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Practical implementation of the new disclosure requirements for shareholders and LLC members

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The new disclosure requirements for acquirers of shares and limited liability company ("LLC") capital contributions have led to considerable uncertainty in practice. The purpose of these requirements is to enable information to be obtained on both the owners and beneficial owners of companies limited by shares or LLCs. There are harsh sanctions for failure to comply with disclosure obligations: membership rights will be suspended and property rights may lapse. In practice, many questions remain unanswered with regard to implementation. Some possible approaches are set out below.

Tight timeframe

- **Any party acquiring bearer shares that are not listed on a stock exchange must be notified to the company within one month of acquiring title.**
- **Any party that acquires unlisted bearer shares, unlisted registered shares or capital contributions and thus holds a package representing at least 25% of the share capital or total votes must, within one month of acquiring title, disclose the beneficial owners to the company.**
- **In the case of companies limited by shares, the Board of Directors has a duty to ensure that acquiring parties that fail to fulfill their disclosure obligations do not participate in general meetings. The Board of Directors must also ensure that dividends are not paid to acquirers that have failed to fulfill their disclosure obligations.**

Practical implementation of the new disclosure requirements for shareholders and LLC members

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The Swiss Federal Act for Implementing the Revised Financial Action Task Force (FATF) Recommendations of 2012 ("FATF Act") was adopted at the end of 2014 in the context of money laundering prevention measures. Articles 697i - 697m of the Swiss Code of Obligations ("CO"), which apply to companies limited by shares, and Article 790a CO, which applies to LLCs, came into force on 1 July 2015 with the specific aim of ensuring transparency in relation to unlisted companies. To help acquirers of shares or capital contributions avoid unanticipated adverse effects, the conditions to be met in relation to the disclosure requirements and the consequences of non-compliance are explained below.

Simple disclosure requirement for all acquirers of bearer shares

Any party that acquires unlisted bearer shares is required to notify the company irrespective of the number of shares acquired. Acquirers must supply their first name and surname or business name and their address to the company, indicating the legal grounds for acquiring the bearer shares, the date of acquisition and the number of shares acquired. The shareholder must prove ownership of the bearer shares and present a copy of an official identification document or excerpt from the Commercial Register. Any change of name or address must also be notified.

The information must be disclosed within one month of **acquiring** the shares. There is only a duty to report the acquisition of shares for ownership or the usufruct thereof, but not the creation of a charge. Ownership may be acquired by purchasing or receiving a gift of shares, subscribing to shares upon incorporation or on the occasion of a capital increase, by way of succession, under a matrimonial property regime or in the event of a merger or demerger. In order to avoid any adverse consequences, it is advisable to establish in advance when, precisely, the one-month period starts to run.

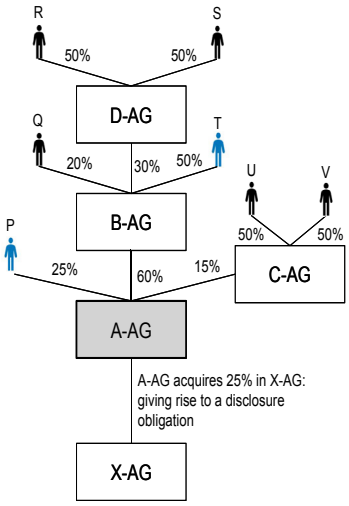
Qualified obligation to disclose beneficial owners for acquirers of bearer shares, registered shares and capital contributions

Any party that acquires unlisted bearer shares, unlisted registered shares or capital contributions and thus holds a package representing at least 25% of the share capital or total votes must inform the company of any natural persons for whom that party ultimately acts. As in the case of the simple disclosure requirement, it is incumbent upon the **acquirer** to fulfill the qualified disclosure obligation. Natural persons who acquire interests for their own account must inform the company that they are both the owner and beneficial owner of the interests concerned. However, where the interests are acquired in a fiduciary capacity, the qualified reporting requirement is met by disclosing the identity of the party for whom the fiduciary agent is acting rather than that of the acquirer. If the acquirer is a legal entity, the identities of any natural persons who have a beneficial interest in the legal entity must be disclosed. Where a party does not meet the **25% threshold value** alone, but in concert with third parties, e.g. under a joint purchase agreement, this arrangement will also give rise to a disclosure requirement.

As in the case of simple disclosure on acquiring bearer shares, any qualified disclosure of a beneficial owner must be made within one month of acquiring title.

Acquirers must inform the company whether they have met the threshold of 25% of the share capital or votes and disclose the first names, surnames and addresses of the natural persons holding

Identifying beneficial owners in the case of multi-level shareholdings



a beneficial interest in the acquiring entity. However, acquirers are not required to provide evidence of or disclose the exact size of the interest held in the acquiring entity by beneficial owners. Neither is it necessary for acquirers to present copies of identification documents for the beneficial owners concerned. Any change in the beneficial owner's name or address must be reported, but not the fact that a natural person no longer qualifies as a beneficial owner due to a reduction in the interest held.

What is meant by a beneficial owner who is a natural person?

The law clearly indicates the shareholding threshold value that would give rise to a disclosure requirement on the part of the acquirer (25%). *Chart on the left: A-AG acquires 25% in X-AG which gives rise to a disclosure requirement.* However, the legislation fails to provide any clarity as to the substance of the disclosure, i.e. concerning the identification of the parties for whom the acquirer "is ultimately acting (the beneficial owner)" (Art. 697j (1) CO). The legislation explicitly states that it is only necessary to report **natural persons**. Acquirers acting on their own account may notify the company accordingly. Acquirers acting in a fiduciary capacity are required to disclose the party for whom they are acting.

However, matters become more complicated in situations involving multi-level shareholding structures, such as holding company structures and group companies. Will any financial stake in the acquirer *(Chart: A-AG)* be sufficient to trigger a disclosure requirement? There is a consensus among legal commentators that it is unworkable to give the wording of the legislation such a broad construction. *Chart: It would be necessary to notify all natural persons P-V.* Instead, there is a presumption that it is only necessary, in line with the FATF Act, to disclose parties that exercise **effective control over the acquirer**, whether through qualifying equity interests, voting rights or by some other means. Various methods of calculation have been developed in practice. The "multiplication test" is perhaps the most common and, in our opinion, the most workable method. The **multiplication test** involves multiplying all ownership interests at all levels of the shareholding chain, from the acquiring entity at the bottom up to natural persons. If an interest of 25% or higher results from the multiplication test, a natural person will be deemed to be a beneficial owner of the acquiring entity and must be reported. *Chart: It is only necessary to report P (who has a 25% direct interest in A-AG) and T (who has a 30% indirect interest in A-AG). The indirect interests of Q, R, S, U and V are smaller.* However, it is also necessary to take account of **facts and legal relationships** that allow one party to exercise control over the acquiring entity **in some other recognisable way**. This could involve shareholders' agreements, but also loan agreements, marital agreements and influence exerted due to family relationships, although it will be necessary to assess on a case-by-case basis whether the control is exercised within the meaning of the law. *Chart: If there were a shareholders' agreement between Q and T that included a voting clause, Q would therefore be a co-controlling party and would need to be notified together with T.*

There may be situations in which a beneficial owner who is a natural person cannot be determined either by using the multiplication test or by considering the specific circumstances. This would be the case where interests below 25% result. However, another such example would be collective investment schemes or – depending on the legal arrangement - foreign trusts, given that the parties holding the assets (investors or beneficiaries) are usually distinct from the parties responsible for making the decisions (fund management company or trustee).

In line with the arguments put forward here, there would also be an exemption from the disclosure requirement if one of the intermediary companies in a shareholding chain were listed or held intermediated securities *(Chart: A-AG* or B-AG). In this type of situation, it would not be necessary to disclose the beneficial owners *(Chart: P or T)*, as the specific legislation will ensure that transparency is maintained.

Even if the acquirer cannot identify any beneficial owner who is a natural person or believes that an exemption from the disclosure requirement applies, we recommend that a specific notification to this effect should still be submitted to the company. This will ensure that the acquirer does not suffer any adverse legal consequences from failure to fulfill its disclosure obligation.

Maintaining registers of bearer shareholders and notified beneficial owners

The new requirement to notify bearer shareholders means that all companies issuing bearer shares must also keep a register of bearer shareholders. As well as the new register of bearer shareholders or the traditional share register (in the case of companies with registered shares) and register of capital contributions (in the case of LLCs), it is now necessary for all companies to keep a register of the beneficial owners notified to them.

The register of bearer shares and the register of notified beneficial owners must be kept in such a manner that it can be accessed by the authorities in Switzerland at any time. Shareholders, company members and third parties have no right to inspect the records.
A separate register of notified beneficial owners may be maintained or this may be incorporated into the register of bearer shareholders, of registered shareholders or of capital contributions. In the case of more complex shareholder structures, it is strongly recommended that **separate registers** are maintained, not least in order to avoid disclosure to the authorities of shareholder information which, by law, does not need to be included in the register of notified beneficial owners.

If shareholders fail to comply with their disclosure obligations, their pecuniary rights will lapse.

Sanctions for non-compliance with disclosure requirements

There are sanctions for acquirers which fail to fulfill their disclosure obligations. These impact on membership rights, including voting rights and the right to participate in elections, as well as the right to information and the right to inspect records. The pecuniary rights of acquirers (entitlement to dividends and the proceeds of liquidation) may also be affected. The law does not provide for any criminal penalties. Unfortunately, the legislator failed to articulate clearly when the specific sanctions will be imposed.

According to legal commentators, acquirers may only exercise the **membership rights** attaching to the interests acquired once they have fulfilled their disclosure obligations. The prevailing opinion, which we endorse, is that acquirers may exercise their membership rights in full for up to one month following the date of acquisition. Membership rights will be suspended only after expiration of this one month period, pending submission by the acquirer of the relevant notification.

Article 697m (3) CO provides as follows with regard to **pecuniary rights**: *"If the shareholder fails to comply with their obligations to give notice within one month of acquiring the shares, the property rights lapse. If they give notice at a later date, they may exercise the property rights arising from that date."* The same applies to members of an LLC. Accordingly, if the general meeting declares a dividend in any period in which an acquirer is in default of its obligations, no dividend payment will be made to that acquirer due to the fact that its rights have lapsed, even if the acquirer submits the notification at a later date. Based on our opinion, which appears to be widely shared by legal commentators, the acquirer has exactly one month from the date of acquiring title in which to make the requisite notification. After this point, the acquirer will forfeit any pecuniary rights accruing in the period in which it is in default. However, some legal commentators also argue that the relevant time period is two or even six months. Nevertheless, we strongly advise against any reliance on arguments for longer time periods until the courts have made a determination on this issue.

It is thus the responsibility of the Board of Directors of a company limited by shares or the management of an LLC to ensure that no unauthorised parties, i.e. acquirers that have failed to comply with their

Members of the Board of Directors who fail to comply with their obligations in connection with the disclosure requirements may be held personally liable.

disclosure obligations, participate in general meetings or benefit from dividend payments. Any dividends paid out to unauthorised parties may be reclaimed. Both the company and the other shareholders or company members may bring an action for recovery, but not any company creditors. The relevant sum must be repaid to the company. Any claim for repayment is subject to a limitation period of five years from the date on which the dividend was paid out.

Where unauthorised shareholders or company members were involved in passing resolutions and votes put to the general meeting, the other shareholders or company members may **contest the resolutions or votes concerned**. In addition, members of the Board of Directors may have personal and unlimited liability in the event that an action is brought against them. Where a dividend has been paid to an unauthorised party, members of the Board of Directors may also be held liable for criminal mismanagement. The same liability would attach to the directors of an LLC.

Note: relevance of disclosure obligations to M&A transactions

The practical significance of disclosure obligations becomes abundantly clear in the context of company acquisitions based on share purchases. Given that virtually all M&A transactions involve a purchase of more than 25% of the company's shares, the disclosure obligation will apply in almost all instances. Unless or until the disclosure obligation is fulfilled, there will be uncertainty surrounding the membership rights of the shareholder or company member concerned. This means that any resolutions passed by the general meeting in the context of closing may be contested. This would typically involve resolutions formally approving the actions of former directors or appointing new governing bodies. Depending on whether the purchaser wishes to disclose the natural persons with beneficial interests in the purchaser to the seller, we recommend including **specific clauses in the purchase agreement or the minutes of the general meeting.**

Urgent disclosure necessary for bearer shareholders that acquired shares prior to 1 July 2015

Persons and entities that held bearer shares prior to 1 July 2015 were required to register as shareholders with the company during the transitional period, i.e. before the end of 2015. They were also required to disclose any natural persons with a beneficial interest. We recommend that any person or entity that has omitted to report such information to date should do so immediately, as it will not be possible to exercise any shareholder rights until this situation is rectified.

Practical recommendations

The rules governing the disclosure of acquirers of bearer shares are relatively clear: any acquisition of bearer shares in unlisted companies must be reported to the company. By contrast, the requirement to notify beneficial owners is rather more complex. Given the potentially serious legal implications of failing to comply with disclosure obligations, it is advisable to proceed with caution and seek legal clarification at an early stage. We would be happy to assess for you which parties, if any, need to be disclosed to companies in relation to the new transparency provisions.