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# Commission's Report on New Stock Exchange Offences and Market Abuse Regulation

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On 29 January 2009 the commission of experts on stock market offences and market abuse set up at the request of the Federal Council submitted its report to the head of the Federal Department of Finance. The report contains proposals for new rules on insider trading and market manipulation. According to the experts, the offences should be brought more in line with the solutions applied in the EU and should no longer be contained in the Penal Code, but instead form part of the Stock Exchange Act. The Federal Council will decide in the coming months what further action is required and which of the proposed measures should be implemented after it has received additional clarification from the Federal Department of Finance.

*By Philippe Weber / Petra Ginter*

## 1) Background

On 3 October 2007, the Federal Department of Finance (FDF) appointed a commission of experts (the Commission) to inquire into and report on the Swiss rules and regulations on stock exchange offences and market abuse and to recommend what amendments could be made, inter alia, to bring the Swiss regime closer in line with EU and other relevant regulations. The report of the Commission was issued on 29 January 2009 and published in March 2009 (see http://www.efd.admin.ch/dokumentation/zahlen/00578/01375/index.html?lang=de).

The Swiss regime on the enforcement of stock exchange offences and other forms of market abuse consists of multiple layers of criminal provisions, supervisory law (both at statutory and lower regulatory levels) and self-regulatory rules. The current rules appear in part inadequate as to procedure and/or substance. In addition, they do not provide for the same level of protection against criminal conduct if compared to certain foreign laws, including EU law. Finally, according to international recommendations issued by the Groupe d'Action Financière (GAFI), insider trading and market manipulation should qualify as preceding offence *(Vortat)* of a money laundering offence, which currently is not the case under Swiss law.

Against this background, the Commission has formulated a series of proposals, including (in the annex to its report) a draft bill for a revision of the Stock Exchange Act (SESTA). The Commission is of the view that a modern and effective regime on stock exchange offences constitutes a precondition for a competitive Swiss capital market. If implemented, the proposed changes could lead to a significant overhaul of Swiss law on stock exchange offences and market abuse.

## 2) Findings and Proposals of the Commission

### a) Place of Regulation and Related Matters

The Commission recommends to transfer the current provisions on ***insider trading and market manipulation*** from the Penal Code (PC) (*i.e.,* currently articles 161 and 161[bis] PC) to the SESTA.

Furthermore, the Commission proposes to introduce a new first degree incriminated conduct on insider trading and market manipulation that would qualify as ***crime*** *(Verbrechen)* if an insider trading or market manipulation results in a ***substantial financial profit***. Although the Commission expresses some reservations on this point, a new first degree provision would make it possible to qualify (severe) insider trading and market manipulation as preceding offence *(Vortat)* for a ***money laundering offence***. This would allow to implement the GAFI recommendations and to ratify the convention of the European Council.

These and certain other proposed amendments (see paragraph e) below) would facilitate a more ***uniform enforcement*** of market conduct rules and potentially the prosecution of multiple offences in accordance with the same procedural rules.

### b) Insider Trading: Broadened Meaning of the Term 'Insider'

***Primary Insiders:*** Under current Swiss law, ***only*** those categories of persons who are explicitly mentioned in article 161 (1) PC and who have access to material, non-public information due to a privileged position vis-à-vis the company *(Sonderdelikt)* qualify as ***primary insiders*** and, thus, are subject to criminal sanctions on insider trading under article 161 (1) PC (see CapLaw-2009-1). By contrast, in the UK or Germany the definition of 'insider' is broader and, *e.g.,* also includes persons who do not have a special relationship with the company.

The Commission concludes that the Swiss definition of 'insider' should be brought more in line with the EU Market Abuse Directive (MAD). Accordingly, it proposes to ***expand the definition of the primary insider to persons that have direct access to confidential information***, including, without limitation, persons that under current law qualify as auxiliary persons or as agents, such as assistants and legal advisors, as well as persons below the top management that have access to, or even produce, sensitive information. Different to current law, shareholders would also be covered by the new definition of primary insider. With respect to the origin of the insider information, it would furthermore be irrelevant whether the origin of the information lies within the relevant company (*i.e.,* the direct professional environment of the primary insider) or not; *e.g.,* also facts that occur outside of the relevant company but have an effect on the stock exchange price of the relevant company may qualify as insider information.

***Secondary Insiders:*** The broader definition of 'primary insider' would automatically result in a broader meaning of the term 'secondary insider'. Any person that (directly and actively) receives information from a primary insider (as more broadly defined) would qualify as secondary insider and be subject to the criminal provisions on insider trading. In addition, and in accordance with the MAD, also persons that have received confidential information by committing a crime would newly be considered as secondary insiders.

***Accidental Insiders:*** The Commission proposes that also persons that get access to confidential information only by coincidence should qualify as insiders, which is not the case under current law.

***Safe Harbor:*** The Commission proposes a new safe harbor clause according to which the intention of a person to enter into a specific transaction would, as regards such person and third parties assisting that person in the execution, not per se constitute 'insider information'. For example, the acquisition of shares by the offeror in preparation of a planned tender offer would not, per se, be a punishable insider trading. This rule, which is often described as 'nobody can be its own insider', is widely accepted by Swiss legal scholars; however, by expressly including it in the statute legal certainty would be significantly increased.

***Conclusion:*** If the above proposals will be implemented, Swiss law would level the playing field to the insider trading rule under the MAD. It would also facilitate cross-border transactions because the parties involved could rely on a more uniform regime of insider rules. For example, a transaction between insiders may be exempt from insider rules of country A whereas currently no such exemption may exist in country B.

### c) Market Manipulation: Criminal Provisions remain Unchanged

Under the current article 161$^{bis}$ PC the definition of market manipulation is ***limited to the manipulation of the market price of securities***. By contrast, *e.g.,* in the UK and Germany the definition includes not only behaviour that affects the market price of securities but the market in general, *i.e.,* other important indicators such as trade volume or existing orders. In particular, whereas in Switzerland only 'Wash Trades' or 'Matched Orders' are forbidden transactions (to the extent they have an influence on the market price), the respective rules in the UK and Germany in addition include, *e.g.,* 'Cornering', 'Fixing the Close', 'Capping' and 'Pegging'. Based on the approach to cover such 'real' transactions (and not only simulated transactions), the rules in the UK and Germany contain specific guidance on what is considered as manipulating and non-manipulating behaviour as well as what behaviour is subject to 'Safe Harbours' or 'Accepted Market Practise'. *E.g.,* trading with own shares in the context of a buy back programme would be covered by these exemptions.

The Commission proposes ***not*** to expand the scope of criminal market manipulation (article 161[bis] PC) by including also simple rumours (as would be the case under the MAD). Also, an inclusion of further 'real' transactions which are prohibited under the MAD is not recommended by the Commission because such other 'real' transactions may only be divided into punishable and non punishable behaviour by the element of a good or bad intent which, in the view of the Commission, is an uncertain distinction. Therefore, the Commission believes that these behaviours should not be positioned as criminal provisions applicable to all market participants because it considers their value for the functioning of the stock exchange as less important. Instead, the Commission proposes that these provisions should remain of administrative character, *i.e.,* for regulated entities only, unless they are subject to the Limited Market Supervision as described below.

### d) Limited Market Supervision

The Swiss Financial Market Supervisory Authority FINMA (FINMA) circular 08/38 of 20 November 2008 (FINMA Circular 08/38: http://www.finma.ch/d/regulierung/Documents/finma-rs-2008-38.pdf) as currently in force 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 entities supervised by FINMA, *i.e.,* licenced securities dealers and, within certain limitations, also to banks without securities dealer licence and licenced institutions under the Collective Investment Schemes Act.

The Commission proposes to introduce definitions of 'Volume Manipulation', 'Scalping' and 'Front Running' in the SESTA that would be sanctioned by limited administrative measures. This amendment would give FINMA the competence to enforce certain kinds of misbehaviour which formally do not qualify as (criminal) market manipulation. The proposal would not lead to prudential market supervision but would rather give FINMA the authority to investigate and enforce certain misbehaviour even if it were committed by a non-regulated participant (so-called 'Limited Market Supervision', in German *'Punktuelle Marktaufsicht').*

In order to enforce this conduct, the Commission proposes, in particular, the ***issuance of declaratory orders*** *(Feststellungsverfügungen)* and the ***disgorgement of profit***, each as administrative measures.

### e) New Organisation of Competences for Enforcement of Stock Exchange Offences

On a procedural level, the goal of the Commission is to ***centralise the procedures to the largest extent possible***. The reason for this is not only because of the complexity of the matter but also because a perpetrator may, by one conduct, fulfil different definitions of offences. Therefore, the Commission is of the view that it does not make

sense if different authorities investigate into the same conduct. In order to achieve the described goal the Commission has considered various alternatives of which the following appears to be the preferred proposal:

The Commission proposes to assign all penal proceedings with respect to stock exchange offences to the competence of the ***Office of the Attorney General of Switzerland*** (OAG). This should, however, not undercut the existing practice that normally FINMA has the competence to undertake initial administrative investigations. As an introduction to the current practice, FINMA would, however, forward the results of its investigation to the OAG that is competent to initiate penal proceedings.

In connection with the proposed concept of the Limited Market Supervision by FINMA (as described above), ***FINMA*** would get the following competences with respect to the enforcement of stock exchange offences: It would be entitled ***to issue declaratory orders*** against non-regulated participants as an instrument to enforce its own proceedings with respect to stock exchange offences (as described in the preceding paragraph). This would be in line with current practice with respect to the violation of disclosure duties. Furthermore, FINMA would be authorised ***to impose the disgorgement of profit*** as administrative measure.

According to the preferred proposal of the Commission, the ***Federal Criminal Court*** (FCC) would act as first instance having judicial authority for stock exchange offences, which could be ***appellated to the Federal Supreme Court***. Consequently, under this proposal the Code of Criminal Procedures (StPO) would be applicable with respect to the procedural rights and duties of the perpetrator instead of the, to some extent, outdated Statute on Administrative Criminal Procedures (VStrR). Furthermore, it would abbreviate the process of judicial review.

As an ancillary issue, the Commission further proposes to shift the right to ***suspend voting rights according to article 20 (4$^{bis}$) SESTA from the civil judge to the competence of FINMA***. As a supplementary measure, the Commission also encourages that FINMA should have the competence to issue an order that prohibits further acquisitions of securities *(Zukaufsverbot)* and that disgorges the profit (whereas, monetary fines should be reduced respectively).

## 3) Outlook

The Swiss government has announced that it will decide in the coming months what further action is required and which of the proposed measures should be implemented. Although implementation of the measures will require the amendment of Swiss federal statutes—and hence the approval of the Swiss parliament and potentially of the public by way of a referendum—it would not be surprising if in the current environment the Swiss government will support a fast procedure.

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# SIX Swiss Exchange publishes Guidance on Disclosure of Shareholdings in Capital Market Transactions

Reference: CapLaw-2009-28

*By Andrea Huber*

***Disclosure Requirements for IPOs (Replaces SIX Disclosure Office Notice I/99):*** The disclosure obligations of significant shareholders can be fulfilled at the time of an IPO by providing the appropriate information required under the FINMA Stock Exchange Ordinance (SESTO-FINMA) in the listing prospectus (previous practice). The issuer, however, must publish this information within two trading days subsequent to the IPO by means of the electronic publication platform of the SIX Disclosure Office (new practice) (for further details see http://www.six-swiss-exchange.com/download/admission/being_public/disclosure/notices/2009_01_en.pdf, section 1).

***Fulfilment of Shareholders' Disclosure Obligations upon Capital Increases:*** Shareholders whose participation reaches, exceeds or falls below a threshold as the result of a capital increase may fulfil their disclosure obligation in the listing prospectus, whereby only the shareholder's current information can replace a disclosure in accordance with article 21 SESTO-FINMA. The issuer, however, must publish this information within two trading days subsequent to the capital increase by means of the electronic publication platform of the SIX Disclosure Office (new practice) (for further details see http://www.six-swiss-exchange.com/download/admission/being_public/disclosure/notices/2009_01_en.pdf, section 2).

***Treatment of Subscription Rights:*** If, as a direct result of their shareholders status, shareholders are granted subscription rights in proportion to their previous equity holdings, the subscription rights are not subject to the disclosure requirement. The issuer as well need not disclose the issuance of such subscription rights within the scope of sale positions as per article 12 (1) (b) SESTO-FINMA. A derivative acquisition of subscription rights, *e.g.,* by means of a trading in rights on the SIX Swiss Exchange, leads to a disclosure obligation if as a result the thresholds under article 20 (1) Stock Exchange Act (SESTA) are reached or exceeded (for further details see http://www.six-swiss-exchange.com/download/admission/being_public/disclosure/notices/2009_01_en.pdf, section 2).

***Disclosure in connection with an Over-Allotment (Greenshoe) Option:*** Disclosure in connection with a potential over-allotment option essentially involves the same information as that required from underwriters in the case of a firm deal underwriting (see next paragraph), but in addition the granting of the greenshoe option must be disclosed as a sale position (article 12 (1) (b) SESTO-FINMA). In the section 'Significant shareholders' as per point 2.5.9 Scheme A, a reference must be made where this information has been disclosed in the prospectus. The issuer is not obliged to publish this information via the elec-

tronic publication platform of the SIX Disclosure Office (for further details see http://www.six-swiss-exchange.com/download/admission/being_public/disclosure/notices/2009_01_en.pdf, section 3).

***Disclosure Obligations for Underwriters of Firm Deals (Replaces SIX Disclosure Office Notice I/01):*** The disclosure obligations for underwriters of firm deals in connection with a capital increase can be fulfilled if the information as defined in SIX Disclosure Office Notice I/09 is provided in the prospectus (previous practice). In the section 'Significant shareholders' as per point 2.5.9 Scheme A, a reference must be made where this information has been disclosed in the prospectus. The issuer is not obliged to publish this information via the electronic publication platform of the SIX Disclosure Office. In case of an IPO, the placing consortium bears no reporting obligation within the context of article 20 SESTA as long as the part of the issuance process subject to disclosure obligations has been accomplished prior to the listing (for further details see http://www.six-swiss-exchange.com/download/admission/being_public/disclosure/notices/2009_01_en.pdf, section 4).

***Eased Disclosure of Lock-up Groups in the Prospectus:*** Lock-up groups may waive full disclosure of all group members in the prospectus if certain requirements pursuant to SIX Disclosure Office Notice I/09 are met. If these requirements are not fulfilled, a complete disclosure of all group members must be made. Reserved in this regard is an application for exemptions and easier disclosure according to article 24 SESTO-FINMA (for further details see http://www.six-swiss-exchange.com/download/admission/being_public/disclosure/notices/2009_01_en.pdf, section 5).

## Consolidation of Swiss Blue Chip Trading on SIX Swiss Exchange

*By Andrea Huber*

***SIX Swiss Exchange has reunified share trading in Zurich as of 4 May 2009:*** Trading in the 32 Swiss blue chip stocks (*i.e.,* the shares included in the SMI and SLI) has been transitioned from SWX Europe to the newly created SIX Swiss Exchange "Swiss Blue Chip Segment" as of 4 May 2009. The restructuring will afford trading participants administrative and technical advantages, and issuers will benefit from a reduction of complexity. Going forward, only Swiss law will be applicable in terms of regulation and surveillance of issuers and market participants (for further details see http://www.six-swiss-exchange.com/media_releases/online/media_release_200905040729_en.pdf).

# Repurchase of Convertible Bonds

Reference: CapLaw-2009-29

In light of recent market conditions, many issuers have considered repurchasing their outstanding convertible bonds. Depending on how the repurchase is conducted, a different set of rules applies: While privately conducted repurchases of convertible bonds are outside the scope of the Swiss takeover regime, 'public' repurchase offers are not. Nevertheless, also 'public' repurchase offers benefit from a series of exemptions from the Swiss takeover regulation similar to those applicable to the repurchase of shares. Contrary to publicly conducted repurchase offers, mere offers to induce early conversion of convertible bonds into shares should not be captured by the Swiss takeover rules in our view.

*By Ariane Riedi Wirth and Thomas Reutter*

## 1) Introduction

Repurchases of convertible bonds have been considered by many issuers in the recent past. Usually, they are one feature in a broader debt restructuring of an issuer and are often facilitated by market quotations that are below the principal amount or par value of the respective convertible bond. A repurchase is initiated by an offer by the issuer of the convertible bond (Offeror) to purchase some or all of the outstanding convertible bonds and is perfected by the acceptance of a bondholder to sell convertible bonds held to the Offeror. In most cases, a repurchase is conducted for the purpose of cancellation of the convertible bond.

The repurchase contract is not governed by the terms and conditions of the convertible bonds (Terms of the Bonds) and therefore—unlike any rights to redeem the convertible bonds early—not 'pre-agreed' at the time of issuance of the convertible bonds. Also, the price offered by the Offeror and eventually paid to a bondholder upon acceptance usually differs from the par value or principal amount, at which convertible bonds would be redeemed in case of an event of early redemption based on the governing Terms of the Bonds.

## 2) Private vs. Public Repurchases

An issuer may either approach bondholders ***individually*** without a public announcement or ***publicly offer*** to repurchase its outstanding convertible bonds. Private individual approaches are not uncommon even if the convertible bonds are listed on a stock exchange, because large blocks of convertible bonds are often held by a few major investors. Usually, the Terms of the Bonds also provide for the issuer to avail itself of the possibility to redeem the convertible bonds early if only few convertible bonds remain outstanding (so called 'clean-up call'), thus obviating the need to extend an offer to all bondholders.

Apart from considerations of ad hoc publicity and disclosure of major shareholdings discussed below, ***privately conducted repurchases of convertible bonds*** are ***largely outside of the Swiss regulatory regime***. While criminal law provisions, such as insider trading (article 161 of the Swiss Penal Code (PC)) and price manipulation (article 161[bis] PC), are generally applicable to repurchases of convertible bonds, they apply in particularly extreme cases only. Additionally, the market abuse rules of the Swiss Financial Market Supervisory Authority FINMA (FINMA) apply if a regulated securities dealer or bank is involved (see Circular No. 08/38 of the FINMA on Market Behaviour as of 20 November 2008). The EU Market Abuse Directive, which has been relevant for SWX Europe due to its status as an 'EU-Regulated Market' in the UK, will no longer be applicable after SWX Europe has been relocated to Switzerland.

Pursuant to article 2 (e) of the Stock Exchange Act (SESTA), ***public offers to purchase or exchange equity securities (including, for the following considerations, conversion rights)***—including the announcement of an issuer's intention to repurchase such equity securities via an exchange (see Release no. 1 of the Swiss Takeover Board (TOB) regarding Equity Security Repurchases as of 28 March 2000 (Release))—made to shareholders or holders of other equity securities of a Swiss corporation, which is at least partially listed on a Swiss stock exchange, constitute ***public takeover offers*** and are thus ***subject to the authority and the regulation of the TOB.***

### 3) Practice of the Takeover Board

The TOB held on various occasions that ***the provisions on public takeovers of the SESTA apply to public repurchases of convertible bonds*** listed on a Swiss exchange, because convertible bonds were held to be equity securities in the sense of articles 22 (1) and 2 (e) SESTA, regardless of whether the issuer was a Swiss or foreign entity as long as the convertible bond comprised a right to convert the convertible bonds into shares of the Swiss holding company of the issuer (see article 2 of the TOB Takeover Ordinance (TOO) as in effect at that time; TOB Recommendation 0102/01 in the matter of Sulzer Capital B.V. dated 13 June 2001 and TOB Recommendation 0299/01 in the matter of Actelion Finance SCA dated 23 November 2006). The TOO as in effect since 1 January 2009, however, does no longer consider convertible bonds as equity securities but as financial instruments (see article 2 (b) TOO and article 15 of the FINMA Stock Exchange Ordinance (SESTO-FINMA)). The question thus arises whether such change in the legislation was intended to no longer apply the rules on public takeovers to convertible bonds given that article 22 (1) SESTA limits the scope of the Swiss takeover regulation to offers for 'equity interests' *(Beteiligungen).* Because the change in legislation was driven by the intent to tighten the stock exchange regulation rather than to liberalize it, we think that the ***public repurchase of convertible bonds will continue to be regulated by the rules on public offers to purchase equity securities*** of articles 22 et seqq. SESTA in spite of changes in

nomenclature. However, we also believe that the repurchase of convertible bonds may not simply be treated in the same way as a repurchase of shares in most cases.

Thus, while privately conducted repurchases are outside the scope of the Swiss takeover regime, 'public' repurchase offers are not. However, it has to be noted that there is a fine line between privately conducted repurchases and public repurchase offers. Even ***repurchases that have not been publicly announced may constitute 'public offers'*** for the purposes of the SESTA if the case law of the TOB on tender offers for shares is applied by analogy. That is the case if the number of offerees is such that it cannot be expected to coordinate their position toward an offer (see TOB Recommendation 0067/04 in the matter of Intersport PSC Holding AG dated 11 August 2000, consideration 2.2, in which case 80 offerees were contacted). However, we are of the view that the TOB case law on third party share offers should only be applied to convertible bonds if the convertible bonds are 'equity-like' securities at the time of the offer (*i.e.,* at a minimum not 'out of the money') and if the nature of the offerees is such that the protection afforded by the SESTA is needed, which is generally not the case if only sophisticated institutional investors are targeted.

### 4) Takeover Rules Applicable to 'Public' Repurchases

If the offer to repurchase convertible bonds is subject to the provisions of the SESTA, the Offeror has to treat all bondholders equally (article 24 (2) SESTA), including with respect to the repurchase price (so called 'best price rule' pursuant to article 10 TOO). In case of a partial repurchase offer, tenders must be accepted on a pro rata basis. In principle, the Offeror would also have to comply with various other requirements of the takeover regime, such as the publication of a prospectus (article 24 (1) SESTA and articles 17 et seqq. TOO) and the reporting of transactions (article 31 SESTA and article 38 TOO). However, the ***exemptions*** for repurchases of shares as set out below are also ***applicable to repurchases of convertible bonds***, and, in addition, some specific relief is available to repurchases of convertible bonds. As a result, only a minimal set of takeover provisions are applicable to publicly conducted repurchases of convertible bonds.

Pursuant to the Release, which was held by the TOB to apply to convertible bonds by analogy (see TOB Recommendation 0102/01 in the matter of Sulzer Capital B.V. dated 13 June 2001, consideration 2, and TOB Recommendation 0299/01 in the matter of Actelion Finance SCA dated 23 November 2006, consideration 2), share repurchase programs may be exempt from the provisions governing public takeover offers provided that equality of treatment, transparency, integrity and good faith are ensured and insofar as there is no evidence that the Offeror is circumventing the SESTA or other legal provisions. The Release provides for different exemption procedures depending on the volume of the repurchase. Share repurchase programs affecting less than 2% of the Offeror's share capital are generally exempted according to section II

of the Release and do not have to be announced to the TOB. Based thereon, the TOB decided that ***publicly conducted repurchases of convertible bonds convertible into less than 2% of the share capital of the issuer or, as the case may be, its Swiss parent company are generally exempt from the takeover regulation*** (see TOB Recommendation 0299/01 in the matter of Actelion Finance SCA dated 23 November 2006). ***Repurchases of convertible bonds convertible into between 2% and 10% of the issuer's or its Swiss parent company's share capital or votes are exempted*** pursuant to section III of the Release as well, but in contrast, ***have to be notified to the TOB*** (*e.g.,* TOB Recommendation 0102/01 in the matter of Sulzer Capital B.V. dated 13 June 2001).

Depending on whether the offer to repurchase is a fixed-price or at market price repurchase, additional exemption requirements as further set out in section III (1) to (3) of the Release apply. In particular, we would like to point out that the offer price in case of a fixed-price repurchase may be left open on publication of the repurchase offer, but has to be published via the electronic media at least three trading days prior to the offer's expiry, whereby the offer may only be accepted after publication of the offer price (see section III (2.6) of the Release), and a subsequent acquisition of convertible bonds at a higher price than the repurchase price by the Offeror until the expiry of the offer would trigger the Best Price Rule, *i.e.,* the Offeror must offer the higher price to all repurchase offerees (see section III (2.5) of the Release). Repurchase offers at prices determined by reference to parity plus a premium to parity are also possible in our view. Such pricing mechanisms are implemented to maximize flexibility and to provide for an equitable offer. Although such price determination is not reflected in the Release, we believe that the characteristics of the market price repurchase prevail, but also recommend to seek transaction-specific relief with the TOB in such a case.

Rather than repurchasing convertible bonds, issuers may also consider to launch an ***accelerated conversion offer*** (also referred to as 'early conversion inducement offer'), meaning that the Offeror offers a cash incentive to bondholders to incentivize conversions. As such, the accelerated conversion offer is not a repurchase of convertible bonds, but a monetary incentive to convert a financial instrument into an equity interest according to the Terms of the Bonds. Because of this feature, we are of the view that the rules on public takeover offers are not applicable to accelerated conversion offers.

## 5) Other legal considerations

Pursuant to article 20 (1) SESTA and article 15 (1) (a) SESTO-FINMA, the Offeror has to ***disclose major shareholdings*** in case it attains or exceeds, alone or together with other purchase positions (such as shares or long call options), the relevant thresholds of 3%, 5%, 10%, 15%, 20%, 25%, 33 1/3%, 50% and 66 2/3%. In case the convertible bonds (and with them the conversion rights) are subsequently cancelled, a decrease in previously reported sale positions (short purchase rights by way of issuing convertible

bonds) as well as purchase positions have to be reported when reaching or falling below one of the above mentioned thresholds (see article 15 (1) (a) and (b) SESTOFINMA and article 20 (1) SESTA).

An issuer has to communicate facts not publicly known, which may trigger a significant price movement, to the market (article 72 of the Listing Rules of the SIX Swiss Exchange (SIX) and notes 3 et seq. of the Ad hoc Publicity Directive of the SIX (RLAhP)). Share buyback programs are considered to have the potential to significantly affect the share price and hence will have to be disclosed under the ***ad hoc publicity regime*** (Commentary re RLAhP, note 14). In contrast thereto, no specific rule or guidance regarding the ad hoc publicity of repurchases of convertible bonds exists. We believe that—in the absence of such rule or guidance—the ad hoc relevance of a repurchase of convertible bonds has to be analysed based on the facts of each case in light of the potential share price impact. As a rule, however, we take the view that a systematic, long lasting repurchase of a large amount of convertible bonds is more likely to be qualified as ad hoc relevant than an opportunistic repurchase of small amounts of convertible bonds only.

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## The Swiss Banking Secrecy – Myths and Facts

Reference: CapLaw-2009-30

The Swiss banking secrecy laws have been in the spotlight for many years, but recently enjoyed particular attention and were heavily debated in the public. An announcement made by the Federal Council in mid March provoked widespread coverage and analysis, and led to speculation that Swiss banking secrecy laws have been put dead by the cavalry. This particular article analyzes what has really happened and distinguishes facts from myths.

*By René Bösch*

Before and after and G-20 Summit the Swiss banking secrecy laws have been the subject of heated debates in the press and among politicians in connection with the discussion about 'tax-havens' and the famous black, grey and white lists that the Organization on Economic Co-Operation and Development (OECD) was supposed to prepare and eventually did publish on request by the leaders of the G-20 Summit. Following the immense political pressure mounted on Switzerland over the last few months the Swiss Federal Council announced on 13 March 2009 that Switzerland plans to fully adhere to the OECD tax standard by dropping its reservation against the information sharing provided for in the Model Convention with Respect to Taxes on Income and on Capital.

This step has been heavily debated both nationally as well as internationally, and it has also received wide spread coverage in the press. However, quite a significant number of commentators and journalists over-interpreted this step by claiming that Switzerland had abolished the Swiss banking secrecy and Switzerland as a tax-haven had been cracked. But looking at the fine details, the step, while politically quite far-reaching, is just a small step in legal terms and still preserves the Swiss banking secrecy to a quite significant extent.

Swiss banking secrecy—or better Swiss bank customer secrecy—is principally addressed in and governed by article 47 of the Swiss Banking Act but has its foundation in the fundamental principle of the protection of personality, which fundamental principle is also reflected in the Swiss constitution. The protection of self-relating information—or personal information—is a fundamental principle of Swiss law, expressing the policy that the government shall not have free and unlimited access to personal information. In the context of the bank customer secrecy, a penal and a tax aspect are also relevant: The unauthorized divulgation of protected customer information by a Swiss bank constitutes a criminal offense; and in proceedings before Swiss tax authorities a taxpayer may claim the bank secrecy defense in order not to provide information about his accounts, unless he is alleged to have committed tax fraud. However, it is equally a long standing principal that Swiss banking secrecy protection does not apply in penal proceedings involving criminal offenses such as fraud, money laundering, terrorist financing, etc. Conversely, tax evasion as a matter of Swiss laws is not considered a criminal offense, but simply a civil offense. Therefore, Swiss taxpayers have the bank secrecy defense available when suspected of tax evasion.

Until 13 March 2009, Switzerland adhered to the so-called 'Naples Principle' pursuant to which Swiss authorities did not provide foreign authorities more information than would be available to Swiss authorities. For that reason, the Swiss government did also not grant mutual assistance and thus information sharing in respect of alleged tax evasion by foreign taxpayers. Conversely, Switzerland added a reservation to article 26 of the OECD Model Convention with Respect to Taxes on Income and on Capital that provides for exchange of information in tax matters. Pursuant to that reservation Switzerland did not provide information in case of tax evasion, but only in cases of tax fraud. This principle has been embedded in all double taxation treaties which Switzerland concluded so far.

The announcement of 13 March 2009 relates to one legally simple but psychologically and politically important point: Switzerland withdraws its reservation against article 26 of the OECD Convention, such withdrawal having the following, indirect consequences:

– Switzerland is willing to agree to new double taxation treaties in which the model clause of article 26 is reflected;

- once such new double taxation treaty is agreed and ratified, Switzerland will share information with foreign tax authorities in situations of alleged tax evasion matters upon a sufficient request; and
- information sharing will be provided if the request specifies a sufficiently founded suspicion for tax evasion, names the taxpayer involved, describes the circumstances at hand and specifies the Swiss bank where the tax payer allegedly holds funds.

All this will become law and will be applicable upon the effectiveness of newly negotiated double taxation treaties. The announcement of 13 March 2009 has thus no immediate consequences or effects, other than that Switzerland will now have to negotiate a series of new double taxation treaties.

Moreover, the changes to be reflected in the double taxation treaties ***do not:***

- provide for automatic information exchange;
- allow fishing expeditions or John Doe Summons;
- extend to taxes not covered in the double taxation treaties;
- apply to Swiss residents; and
- apply to facts prior to the entry of the new double taxation treaties.

In summary, fact is that no changes will occur for Swiss residents and for foreigners who did not engage in tax evasion in relation to income and wealth taxes. The only change affects non Swiss-residents: In the future, foreign authorities will have a basis to claim mutual assistance and information sharing in individual, sufficiently founded cases of alleged tax evasion of taxpayers in that foreign state; in such cases Swiss bank customer secrecy may no longer be reserved. It is, however, highly important to note that the bank customer secrecy in itself is not abolished and Switzerland will not agree to automatic information exchange.

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## Transfer of Derivatives Transactions under the 'Special Resolution Regime' for Failing UK Banks

Reference: CapLaw-2009-31

As a result of the crisis in the global financial markets, the UK Government has taken various measures to reform the UK banking regime, to enhance financial stability and to

support increased lending. One such measure is the entry into force of the new Banking Act 2009 on 21 February 2009, which reforms banking regulation by giving new powers to the Bank of England, the Financial Services Authority (FSA) and HM Treasury (together the Tripartite Authorities) to deal with UK banks in financial difficulties. The Banking Act 2009 includes the newly created permanent 'special resolution regime' (the SRR), which gives the Tripartite Authorities the power to transfer all or part of the business of a bank in financial difficulties to a purchaser or a bridge bank and creates a rescue regime for a failing bank. The Banking Act 2009 also establishes new insolvency and administration procedures for banks. The SRR in the Banking Act 2009 replaces the provisions in the Banking (Special Provisions) Act 2008, which was enacted in the context of the nationalization of Northern Rock and expired on 20 February 2009. The power of the Tripartite Authorities to transfer part of the business of a bank under the SRR raises questions with respect to the treatment of pre-existing contracts. This article focuses on how derivatives transactions are protected in this context.

*By Olivier Favre*

## 1) Applicability of SRR

The SRR applies to banks authorized, as UK institutions, to carry out the regulated activity of accepting deposits. The provisions of the SRR are triggered if the FSA establishes that the bank is failing, or is likely to fail, to meet the 'threshold conditions', which are the minimum standards the FSA expects banks to satisfy in order to become and remain authorized by it. These 'threshold conditions' include a requirement for the bank to maintain adequate resources, including financial resources, to perform the regulated activity it is engaged in. The SRR also applies, with certain modifications, to UK building societies.

## 2) Transfer options under SRR

If the SRR applies, the Tripartite Authorities may transfer the business of the bank in one of three ways to save a bank in financial difficulty from insolvency: (i) transfer of all or part of the business to a private sector third party purchaser; (ii) transfer of all or part of the business to a publicly-controlled bridge bank (*i.e.* a company wholly-owned and controlled by the Bank of England and regulated by the FSA); or (iii) transfer of the bank into temporary public ownership. The first and the second measures are exercisable by the Bank of England, while the third measure is exercisable by HM Treasury. The transfer to a bridge bank is meant to operate as a temporary solution until a private sector purchaser can be found. The third measure is viewed as a solution of last resort that is available where the other two options are not feasible.

When exercising the powers given to them under the SRR, the Tripartite Authorities will have regard to the following objectives set out in the Banking Act 2009: (i) to protect and enhance the stability of the UK financial system; (ii) to protect and enhance public confidence in the stability of the UK banking system; (iii) to protect depositors; (iv) to

protect public funds; and (v) to avoid interfering with property rights. In February 2009, HM Treasury published a Code of Practice to the SRR that provides guidance on how the Tripartite Authorities will use the powers of the SRR in order to meet the objectives set out in the Banking Act 2009.

### 3) Partial property transfers

The powers of the Tripartite Authorities under the SRR allow partial transfers of the assets, rights and liabilities of a bank in financial difficulty and, therefore, allow the separation of those assets, rights and liabilities that are not affected by existing or potential future losses from those that are affected by such losses. Where such separation takes place, this is known as a 'good bank/bad bank' structure. The assets, rights and liabilities that are to form part of the surviving 'good bank' may be transferred from the existing bank to a new entity, while all other assets, rights and liabilities may be left behind in the 'bad bank'. Alternatively, the assets, rights and liabilities that are to form part of the 'bad bank' may be transferred to a new entity to be liquidated, while those which are to form part of the surviving 'good bank' are left behind in the pre-existing bank. The intention behind such 'good bank/bad bank' structure is that the 'good bank' will survive as a solvent entity and the 'bad bank' will become insolvent.

The Tripartite Authorities have used their powers to effect partial property transfers under the SRR for the first time in connection with the resolution of Dunfermline Building Society (Dunfermline) on 30 March 2009. The solution that was implemented was a transfer of the principal part of the business of Dunfermline to Nationwide Building Society, combined with a transfer of Dunfermline's social housing portfolio to a bridge bank. The remainder of Dunfermline's business (including commercial loans, acquired residential mortgages, pension liabilities, subordinated debt and certain treasury assets) was put into administration.

### 4) Impact of partial property transfers on bank counterparties

One of the most controversial aspects of the SRR is the impact of partial property transfers on pre-existing contractual arrangements entered into with the failing bank. The main concern is that the risk of a contract being affected by a partial property transfer could lead to legal uncertainty and weaken the confidence counterparties have in doing business with banks that are subject to the SRR.

In order to tackle this issue, the Government consulted with market participants (please see 'Special resolution regime: safeguards for partial property transfers, HM Treasury, November 2008', which is available on www.hm-treasury.gov.uk/consult_special_resolution_regimes.htm) and included certain safeguards into the secondary legislation to the Banking Act 2009 such as: (i) the protection of set-off and netting arrangements, which requires that, subject to certain exceptions, any rights and liabilities sub-

ject to set-off or netting arrangements are transferred collectively, or not at all, in order to avoid a disruption of such arrangements; (ii) the protection of security interests, which requires the collateral asset to be transferred jointly with the secured liability, or not at all, in order to avoid that secured creditors cannot enforce their security; (iii) the protection of capital markets arrangements within the meaning of the Insolvency Act 1986, which requires rights and liabilities forming part of such capital markets arrangement to be transferred collectively or not at all; and (iv) restrictions on reverse transfers which limit, inter alia, the ability of the Tripartite Authorities after an initial partial property transfer to transfer financial instruments back to the transferor.

In addition, a compensation scheme has been established to compensate creditors for a loss suffered as a result of a partial property transfer under the SRR. Under such compensation scheme, a creditor of the bank is entitled to compensation if a loss suffered as a result of the partial property transfer is greater than the loss he would have suffered had the bank become insolvent without a partial property transfer.

### 5) Transfer of derivatives transactions

Derivatives transactions are normally entered into under a market standard master agreement that includes netting provisions applicable in a close-out scenario following the occurrence of an event of default or a termination event. As a result of applying such netting provisions, a single net amount for all terminated transactions is calculated, representing the aggregate value of each terminated transaction. In addition, several master agreements may be linked together under the terms of a master netting agreement. This expands the scope of the netting mechanics across the master agreements subject to such master netting agreement. Alternatively, net amounts due under a master agreement may be subject to set-off under the terms of a set-off arrangement against amounts due by the counterparty. While, under English law, such netting and set-off arrangements are generally viewed as enforceable even in insolvency proceedings, an unlimited power of the Tripartite Authorities to effect partial property transfers and allow the transfer of some, but not all, of the transactions subject to a netting or set-off arrangement could disrupt such netting or set-off arrangement. In such circumstances, counterparties would have to account for those transactions that are split off from a netting arrangement on a gross, rather than a net, basis for the purposes of calculating the credit exposure to the bank and the netting arrangement may not be recognized for regulatory capital purposes if a counterparty is subject to regulatory capital requirements. In order to avoid such outcome, the legislator has put in place a safeguard that aims at preserving the effectiveness of set-off and netting and, at the same time, attempts to give as much flexibility as possible to the Tripartite Authorities to execute partial property transfers.

Instead of creating a safeguard that protects only master agreements commonly used in the finance industry or certain qualifying financial contracts specified in the legislation, the solution that was implemented in the secondary legislation to the Banking Act 2009 is a

broad safeguard that protects all contracts that contain netting or set-off provisions by specifying that a partial property transfer may not provide for the transfer of some, but not all, of the rights and liabilities covered by such netting or set-off arrangement. The safeguard also specifies that the transfer order may not modify or terminate such rights and liabilities. The following rights and corresponding liabilities are excluded from the safeguard, to the extent that they would fall under the netting or set-off arrangement: (i) rights and liabilities arising from subordinated debt; (ii) liabilities to depositors in connection with retail deposits (retail deposits are protected under the Financial Services Compensation Scheme) and rights relating to a retail liability owed to the bank; (iii) rights and liabilities under a claim for damages, an award of damages or a claim under an indemnity which arose in connection with the carrying on by the bank of an activity relating solely to relevant financial instruments; and (iv) rights and liabilities relating to a contract entered into otherwise than in the course of carrying on of an activity relating solely to relevant financial instruments. The legislation also specifies that the safeguard would not be breached, where any rights and liabilities arising from foreign property (with respect to derivatives transactions, *i.e.* rights and liabilities governed by a law of a country outside the UK) cannot be effectively transferred by the transfer order.

As a result of this broad safeguard, all transactions that have, for instance, been entered into under a particular master agreement or under the umbrella of a master netting agreement would have to be transferred as one entire package or not at all, subject to the carve-outs mentioned above. A consequence of this is that, to the extent derivatives transactions to be allocated to the 'bad bank' have been entered into under the same set-off or netting arrangement as other derivatives transactions that would best be allocated to the 'good bank', the Tripartite Authorities would have to determine, when structuring a partial property transfer, whether all derivatives transactions under such set-off or netting arrangement should be allocated to the 'bad bank' or left in the 'good bank'.

### 6) Termination of derivatives agreements

If rights and liabilities under a derivatives agreement are transferred in accordance with the provisions of the SRR, the question may arise to what extent such transfer could constitute an event of default or another event giving rise to a right of the counterparty to terminate the derivatives agreement. While the general provisions of the Banking Act 2009 allow the partial property transfer instrument to specify that the partial property transfer is to be disregarded for the purposes of determining whether an event of default or a termination event has occurred, the netting and set-off safeguard in the secondary legislation to the Banking Act 2009 protects the events of default or termination events included in the derivatives agreement, save for those rights and liabilities which have been carved-out from such safeguard (as mentioned above).

### 7) Outlook

In light of the concerns about partial property transfers that were flagged by some market participants in the consultation process before the secondary legislation to the Banking Act 2009 was finalized, it will be interesting to see whether the market will consider the safeguards that have been put in place as sufficient, and in particular whether the netting and set-off safeguard will be sufficient not to undermine legal certainty with respect to the enforceability of set-off and netting arrangements (please see the letter submitted by ISDA to HM Treasury dated 27 February 2009, available on www.isdadocs.org/c_and_a/collateral-Financial.html, which raises that the netting and set-off safeguard may exclude spot and forward foreign exchange transactions, certain OTC bullion options, certain OTC physically-settled commodity transactions and certain CFDs by using the term 'financial instrument', as defined in MiFID, *i.e.* in Section C of Annex I to Directive 2004/39/EC, and that the use of the word 'solely' in the carve-out mentioned as carve-out (iv) above could lead to the result that all transactions under a master agreement are excluded if only one transaction is excluded).

It will also be interesting to see to what extent the Tripartite Authorities will have to resort to using their powers under the SRR for UK banks that have chosen to participate in the UK Asset Protection Scheme, which offers protection for assets with a high degree of uncertainty about their future performance. Details of such scheme were announced in February 2009. Against payment of a fee, HM Treasury provides protection for 90 per cent of the losses related to the qualifying assets above a certain 'first loss' amount to be borne by the bank.

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## CDS Standardization Aims To Introduce More Clarity

Reference: CapLaw-2009-32

The International Swaps and Derivatives Association recently successfully implemented its '2009 ISDA Credit Derivatives Determinations Committees and Auction Settlement CDS Protocol'—known as the 'Big Bang' protocol. This protocol demonstrates the next step to further strengthen and improve the industry's infrastructure, enhance operational efficiencies and reduce risk in the derivatives business.

*By Thomas Werlen / Stefan Sulzer*

On 12 March 2009, the International Swaps and Derivatives Association (ISDA) published the '2009 ISDA Credit Derivatives Determinations Committees and Auction Settlement Supplement' (the Auction Supplement) to the 2003 ISDA Credit Derivatives Definitions, together with a new protocol (the Protocol)—known as the 'Big Bang' protocol. By its implementation on 8 April 2009, over 2,000 banks and asset managers had already adhered

to the Protocol. The Protocol represents the final step in the process known as 'hard-wiring', aiming to put the industry on a more robust footing by introducing more standardization which makes it easier for investors to know what will happen to credit default swaps (CDS) contracts if debt defaults occur. The new terms include the following:

### 1) Auction process

The Auction Supplement is comprised of the 2009 ISDA Determination Committees Rules (the DC Rules) and the Form of Credit Derivatives Auction Settlement Terms (the Auction Terms). Parties can elect to incorporate the Auction Supplement in new CDS trades by referencing the Auction Supplement in the trade confirmation. For parties adhering to the Protocol, the Auction Supplement will also apply to (i) covered CDS trades outstanding as of 8 April 2009; (ii) new covered trades entered into between 8 April 2009 and 11 January 2011; and (iii) novated trades which would have been covered pursuant (i) and (ii) if the original parties had adhered to the Protocol. Parties who do not agree to include the Auction Supplement in future confirmations, or who do not adhere to the Protocol, will need to settle their trades in accordance with the terms of the relevant confirmation, unless there is an agreement to an alternative approach. The Auction Supplement regulates that, if a company defaults, the outstanding claims linked to CDS contracts will be settled according to a pre-designated procedure rather than in an ad hoc manner, as they were before. The new process eliminates the need for credit event protocols to cash settle CDS transactions.

### 2) Determination committee

By establishing determination committees (the DC), the Auction Supplement creates a binding and streamlined method to address issues affecting CDS in the relevant market. Within each of 5 regions (Americas, Asia ex-Japan, Japan, Australia-New Zealand and Europe), each DC will be comprised of 8 global dealers, 3 regional dealers, 5 buy-side members, 2 non-voting dealers (as alternates), and 1 non-voting buy-side member (as an alternate). The DC will make binding decisions on issues such as whether a company's default has triggered the CDS contract, whether an auction will be held and whether a particular obligation is deliverable.

### 3) Look-back period

The Auction Supplement creates the concept of a 'look-back period' applicable to credit events (60 days) and succession events (90 days). An event will only have relevance for a specific transaction if it occurs during the look-back period. A credit event or a succession event occurring prior to the relevant look-back period will have no impact on the relevant trade even if such an event occurs within the term of such trade. As the look-back period may commence prior to the effective date of a trade, it effectively extends the term within which an applicable event may occur. The concept of the look-back period will not be effective until 20 June 2009.

The Auction Supplement and the Protocol occur alongside other reforms, such as a move to adopt centralized clearing to reduce counterparty risk (see CapLaw-2009-22). Centralized clearing becomes much easier once standardized contracts are in place. In the US, Intercontinental Exchange (ICE) has recently started clearing CDS transactions. In its first four weeks of operations, its subsidiary ICE Trust cleared 613 CDS transactions with a notional value of USD 71 bn.

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## Option Transactions of Swiss Companies in Respect of Own Shares

Reference: CapLaw-2009-33

For various reasons, a company may wish to engage in option transactions with a counterparty—either writing or buying (and selling) call or put options—in respect of its own shares. This article discusses certain legal restrictions and disclosure obligations that apply in this context, observing the views expressed in recent scholarship.

*By Daniel Raun and Roland Truffer*

### 1) Issue

Both the purchase and the sale by a Swiss stock corporation of its ***own shares*** have long been the subject of extensive discussion by legal writers under various aspects. Option transactions in respect of own shares, however, have received more marginal and unsystematic attention. Such transactions may recommend themselves to a company for different reasons; they may, *e.g.,* appear a convenient instrument for managing or hedging holdings of treasury shares or for the implementation of a share repurchase programme, or have an ancillary role in connection with an equity-linked financing transaction.

If a company writes (*i.e.,* grants) put options or acquires call options in respect of its own shares, it is as a consequence bound or entitled, respectively, to ***acquire*** a number of own shares at a pre-determined price. It will therefore normally be interested to see its share price rise after entering into the transaction. Where, conversely, the company writes call options or acquires put options in respect of its own shares, it is bound or entitled, respectively, to ***deliver*** a number of own shares at a pre-determined price; it will therefore typically be interested in (or at least more indifferent to) a fall of its share price.

Important ***tax considerations*** apply to such transactions which are, however, not discussed in this article.

## 2) Legal Restrictions

### a) General

Under Swiss company law, dealings of a company relating to its own shares are generally within the ***authority*** of the board of directors. They do not require shareholder approval, with two notable exceptions: if the company's share capital is to be changed in connection with the transaction (*e.g.,* by cancellation of repurchased shares in a share capital reduction, or by creating conditional capital for the servicing of option or conversion rights), a respective shareholder resolution is required; and if the classification of the company's equity on its statutory balance sheet does not permit the acquisition of own shares under the relevant statutory rules (see below lit. b on the requirement of 'unrestricted equity'), the shareholders need to assent to a re-classification. All dealings of the company furthermore need to be within the bounds set by its ***corporate purpose*** as recorded in its articles of association; that purpose is, however, usually defined in a sufficiently broad manner to permit all types of financing and treasury transactions.

In respect of the directors' (and executive officers') duty to perform their functions with all care and to loyally serve the ***interests of the company*** (article 717 (1) of the Swiss Code of Obligations (CO)), the chief consequence for option transactions is that they may only be conducted at arm's-length terms (even with related parties), and pursuant to a financial strategy deemed in good faith to be conductive to the company's interests. Many authors also refer, in connection with the acquisition and disposal of a company's own shares (or options therefor), to the rule requiring a company's directors to ***treat shareholders equally*** in equal circumstances (article 717 (2) CO). It is maintained as a consequence that both in situations involving an acquisition and a disposal of own shares, the company should, where possible, conduct transactions proportionally with all interested shareholders. The company may, however, depart from that principle where it is justified by its interests and does not result in any undue benefits or prejudices to individual shareholders. A significant financial advantage to the company is generally seen as a conceivable justification for 'unequal treatment'.

### b) Acquisition of Own Shares (Call Options Bought, Put Options Written)

Swiss law provides for certain ***statutory restrictions*** on the acquisition by a company of its own shares, in articles 659-659b CO. Such acquisitions are only permitted to the extent that the aggregate nominal value of the company's total holdings in such shares does not as a consequence exceed 10 per cent of its share capital, and that the company has, on its statutory balance sheet, unrestricted equity in the amount of the consideration to be paid (article 659 (1) CO). Pursuant to article 659b CO, the same restrictions apply where a company's shares are acquired by a subsidiary in which it has a majority shareholding. They do not apply, however, to an acquisition of shares for cancellation in the context of a capital reduction procedure agreed by the general meeting of shareholders.

The described restrictions also have to be observed by a company that intends to ***write put options*** in respect of its own shares. It is, however, controversial in legal doctrine what exactly this implies. Certain writers propose to apply the restrictions only at the time of exercise, holding that the company may only honor put options if the resulting acquisition of own shares complies with the statutory rules. The company would therefore need to make put options granted by it conditional upon its (i) having the necessary unrestricted equity and (ii) not exceeding the 10 per cent limitation at the time of exercise. Proponents of another concept hold that already the granting of put options should for these purposes be treated as tantamount to the acquisition of the underlying shares (at least where they provide for physical settlement, but application is also conceivable to cash-settled options); the company would thus need to have the necessary unrestricted equity, and observe the 10 per cent limitation (for shares held and shares underlying put options cumulatively), at the time when the options are granted. One prominent voice, finally, is altogether critical of the granting of put options by a company for its own shares, considering it inadmissible except in the context of a repurchase offer made to all shareholders.

The ***acquisition of call options*** by the company is generally not held to be subject to the restrictions on the repurchase of own shares (although the company will need to observe these restrictions when deciding on the exercise of the options, to the extent they provide for physical settlement). This view is, however, geared to the typical situation that a call option is acquired at a relatively modest price (option premium), while the exercise price is a sum in the order of the share's current market price. If an option is structured in such a way that a significant part of the underlying shares' current market value is paid in the form of option premium—in exchange for a correspondingly low exercise price -, it would seem adequate to apply the legal restrictions on the acquisition of own shares to the acquisition of such options. An argument could, in fact, be made for application in case of all call options, at least for purposes of the financing of the share premium from unrestricted equity.

### c) Disposal of Own Shares (Call Options Written, Put Options Bought)

Option transactions which may result in the ***disposal*** by the company of own shares do not present problems in relation to articles 659-659b CO.

Article 653b (3) CO, however, concerning conditional capital increases, states that any conversion or option rights granted (sc. by a company in respect of its shares) prior to the registration with the Commercial Register of the conditional share capital are invalid. Some writers hold that, as a consequence of this provision, a company may only write (grant) call options for its own shares at a time when it either has a corresponding conditional share capital, or holds a sufficient number of issued shares in treasury reserved to honor the options in case of exercise. No ***'empty' writing of call options*** would thus be permitted. Others, however, argue that the rule should not be

applied to that effect at least in case of listed companies, because they could always obtain the shares needed upon the exercise of option rights on the market.

### 3) Disclosure

Following the recent revisions of the rules on ***disclosure of material shareholdings*** (article 20 of the Stock Exchange Act and implementing provisions in the FINMA's Stock Exchange Ordinance), positions in options of any description—whether or not permitting physical settlement—enter into the calculation of the aggregate 'long' and 'short' positions to be disclosed. These rules also apply to the company whose shares are concerned, as to any other investor. Not only the creation, purchase or sale, but also the exercise or lapse of options may trigger disclosure obligations, if a relevant threshold is reached or crossed as a consequence. This may, *inter alia,* occur because the movement of the number of shares physically held must be monitored and disclosed separately, in addition to the overall 'long' position.

In respect of the company's obligation to disclose details of holdings and transactions in own shares in the notes to its annual (stand-alone) ***financial statements*** (article 663b (10) CO), legal doctrine is divided on the question of the inclusion of option transactions; the predominant view appears to favor it in case of options granted by the company, but not in case of options bought.

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## Takeover Board Decision Regarding Partners Group: New Rules for Buy-Back Programmes Above 10% Own Shares

Reference: CapLaw-2009-34

By decision of 2 April 2009 in the matter of Partners Group Holding AG (Partners Group) the Takeover Board (TOB) has formally published its recently announced new practice for buy-back programmes in cases where the buy-back programme size, together with own shares already held, may exceed 10% of the registered share capital of the company.

Partners Group intends to launch a buy-back programme via a second SIX trading line for up-to 2,670,000 shares representing 10% of its registered capital but in a maximum amount of CHF 140,000,000. Given that Partners Group already holds approx. 7.85% of own shares, the buy-back may lead to a total shareholding exceeding 10 per cent.

According to article 659 (1) Code of Obligations (CO) a company may not hold more than 10% of its own shares. Under previous practice, buy-back programmes in excess of that limit, typically, were executed in two steps: In a first step, the shareholders' meeting of the company passed a resolution authorising the board of directors to execute the programme *(Ermächtigungsbeschluss);* no special quorum or notarisation was required for this resolution. After the shares had been bought back, at a second shareholders' meeting (typically the next following AGM), shareholders resolved to cancel the shares in accordance with the corporate law provisions on capital reduction (article 732 CO), including an amendment of the articles by way of public deed and a three times creditors' call.

The TOB has now held that with respect to a >10% buy-back programme (including previously held own shares) the requirements of article 732 CO must, in principle, be met in advance and that following course of action was permissible: (i) prior approval in principle *(Grundsatzbeschluss)* of the shareholders' meeting by way of public deed, (ii) based on a special report of the auditors, and (iii), exceeding the threshold of 10% only once the two months waiting period following the creditors' call has lapsed. The TOB further held that it was not permissible to reserve the right, in advance, to resell shares bought back under the programme. De facto, the TOB decision means that as from now buy-back programmes that may result in a buy-back of more than 10% (including previously held own shares) will require two notarised public deeds and potentially two audit reports and creditors' calls (*i.e.,* one of each before start of the programme and a second one at cancellation of the shares).

The TOB adopted its new practice based on a controversial interpretation of corporate law. The decision raises doubts as to whether such practice is permissible since, apart from article 37 of the Takeover Ordinance (defensive measures undertaken by target companies in clear violation of corporate law provisions), takeover legislation does not provide for the TOB to have jurisdiction on matters of corporate law.

## BASF Closes Acquisition of Ciba

Reference: CapLaw-2009-35

BASF Handels- und Exportgesellschaft mbH has completed the acquisition of Ciba Holding AG. The closure of the public tender offer including the transfer of tendered shares to BASF and the payment of the offer price to shareholders who tendered their shares took place on 9 April 2009. According to news releases issued by BASF and Ciba, the public tender offer resulted in BASF now holding 95.8% of the shares of Ciba.

## Zurich Financial Services Completes Share Placement

Reference: CapLaw-2009-36

Zurich Financial Services Ltd. successfully completed the placement of 6,714,096 shares with institutional investors to raise CHF 1.26 billion for the purpose of acquiring, through Zurich's US subsidiary Farmers Group, Inc., American International Group, Inc.'s US Personal Auto Group. The shares placed represent approximately 4.7 per cent of Zurich's registered share capital prior to the placement.

## Bankenkrise: Konsequenzen für die Regulierung (Banking Crisis: Implications for Regulation)

Tuesday, 19 June 2009, 12:15 p.m. – 13:45 p.m. (registration period ends 5 June 2009)

CS Forum St. Peter, St. Peterstrasse 19, 8001 Zürich

Speaker: Prof. Dr. Hans Geiger

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

## Schweizer Bankenplatz: Zurück in die Zukunft (Swiss Financial Center: Back to the Future)

Monday, 15 June 2009, 18:00 – 19:15

Zürcher Kantonalbank, Josefstrasse 222, Zürich

Panel duscussion: Bénédict G.F. Hentsch, Dr. Urs Oberholzer, Urs Rohner

Registration mandatory on
http://www.swissfinanceinstitute.ch/events/aboutus_events_template.htm?event=70