THE ONLY GLOBAL ASSOCIATION OF YOUNG LAWYERS

Let´s fight. Minority shareholders and capital investors.

National Report of (Switzerland)

Dr. Paul Peyrot, LL.M.
Peyrot & Schlegel

Beethovenstrasse 47
8002 Zürich
Switzerland
+41 43 500 55 70
paul.peyrot@peyrot-schlegel.ch

Date: 9 February, 2006

1. GENERAL PART ON MINORITY RIGHTS

1.1 Minority shareholders' rights concept

1.1.1 How is the minority shareholder defined in your jurisdiction?

Neither statute law nor jurisprudence define the term minority shareholder. Thus every shareholder having less than 50% of the voting rights is a minority shareholder.

1.1.2 In your jurisdiction, is there the principle of equal treatment of shareholders and how does it protect minority shareholders?

The principle of equal treatment of shareholders is expressly provided for in Art. 717 sec. 2 of the Code of Obligations (CO). The board of directors has the obligation, circumstances being equal, to give equal treatment to shareholders. According to established jurisprudence, also the shareholder's meeting has the same obligation of equal treatment.

Equal treatment of shareholders means that all shareholders are protected against discriminatory treatment. Discriminatory treatment is given, if one shareholder oder group of shareholders has to suffer disadvantages without this being justified by compelling interests of the Company as a whole.

1.1.3 Does your jurisdiction allow the establishment of privileged shares? Which kind of privileged shares are permitted?

Art. 693 CO provides for shares with privileged voting right. The privileged voting right is obtained if shares with different par value all have one vote per share. E.g. shares with a par value of CHF 1'000.- do not have more voting power than shares with a par value of CHF 100.--. With shares of CHF 100.-- the shareholder can obtain disproportionate voting rights in comparison with his investment.

There are limits to the possible privilege of voting rights: first the difference in par value between the normal and the privileged shares may not exceed ten times. Second the privilege in voting rights does not apply in votes regarding the election of the auditors, the appointment of experts for the review of the management, a resolution regarding a special audit and the decision on the initiation of an action for responsibility against directors.

1.1.4 Can minority shareholders exercise their rights jointly to obtain a necessary minimum share for certain actions or qualified minorities?

Yes, this is in most cases even provided for expressely, as in Art. 699 sec. 3 CO: "*The calling of a general meeting of shareholders may also be requested by one or more shareholders representing together at least ten percent of the share capital*."

1.2 Right to call a shareholders' meeting and attend to the meeting?

1.2.1 Do minority shareholders have the right to call a shareholders' meeting?

Yes, see Art. 699 sec. 2 CO cited above.

1.2.2 Is a qualified minority needed?

Yes, the shareholders calling for a shareholders' meeting need to represent either ten percent of the share capital or shares with a par value of one million Swiss Francs.

1.2.3 Does a minority shareholder have a right to bring a matter on the agenda for the meeting?

Shareholders who have the right to call a shareholders' meeting also have the right to bring a matter on the agenda. In fact, if they call for a shareholders' meeting, they have the obligation to formulate a specific motion which can be put to vote.

During the meeting, any shareholder (whithout having to meet a qualified minority requirement) can bring in motions regarding the matters on the agenda for the meeting. However, he cannot not bring in new matters on the agenda, as those would not have been duly announced.

1.2.4 Are there any restrictions for the minority shareholder to attend the meeting?

No. Attenting the shareholders' meeting is considered a fundamental shareholders' right and may not be restricted.

1.3 Right to vote during the Shareholders' Meeting

1.3.1 What are the majority requirements in general?

According to Art. 703 CO, the general meeting of shareholders passes resolutions and carries out elections by absolute majority of the votes allocated to the shares represented, to the extend the law or the articles of incorporation do not provide otherwise.

1.3.2 Which key resolutions require a greater majority?

A double qualified majority (i.e. two thirds of the votes represented and the absolute majority of the par value of the shares represented) is required in the following cases (see Art. 705 CO): (1) change of the purpose of the Company, (2) the creation of shares with privileged voting right, (3) the restriction of the transferability of registered shares, (4) an increase of capital, authorized or subject to a condition, (5) an increase of capital out of equity, against contributions in kind, or for the purpose of acquisition of assets and the granting of special benefits, (6) the limitation or withdrawal of preemptive rights on newly issued shares, (7) the change of domicile of the Company, (8) the dissolution of the Company whithout liquidation.

1.3.3 To what extent can these requirements be modified by the Articles of Association?

The Articles of Association may set higher majorities required, but not lower.

In order to introduce higher majorities than those provided for by the law, the same double majority in the vote needs to be reached (i.e. two thirds of the votes represented and the absolute majority of the par value of the sahre represented at the meeting).

1.4 Right for information

1.4.1 Does a right of information exist and what is the extent of the information that can be obtained?

First, each shareholder has the right to obtain a copy of the Company's business report and of the auditor's report (Art. 696 CO).

A specific right of information and of inspection (of the books of the Company) is provided for in Art. 697 CO. Any shareholder is entitled to request information from the board of directors concerning the affairs of the Company and from the auditors concerning the execution and the results of their examination.

1.4.2 How and when can the information be obtained?

The information can only be obtained during the general meeting of shareholders.

Also, the right to obtain information is limited by two factors: (a) the information requested needs only to be given to the extent necessary for the exercising of shareholders' rights. In specific it may be refused if business secrets or other interests of the Company are jeopardized. (b) The books of the Company and correspondence may only be inspected with the express authorization of the general meeting of shareholders or by the resolution of the board of directors and subject to the safeguarding of business secrets.

Obviously, these two limitations grant broad discretionary power to the board of directors, as they are to decide to which extend the information requested is "*necessary for the exercising of shareholders' rights*" or when "*business secrets or other interests of the company are jeopardized*". At least, shareholders whose request for information has not been fulfilled, have the possibility to call upon the judge to decide on the request.

1.5 Right to ask for an independent audit and judicial administration or control of the company's affaires

1.5.1 Do these rights exist and what are its requirements? If yes, is it enforceable?

Swiss corporation law provides for an independent audit, but - under normal circumstances - not for judicial administration or control of the Company's affairs.

According to Art. 697a CO, any shareholder may introduce a motion at the general meeting of shareholders calling for certain facts to be subject to a special audit by a special and independent auditor. The special audit has to be necessary for the exercising of the

shareholders' rights. If the shareholders' meeting approves the motion, the judge (called upon by the Company or by a shareholder) appoints the special auditor.

If the general meeting does not approve the motion calling for the appointment of the special auditor, shareholders who represent at least ten percent of the share capital or who represent shares with a par value of two million Swiss francs, may request the judge to appoint a special auditor. The shareholders are legallly entitled to the appointment of a special auditor if they credibly establish that corporate bodies have violated the law or the articles of incorporation and have thereby damaged the Company or the shareholders.

Founders, corporate bodies, mandatories and employees of the Company are obliged to inform the special auditor about relevant facts. The special auditor provides a detailed report about his findings. However, he is not allowed to unveil business secrets in the report. There is a special procedure if disputes arise whether specific facts are business secrets or not. The edited report is submitted to the shareholders at the next general meeting.

The costs for the special audit are in general charged to the Company, only in presence of special circumstances the judge may charge the costs in full or in part to the applicants.

1.6 Right to ask for the dissolution of the company

1.6.1 Does this right exist and what are its requirements? If yes, is it enforceable?

The Company is dissolved if the general meeting decides so (there is no special quorum needed, a simple majority is sufficient), Art. 736 sec. 1 para. 2 CO.

If the minority shareholders do not manage to get a majority of the votes in favour of the dissolution of the company, shareholders representing at least ten percent of the par value of the share capital can request the dissolution of the Company by the judge. For this they must show that valid reasons exist (Art. 736 sec. 1 para. 4 CO). In practice, the dissolution of a company by the judge is rare - courts have pointed out that minority shareholders have to accept the majority rule. Only in exceptional cases (blatant disregard of minority shareholders' rights or gross mismanagement of the Company dominated by the majority shareholders), courts have enforced the dissolution of the Company.

If the judge finds that dissolution goes too far but wants to remedy a situation prejudicial to the interests of the minority shareholders, he can order "*another solution appropriate in the circumstances and acceptable to the interested parties*" (Art. 736 sec. 1 para. 4 CO). Possible solutions in this sense would be higher dividends, the appointment of a minority shareholder to the board of directors, a special audit, buying out minority shareholders etc.

1.7 Right to ask for the dividend

1.7.1 Do minority shareholders have the right to demand the payment of dividends or other distributions?

All shareholders are entitled to a proportionate share of the profits (dividends) and to a proportionate share of the liquidation proceeds upon liquidation of the Company (Art. 660

CO). However, the question of the amount of the dividends paid out is a matter of business judgment and courts only rarely interfere with decisions of the board of directors. Only in blatant cases of disregard of the interests of minority shareholders courts would order the paymend of dividends in a specific amount. This would be an order by the judge as an alternative to the dissolution of the Company according to Art. 736 sec. 1 para. 4 CO.

1.7.2 Is it customary to agree on a minimum dividend in a Shareholders' Agreement?

No.

1.8 Minority Shareholders and Board of Directors

1.8.1 Have minority shareholders the right to be represented on the board?

In general no. Only if there are different classes of shares providing for different voting rights or financial claims of the shares, at least one representative of these classes of shares must be elected to the board. But this right does not exist for minority shareholders per se.

The judge could order the appointment of a representant of the minority shareholders to the board in cases of blatant disregard of minority shareholders' interests as an alternative to the dissolution of the Company according to Art. 736 sec. 1 para. 4 CO.

1.8.2 Can minority shareholders join to be represented on the board?

Yes, but the right to be represented on the board is only very limited. They would have to find a majority of the votes in order to have their candidate elected to the board.

1.8.3 Can minority shareholders enforce the dismissal of members of the board?

No. Only the general meeting of shareholders can remove members of the board by a majority vote (Art. 705 CO). Minority shareholders have no special rights enabling them to dismiss a member of the board.

1.9 Other rights which could be included in the Articles of Association

1.9.1 Can the Articles of Association provide for additional rights of the minority shareholders?

Yes, Swiss corporations law is rather liberal as to the possible contents of the Articles of Association. As far as the representation of minority shareholders on the board is concerned, Art. 709 sec. 2 CO expressely provides that the Articles of Association may give minority shareholders special rights of representation.

1.9.2 If not, can such rights be provided for in shareholders' agreements?

Yes, but - of course - shareholders' agreements cannot be enforced against the Company, only against the other shareholders who have contractually bound themselves.

1.9.3 Which minority rights are typically included in Articles or Agreement?

The *Articles of Association* could provide for minority shareholders to have one or more representants on the board. This way they would not only have more influence on running the Company but also they could profit from the better rights to information and inspection of a board member (although the board member has the obligation to safeguard the Company's business secrets). For important decisions, the Articles could provide for higher decision quora, so that the majority cannot impose these decisions on the minority if they do not reach the quora necessary. Payment of dividents can also be explicitly provided for in the Articles and these can be guaranteed in a certain amount relative to the profits.

In a *Shareholders' Agreement* the majority shareholders could promise arrangements of the same kind to the minority shareholders. Of course the promise could only be that the majority promises to cast their votes in the general meeting of shareholders in such a way that the minority's interests are safeguarded. Additionally, Agreements often provide for the right of minority shareholders to sell their shares to the majority at predermined conditions (put-options).

1.10 Capital increase and decreases

1.10.1 To what extent have minority shareholders the right or obligation to participate in capital increases? Under which circumstances can such right be excluded?

Each shareholder is entitled to a portion of the newly issued shares corresponding to his prior participation (Art. 652b sec. 1 CO).

These preemptive rights may only be excluded if the general meeting of shareholders decides so for valid reasons. The law cites as examples for such valid reasons: the takeover of an enterprise, participations in other enterprises and participation of employees in the share capital of the Company. It adds that no shareholder may be disadvantaged or advantaged by a withdrawal of the preemptive rights if no such proper reason exists (Art. 652b sec. 1 CO).

1.10.2 To what extent are minority shareholders protected against capital decreases that might lead to loss of shares or a reduction of their capital share and a possible loss of rights?

Minority shareholders have no right to block a capital decrease in general if the general meeting of shareholders decides so. They have only the right to equal treatment, meaning that all shares incur the same decrease in par value and - if payouts of capital are made - they receive the same amounts. That being said it is clear that the Company cannot reduce its capital by invalidating specific shares only - minority shareholders run no risk of being dispropriated by capital decreases.

1.10.3 Do minority shareholders have the right of preemption regarding the subscription of shares?

Yes, see 1.10.1 above.

1.11 Transfer of shares

1.11.1 Which restrictions restricting the free transfer of shares are permitted?

Restrictions on the free transfer of shares are transmitted but the Company is not totally free in doing so. First, only the transfer of registered shares can be restricted - bearer shares are transferable freely. Second, restrictions of the free transfer of registered shares must be provided for in the Articles of Association. The Articles must name valid reasons for which the Company may refuse to register the acquirer of shares.

Then different regimes apply to registered shares that are listed on a stock market and those that are not:

(a) In a Company not listed, valid reasons for restricting the transfer of shares may be the purpose of maintaining the independence of the enterprise or of maintaining a certain composition of the circle of shareholders, like keeping competitors out of the Company or to provide for specific personal prerequisites of the shareholders (e.g. professional qualifications where the Company provides professional services or political, philosophical or religious affiliations where the Company serves such special purposes). Additionally, the Company may refuse to register an acquirer of shares without providing a valid reason if it offers to buy his shares at their real value.

(b) In a listed Company, the Articles of Association may only restrict the free transfer of shares by providing for percentage limit of the shares that can be registered for the same shareholder.

1.11.2 Do minority shareholders have the right to sell their shares in case of a change of control (mandatory takeover bid)?

Mandatory takeover bids are regulated not in the corporations law of the Code of Obligations, but in the Federal Act on Stock Exchanges and Securites Trading (SESTA). This means in the first place, that there is no mandatory takeover bid in non-listed companies.

For listed companies, Art. 32 SESTA provides that the acquiror of 33 1/3 percent of the voting rights has to make an offer to acquire all shares of the Company.

1.12 Derivative Actions

1.12.1 Can (minority) shareholders enforce rights of the company against a) other shareholders, b) directors or c) third parties?

There are no derivative actions in general. Only in the case of a claim of the Company against the members of the board of directors and other persons engaged in the management of the Company, there is an instrument that resembles a little bit a derivative action. Art. 756 CO provides that in addition to the Company itself, each shareholder is entitled to file an action for damage caused to the Company. In such case, the claim of the shareholder is for damages to be paid to the Company, not to himself. However, starting a lawsuit is not

attractive for a shareholder under normal circumstances: it is not a Derivative Action in the sense that the Company carries the costs of the litigation. The costs of the ligation are carried by the shareholder starting the lawsuit. Only if the judge deciding the case deems that the shareholder had sufficient cause to file an action, he may divide the costs in his discretion between the Company and the shareholder. So the shareholder may run a high cost risk but in the case of success, the damages are paid to the Company.

Action against directors and managers are more attractive in case of bankruptcy of the Company, as the shareholder participates in the damages paid out directly (but only in propotion of his participation in the Company, the remainder falls into the bankruptcy estate).

1.13 Remedies against shareholders' right infringement (please note question II.4. below for avoidance of overlap)

1.13.1 What remedies are available?

Which remedies are available depends on whether the shareholders' rights have been infringed by decisions of the general meeting of the shareholders or by the board of directors.

(a) Blatant infringements of shareholders' rights by the general shareholders' meeting are null and void, meaning that a shareholder does not have to sue the Company in court to have them voided. All legal bodies have to treat null and void decisions like they didn't exist at all. According to Art. 706 b CO, decisions of the general meeting of shareholders are null and void in particular, if they (aa) withdraw or limit the shareholders' rights to participate in the general meeting of the shareholders, the minimum voting right, the right to sue, and other rights granted by mandatory provisions of law; (bb) limit the shareholders' rights to control the management of the Company beyond the extend provided by law; (cc) disregard the fundamental structures of the Company or violate the provisions for the protection of the capital.

(b) In less blatant cases of violation of shareholders' rights, decisions of the general meeting of shareholders can be challenged in court. Art. 706 CO provides that resolutions of the general meeting of shareholders can be challenged in an action against the Company, if they violate the law or the articles of incorporation. In particular, decisions are challengeable, which (aa) withdraw or limit shareholders' rights thereby violating the law or articles of incorporation; (bb) withdraw or limit shareholders' rights without proper reason; (cc) discriminate against or disadvantage shareholders in a manner not justified by the company purpose; (dd) withdraw the profit orientation of the general meeting without the consent of all shareholders.

(c) In the case of decisions of the board of directors infringing shareholders' rights, the case is more difficult: there is no direct right of shareholders to challenge decisions of the board in court. But decisions of the board can be null and void for the same reasons as decisions of the general meeting of shareholders. The rules of Art. 706b CO are applied by analogy

(Art. 714 CO). So a minority shareholder could start action for the court to declare the decision null and void.

2. FOCUS ON MINORITY RIGHTS IN THE CONTEXT OF CAPITAL INVESTMENTS

2.1 Mandatory nature of minority rights

2.1.1 Are the minority rights incorporated by mandatory law?

Only some core minority rights are mandatory law and may absolutely not be waived. These rights do not only protect the interests of the shareholders but also guarantee the very structure of the Company. These rights are (a) the right to challenge resolutions of the general meeting of shareholders; (b) the right to make founders, directors, auditors and liquidators of the Company liable for damages suffered; (c) the right to participate in the general meeting of shareholders; (d) the information and inspections rights.

Generally the law describes the circumstances when exceptions to minority rights exist: e.g. the preemptive rights to buy newly issued shares can be set aside by the board of directors for valid reasons.

2.1.2 Generally, to what extent can a shareholder waive its minority rights and can such waiver be of a "blanco" or "general" nature for the future or does the waiver have to be repeated each time needed or be specific in nature?

The core minority rights cannot be waived at all. An agreement (be it of "general" or "specific" nature) to waive these rigths would be null and void.

2.2 Investors' requests for waivers

2.2.1 Do capital investors generally require minority shareholders to waive their minority rights – please describe in which scenarios such requirements are normally made.

Given the mandatory nature of the most important minority rights, there is neither a practice nor are there many practical scenarios of capital investors requiring the waiver of minority rights.

2.2.2 What minority rights are normally required to be deviated from?

Minority rights can be reduced by introducing privileged shares (see above 1.1.3). Also the right to dividends could be theoretically reduced by provisions in the articles of incorporation (e.g. that part of the profits are to be retained in the company or given to a charity).

2.3 Implementation of deviations from minority rights

2.3.1 How are waivers implemented in practice (articles of association, shareholders agreements, other agreements)?

Waivers infringing minority rights cannot be implemented neither in the articles of association, nor in shareholder agreements nor in other agreements. If the law provides for exceptions in the mandatory minority rights, usually these have to be introduced into the articles of association.

2.3.2 If waivers are implemented contractually, what kind of strengthening provisions are used (e.g. contractual penalties / liquidated damages, pledge and forfeiture of shares, etc)?

If a waiver infringes on mandatory minority rights and is thus null and void, also strengthening provisions are null and void.

2.4 Enforcement and remedies

2.4.1 If deviations from / waivers of minority rights have been implemented contractually (e.g. by a shareholders' agreement), can the minority shareholder still enforce its minority rights on a corporate law basis - although in breach of contract?

Yes. The Company cannot object to the enforcement of minority rights that the shareholder is in breach of a contractual agreement with other shareholders. E.g. it has to count the vote cast by the minority shareholder as is, not the way it should have been cast according to a shareholders' agreement.

The other shareholders that are party to the agreement cannot claim specific performance of the obligation entered into by the minority shareholder if this infringes on mandatory minority rights. Such an obligation is illegal and not enforceable.

2.4.2 If yes, what measures (e.g. interim injunctions) does the investor have access to?

2.5 Avoidance of rights abuse by minority shareholders

2.5.1 What remedies exist against the abuse of rights by minority shareholders (paralyzing effect on governance/function of the company)?

In such a case, the minority shareholders may resort to the action for dissolution of the Company. This is a practical solution, as according to Art. 736 sec. 1 para. 4., instead of dissolution of the Company, the judge may decide on *another solution appropriate in the circumstances and acceptable to the interested parties.* Obviously, the judge is given broad discretionary power.

Such solutions could be: obligation to pay out dividends; appointment to the board of directors of a representant of the minority shareholders, demerging parts of the enterprise, buy-back of the minority shareholders' shares, partial liquidation of the enterprise.