw-2009-9

By René Bösch

In November 2008 the Swiss Federal Banking Commission (SFBC), the predecessor of the Swiss Financial Market Supervisory Authority (FINMA), reached an agreement with UBS and Credit Suisse to raise current capital adequacy requirements and introduce additional elements to the regime. These new requirements must be complied with by the year 2013.

The Swiss banking regulator felt that the losses of unheard proportions which banks encountered since the onset of the financial crisis in the summer of 2007 called for swift regulatory action. In close collaboration with the Swiss National Bank, the SFBC developed a new capital adequacy regime which it felt would make the two large Swiss banks more resilient. The SFBC (now FINMA) now requires that UBS and Credit Suisse comply with new capital adequacy ratios, in lieu of the previously applicable 'Swiss finish' under Basel II, and leverage capital requirements by the year 2013. The new capital adequacy target will be in a range between 50% and 100% above the Pillar I requirements under Basel II. In addition, the decree includes leverage capital requirements that requires the banks to maintain by 2013 a ratio of core eligible capital to total assets (on a non-risk-weighted basis) of 3% at group level and at 4% for the individual institutions.

Enforceability of Standard Credit Default Swap Contracts

Reference: CapLaw-2009-10

Over the past years, financial institutions have executed many trillions notional value of Credit Default Swap ('CDS') transactions through the ISDA Master Agreement and related documents.[1] To ensure stability of the legal framework based on such standardized agreements, it is important that courts enforce the plain terms of these agreements. Recently, a U.S. District Court provided strong support for the enforceability of standard CDS terms under the ISDA Master Agreement and related documents despite efforts by a hedge fund protection seller to find relief via litigation from the current harsh reality of dropping asset values and rising collateral calls.

by Thomas Werlen/Stefan Sulzer

In July 2007, VCG Special Opportunities Master Fund (VCG) entered into a CDS transaction with Citibank in which VCG sold credit protection to Citibank on USD 10 million of certain Class B Notes issued by Millstone Ltd. (Millstone). VCG v. Citibank, 2008 U.S. Dist. LEXIS 92709, *1 ff. (SDNY 2008). To document the CDS transaction, VCG and Citibank used a 2002 ISDA Master Agreement, the 1994 ISDA Credit Support Annex, and a confirmation letter that incorporated the ISDA Credit Derivatives Definitions.

Only one month after the parties entered into the CDS transaction, Citibank demanded that VCG deposit additional collateral as a result of decreased market value of the Class B Notes. In total, Citibank demanded and received more than USD 7.5 million in additional collateral during the period from August 2007 through November 2007. Finally, in January 2008, Citibank declared a credit event and demanded payment of the full USD 10 million in credit protection. When VCG refused to pay, Citibank seized the collateral and was still owed approximately USD 600,000 under the CDS transaction.

VCG filed suit against Citibank in February 2008. According to the complaint, Citibank breached its contractual obligations under the CDS transaction by, *inter alia,* demanding the additional collateral in the August 2007 to November 2007 period. In addition, VCG sought equitable rescission of the contract based on the parties' alleged failure to reach a full meeting of the minds concerning the terms of the contract. VCG also alleged that Citibank had breached an implied duty of good faith and fair dealing, had unlawfully converted the collateral, and had been unjustly enriched.

Additional collateral. The Court treated the CDS transaction documents as simple contracts that merely required the Court to follow their terms to logical conclusions. With respect to the demanded additional collateral, the Court identified the relevant

1 According to the ISDA Market Survey, the CDS markets exceeded USD 54 trillion notional value as per 30 June 2008 (USD 62 trillion as per 31 December 2007).

clause in the Credit Support Annex and then described the portion of the confirmation letter that incorporated the Credit Support Annex by reference.

Equitable rescission. After strictly holding VCG to the terms of the CDS transaction documents, the Court summarily dismissed VCG's alternative grounds for attacking Citibank's actions. The Court found that rescission was not available to a 'sophisticated hedge fund' under New York law because it appeared to the Court that VCG 'simply failed to review carefully the terms of the parties' agreements.' VCG v. Citibank at *21. As the Court stated, one party's negligence cannot support a claim for rescission of a contract.

Good faith and fair dealing. The Court held that VCG's remaining claims for breach of an implied covenant of good faith and fair dealing, unjust enrichment and conversion were either waived or improperly duplicative of the breach of contract claims.

While specific economic outcomes for particular CDS transactions may result in severe financial difficulties for some parties, the potential damage to the entire financial system could be much worse if CDS trades could be rescinded based on the type of claims asserted by the disadvantaged parties. The VCG decision continues the trend providing legal support for market stability and future credit liquidity. See Eternity Global Master Fund Limited v. Morgan Guaranty Trust Company, 375 F.3d 168 (2d Cir. 2004); Aon Financial Products v. Société Generale, 476 F.3d 90 (2d Cir. 2007); Merrill Lynch International v. XL Capital Assurance, 564 F.Supp. 2d 298 (SDNY 2008).

Implenia: Federal Administrative Court Rules Against Laxey

Reference: CapLaw-2009-11

The Federal Administrative Court has dismissed Laxey's objections to the Federal Banking Commission's (now FINMA) rulings of 7 March 2008 and 12 December 2007. The court confirmed in its two decisions, dated 18 December 2008, that Laxey has failed to comply with stock market notification regulations when it invested in Implenia in early 2007. The system Laxey used, was based on CFDs (contracts for difference), issued by various banks on Implenia shares after Laxey transferred shares to them, allowing Laxey to terminate the CFDs at any point in time and to then purchase the shares, held by the banks to secure their positions. The Federal Administrative Court confirmed the qualification of the Federal Banking Commission that Laxey, by using CFDs, has indirectly acquired the underlying shares and was therefore subject to a notification obligation when it purchased the shares and entered into the CFDs and not when Laxey called the shares at a later point in time.

6. Zürcher Aktienrechtstagung (6th Zurich Conference on Corporation Law)

Wednesday, 25 March 2009 (registration period ends 4 March 2009)

Park Hyatt, Zurich

Chair: Dr. Gaudenz G. Zindel

Speakers: Prof. Dr. Hans Caspar von der Crone, Michael Gwelessiani, Dr. Hanspeter Kläy, Dr. Andreas von Planta, Prof. Dr. Ulrich Seibert, Prof. Dr. Rolf Sethe, Rodolfo Straub, Dr. Gaudenz G. Zindel

Further information and registration on *http://www.eiz.uzh.ch.*

3. Zürcher Tagung zum Wirtschaftsstrafrecht (3rd Zurich Conference on Business Criminal Law)

Tuesday, 31 March 2009 (registration period ends 12 March 2009)

Lake Side Casino Zürichhorn, Zurich

Chair: Prof. Dr. Jürg-Beat Ackermann, Luzern, Prof. Dr. Wolfgang Wohlers, Zürich

Speakers: Prof. Dr. Jürg-Beat Ackermann, Prof. Dr. Gunther Arzt, Dr. Stefan Heimgartner, Saul M. Pilchen, Prof. Dr. Franz Salditt, Dr. Jörg Schwarz, Prof. Dr. Rolf Watter, Prof. Dr. Wolfgang Wohlers, Dr. Urs Zulauf

Further information and registration on *http://www.eiz.uzh.ch.*