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CROSS-BORDER FINANCING REPORT 2013

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Section 1 – Bank licences

1.1 What licences or approvals do lenders need to have if lending to a borrower in this jurisdiction if a) the lender is a bank or b) the lender is a not a bank? Describe any mitigants typically employed to structure around any such requirements.
No licences or approvals are required to make commercial loans.

Section 2 – Taxes

2.1 Are there any requirements to make deductions or withhold tax from payments made to domestic or foreign lenders in this jurisdiction? Describe any mitigants typically employed to structure around any such requirements.
While interest paid on a loan granted to a Swiss non-bank is generally free from taxes, interest payments may become subject to 35% Swiss withholding tax if such loan qualifies as a bond for Swiss withholding tax purposes.

According to the prevailing practice of the Swiss Federal Tax Administration, a loan qualifies as a bond for withholding tax purposes if: (i) the aggregate number of non-bank lenders (including sub-participations) to a Swiss entity under a facility agreement with identical terms exceeds 10; or, (ii) the aggregate number of non-bank lenders (including sub-participations) to a Swiss entity under various facility agreements (that is, with varying terms) exceeds 20.

Swiss or foreign banks do not count as non-banks. Therefore these rules are referred to as the '10 and 20 Non-Bank Rules'. Also, intra-group lenders, in general, do not count as creditors under these rules.

Typically employed mitigants are:

(i) to restrict the number of non-bank lenders in the facility agreement to a maximum of 10, or to subject the accession of any (additional) non-bank lenders to the facility agreement to the previous approval of the borrower(s); and,

(ii) to oblige any Swiss borrower in the facility agreement to limit the number of its non-bank lenders to a maximum of 20 at any time.

2.2 Is interest on debt tax deductible for borrowers incorporated in your jurisdiction?
For corporate borrowers in Switzerland, interest on debt is tax deductible, provided that there is a legitimate business reason for such interest payment and, if applicable, interest payments to a related party are at arm's length.

2.3 Are there any thin capitalisation rules in effect in this jurisdiction which would impact the amount of debt that can be borrowed/guaranteed by entities incorporated there?
The Swiss thin capitalisation rules restrict the amount of debt raised from related parties as well as the interest paid on such debt. Debt raised from independent third parties is not restricted, provided that the debt is not guaranteed by related parties; but such debt reduces the amount of debt that may be raised from related parties.

Any excess debt from related parties is considered 'hidden equity', which is subject to Swiss capital tax. Interest paid or accrued on loan amounts qualifying as hidden equity is, in general, not tax-deductible. In addition, such non-deductible interest is considered a deemed dividend distribution which is subject to 35% Swiss withholding tax.

2.4 Are there any other important tax concerns that lenders to borrowers incorporated in this jurisdiction should be aware of?
Swiss income taxes at source (*Quellensteuer*) may become due on interest payments secured by Swiss real estate. If so, a Swiss borrower would have to withhold the source taxes from the gross interest payments on the part of the loan which is secured by Swiss real estate. The applicable combined tax rate would be in the range of 13% and 33%, depending on the domicile of the Swiss borrower. However, many double taxation treaties provide that the applicable tax rate is reduced (for example, for lenders in the USA, UK, Germany, Ireland or Luxembourg, which can rely on a double taxation treaty with Switzerland, the applicable tax rate is reduced to nil). However, in particular, if there is no Swiss borrower or the interest is not paid to the lender but to a third party, an advance tax ruling should be obtained from the competent Swiss tax authorities to ensure that no income taxes at source become due.

The Swiss Federal Tax Administration may treat a foreign bond guaranteed by the issuer's Swiss parent as a bond issued by the Swiss company, if the borrowed funds are used in Switzerland. Consequently, interest paid on such a bond may become subject to 35% Swiss withholding tax. Upstream and cross-stream guarantees in favour of the foreign issuer will usually not trigger Swiss withholding tax, but this should be agreed with the Swiss Federal Tax Administration in an advance tax ruling.

Section 3 – Security interests

3.1 Please confirm that viable security is available over the following asset classes, with reference to the documentation or formalities or costs required to create, perfect and maintain such security and confirm whether or not a universal security agreement which grants security over all assets can be utilised.
a) shares
b) bank accounts
c) receivables (including intercompany, shareholder and trade receivables)
d) contractual rights other than receivables
e) insurance policies
f) real property
g) plant, machinery, equipment and other movables
h) intellectual property
i) debt securities
j) future/after acquired property

Security can be granted over the assets listed above under a security agreement for each type of asset at issue (subject to the perfection requirements set forth below).

In order to perfect and maintain a pledge over shares (or other movable objects), the security trustee needs to be in possession of the pledged movable objects during the security period (*Faustpfandprinzip*). As a consequence of this requirement, security over plants, machinery, equipment or inventory is possible, but is usually not taken.

An assignment of bank account balances and receivables is valid without a notification to the debtors. However, prior to such a notification, *bona fide* payments by the debtors to the assignor will release the debtors from their

payment obligations. A pledge of bank account balances and receivables is also possible, but lenders usually prefer assignments.

Security taken over real estate that serves primarily as living accommodation may be limited and in certain cases of assignment or pledge of mortgage certificates, formalities must be observed, but the quality of the security is usually worth the extra effort.

The assignment or a pledge of IP rights may provide additional security. However, since a pledge or a security assignment of trademarks/designs may only be invoked against a non-*bona fide* third-party, registration is advised.

Perfection of Swiss security is usually subject to the transfer of title or possession. Therefore, future/after acquired property will generally require an amendment of the existing security document, with the exception of the assignment of future bank account balances and receivables.

In order to obtain security over all assets of a Swiss company, a combination of a share pledge agreement and of security agreements over the company's assets is required.

3.2 Highlight any issues with securing obligations that may arise in the future.
Generally none.

3.3 Can security trustee or security agent structures be used in this jurisdiction to secure obligations that are owed to fluctuating creditor classes? If not can parallel debt or joint and several creditor structures or similar techniques be employed to similar effect?
Security trustee or security agent structures can be used to secure obligations that are owed to fluctuating creditor classes, provided that the security is taken by way of a security assignment.

Because of the principle of accession (*Akzessorietätsprinzip*), which is applicable to pledges, each of the secured parties would need to be a party to the relevant security agreement. In order to facilitate changes to the secured parties in case of a pledge, occasionally parallel debt structures are used in connection with pledge agreements. While most legal writers agree that parallel debt structures are permissible under Swiss law, there can be no absolute certainty due to the absence of case law.

3.4 Briefly outline any issues that need to be considered when transferring loans and accompanying security interests between lenders.
No transfer tax applies to the transfer of loan shares, but Swiss withholding tax at 35% on interests may become due, if the number of non-bank lenders exceeds 10/20 due to the transfer.

3.5 Can security be granted by an entity which is neither a borrower nor a guarantor? Are there any rights of contribution, subrogation or similar that might arise as a result of granting/enforcing purely third party security that ought to be/can be waived?
Generally yes – to both questions. However, the significance of security provided by third parties (that is companies which are not members of the borrower's group) is very limited.

3.6 Briefly outline the registration requirements, if any, applicable to security interests in this jurisdiction including any practical considerations such as the time or expense associated with registration.
Except for certain types of real estate securities, there are no registration requirements. However, since the assignment or pledge of intellectual property rights may not be invoked against a *bona fide* third party, registration is advised.

3.7 Briefly outline any regulatory or similar consents that are required to create security over a local company's assets.
In the course of enforcement against Swiss real estate held by the security grantor or against the shares in a Swiss company, a confirmation of non-application of the relevant rules by the relevant Swiss authorities may be required, to the extent that excessive reserves of undeveloped land exist or that the property at issue is partly used for residential purposes, if foreign secured lenders were to take possession or if the relevant assets were to be sold to other persons domiciled abroad.

3.8 Briefly explain the rules governing the priority of competing security interests.
Secured creditors rank before unsecured creditors to the extent that their claim is covered by the security. Creditors secured by a pledge will usually take priority pursuant to the sequence in which their pledges have been perfected. Generally, there can be no priority conflicts with regard to security assignments, because the security grantor may not transfer more rights than it is entitled to. However, if an assigned asset were pledged, the pledge would usually take priority.

Section 4 – Guarantees

4.1 Briefly explain any formalities required for guarantees to be enforceable.
A Swiss guarantor's articles of association should allow the company to grant security within the group. If required, the necessary changes to the articles of association can usually be made within two weeks.

4.2 Briefly explain the downstream (parent to subsidiary), upstream (subsidiary to parent) and cross-stream (between sister companies within one group) guarantees available, with reference to the any particular restrictions or limitations. Are there any techniques typically employed to enhance credit support/guarantees that might otherwise be limited?
Under Swiss law, upstream and cross-stream guarantee payments are considered to be constructive dividends and, hence, they are limited to the profits and reserves freely available for distribution in the guarantor's balance sheet. Swiss guarantor limitation language usually contains the obligation of the guarantor to maximise the available assets for distribution. In order to enhance the proceeds from the guarantee, it is standard to combine a guarantee with a pledge over the shares in the Swiss guarantor.

4.3 What regulatory or other consents are required for the granting of downstream, upstream and cross-stream guarantees?
None.

4.4 Briefly outline any enforceability concerns associated with the granting of downstream, upstream and cross-stream guarantees that lenders should be aware of, including reference to any exchange controls or similar obstacles.
Since upstream and cross-stream payments are considered as a distribution of dividends, the rules in connection with the distribution of dividends have to be observed. This includes the preparation of an up-to-date balance sheet by the guarantor and an approval of the resulting distribution by the shareholders' meeting.

In addition, dividend payments are subject to 35% Swiss withholding tax. Therefore, it is required to include language in the finance documents to address the issue.

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Section 5 – Enforcement

5.1 Do the local courts generally recognise and enforce foreign-law governed contracts?
Yes.

5.2 Will the local courts generally recognise and enforce a foreign judgment that is given against a domestic company in foreign courts (particularly the New York or English courts) without re-examining the merits of the decision?
Provided that the prerequisites for recognition and enforcement according to the Swiss Federal Code of Private International Law (for New York decisions) or, in the case of decisions by a Lugano Convention contracting state, according to the Lugano Convention (for English court decisions), are met, Swiss courts will not re-examine the merits of a foreign decision.

5.3 Will the local courts recognise and enforce an arbitral award given against the company without re-examining the merits of the decision?
Yes, Swiss courts will recognise and enforce foreign arbitral awards under the New York Convention without re-examining the merits of the case.

5.4 When enforcing security, what factors significantly impact the time such enforcement takes and the value of the proceeds received from such enforcement? For example, are there any statutory requirements such as (a) holding a public auction; (b) court involvement; or (c) obtaining regulatory consents?
If the underlying security agreement is properly drafted, no public auction, court involvement or regulatory consents are required to enforce security. It may be agreed that the security is enforced by way of private sale or self-sale.

5.5 Briefly comment on the likely cost of any enforcement process.
Enforcement costs for security vary depending on the assets at issue and whether the security is enforced in the course of bankruptcy proceedings by way of private sale or self-sale.

5.6 Are there any restrictions that apply specifically to foreign lenders when taking enforcement action?
Generally no. However, the sale of Swiss real estate that is partly used for living accommodation purposes is limited. This can result in additional enforcement costs, because a split of ownership may be required.

Section 6 – Bankruptcy and insolvency proceedings

6.1 Briefly, outline the main bankruptcy/insolvency processes in your jurisdiction, with reference to any control or influence that creditors can exert on the process, the timeframes usually involved and any mandatory filing requirements.
Swiss bankruptcy and reorganisation proceedings are generally governed by the Swiss Debt Enforcement and Bankruptcy Law.

If a creditor initiates enforcement proceedings and the debtor subject to debt collection under bankruptcy (companies) fails to pay the debt within 20 days, the creditor can request that the judge declares the debtor bankrupt. During the bankruptcy proceedings, an inventory of the debtor's assets is prepared and the creditors will be requested to file their claims. A schedule of claims is drawn up. Creditors whose claims were not included or who want to contest the admittance of other claims can file a claim within 20 days. Once the schedule of claims is final, the proceeds from the realisation of the company's assets are distributed among the creditors. In addition, interim payments may be made before the schedule of claim becomes final.

6.2 Are there any preference, fraudulent conveyance, claw-back, hardening periods or similar issues or preferential creditor rights that lenders should be aware of?
Yes, the enforceability of any contract may be limited under the rules of the Swiss Federal Act on Debt Enforcement and Insolvency.

- In particular, the following transactions may be fully or partially voidable: (i) transactions carried out during the year prior to the bankruptcy or insolvency decree, in which the Swiss security grantor accepted to receive no consideration at all or a consideration out of proportion to its own performance; (ii) certain financially inadequate transactions, if carried out during the year prior to the bankruptcy or insolvency decree and if the Swiss security grantor was at the time of the transaction already insolvent; however, the transaction is not voided if the recipient proves to have been unaware of the security grantor's insolvency; and, (iii) all transactions which the Swiss security grantor carried out during the five years prior to the bankruptcy or insolvency decree with the apparent intention of disadvantaging its creditors or of favouring certain of its creditors to the disadvantage of others.
- What must be kept in mind furthermore is the Swiss Parliament has recently decided to reverse the burden of proof for preference claim according to (i) or (iii) above. Close third parties (for example, related companies) will need to substantiate that they have not received any advantages or did not know about the disadvantage. If no referendum is initiated by October 2013, these changes will enter into force, very likely already, in January 2014.

6.3 Do bankruptcy/insolvency processes provide for any kind of stay/moratorium on enforcement of lender claims? If so, does the stay/moratorium apply to the enforcement of security interests?
During a debt restructuring, moratorium enforcement proceedings can neither be initiated nor continued. However, enforcement proceedings for the realisation of collateral for claims secured by a mortgage of real estate may continue, but the property may not be realised during the moratorium. In addition, with the granting of the moratorium, interest ceases to accrue against the debtor for all unsecured claims, unless the composition agreement stipulates otherwise.

Section 7 – Other matters

Financial assistance

7.1 Are there any restrictions in place on locally incorporated companies in assisting the acquisition of shares in itself, its sister companies or in its holding companies? Do these prohibitions apply to all forms of company, to companies being acquired which are incorporated outside this jurisdiction and indirect holding companies?
Apart from upstream and cross-stream limitations there are none.

7.2 Are there any exceptions to these restrictions? Are there any structuring techniques that can be employed in order to achieve target collateral support?
Not applicable.

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The head of Prager Dreifuss' corporate and M&A team, he specialises in M&A (mainly strategic buyers), corporate finance, banking, restructuring and bankruptcy proceedings, and general corporate matters. He advises clients in all types of domestic and cross-border transactions and represents creditors, including banks, hedge funds and other financial institutions, in insolvency and restructuring proceedings. He also represents clients in court and before arbitrational tribunals. Lately, his practice has involved acquisitions of Swiss targets for major strategic buyers from a variety of industries, such as chemical, automotive, transport, as well as insolvency litigation matters (ISDA Master Agreements, aircraft financing, and so on).

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Flink focuses mainly on restructuring transactions and financing. He is experienced in representing lenders as well as borrowers in the negotiation of credit facilities regarding leveraged finance and project finance as well as in acquisition finance for private equity companies and providers of senior and mezzanine debt.

He has recently represented major banks in domestic and cross-border transactions, in the areas of corporate finance, real estate and intellectual property.