Restructuring and insolvency in Switzerland

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Switzerland

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In 2004, 10,524 new bankruptcy proceedings against individuals or firms were opened in Switzerland. Creditors lost SFr4.7 billion in bankruptcy proceedings closed during that year. Composition proceedings opened and losses realised through such proceedings must be added to these figures, but no relevant statistics are available.

Insolvency legislation in Switzerland is a federal matter and the 1889 Federal Act on Debt Enforcement and Bankruptcy, as amended, is the main source of legislation. Separate laws apply to enforcement actions against counties and cantons, bankruptcy and composition proceedings against financial institutions, bankruptcies of insurance companies and so on.

Cantons are responsible for the establishment of debt enforcement and bankruptcy offices, and one or two levels of court supervision. In addition, the Federal Tribunal supervises the (upper) cantonal supervisory authority. Cantonal public bankruptcy offices may be adequate to deal with bankruptcies of smaller businesses. They handle bankruptcies where the debtor's assets are insufficient to cover the costs of ordinary bankruptcy proceedings. Public bankruptcy offices are not staffed, nor are their personnel trained, to handle large and complex bankruptcies.

A private bankruptcy administration, such as an accounting or law firm, may be elected at the first creditors' meeting if only 25 per cent of all known creditors are present. If the quorum is not met, the public bankruptcy office will handle the proceedings up to the second creditors' meeting, which takes place only after the schedule of claims has been published. This quorum provision operates as a powerful incentive for debtors and creditors to avoid bankruptcy in favour of a moratorium, usually followed by liquidation pursuant to a composition agreement.

Companies are rarely rescued through court-initiated restructuring proceedings, but viable parts of a business frequently survive: they are taken over by a new legal entity for what is considered an acceptable price by the old management and commissioner and the judge, who must (among other things) approve disposals of fixed assets during a moratorium, or by the liquidator and creditors' committee, once a composition agreement with assignment of assets has become binding. The remaining assets are then sold for the creditors' benefit. Since fresh money is injected into a new legal entity, it is effectively shielded from creditors of the insolvent company (at least on a national level, as long as these monies and the assets bought with such monies remain in Switzerland), provided that the purchase price for the viable parts of the business is fair and does not further harm the interests of the creditors

of the insolvent company. The existing legislation thus enables the survival of valuable businesses or parts thereof, while preserving the rights of creditors of an insolvent company.

The lack of provisions on consolidation of insolvency proceedings relating to companies that form part of a corporate group gives rise to many difficulties in complex insolvencies. Groups of companies are frequently managed as though they were a single legal entity; but in restructuring proceedings, each legal entity must be treated separately. Unless guarantees or legally binding letters of comfort are issued by parent or sister companies, creditors cannot usually hold the parent or sister company liable for debts incurred. The courts sometimes use the enterprise liability doctrine to disregard the separate legal entity of a parent and its subsidiary, and a parent company may be held liable if its actions gave rise to reasonable expectations that it would financially support its subsidiary and it subsequently did not fulfil those expectations. The legal obligation to prepare consolidated accounts does not give rise to joint liability of all companies of a group.

1 The legal framework and the effectiveness of court processes/ legal remedies

1.1 Describe the nature and the effectiveness of the following:

(a) Debt recovery remedies where the creditor has no security

Outside bankruptcy or composition proceedings, creditors – whether secured or unsecured – wishing to enforce a receivable may request the competent debt enforcement office to serve a formal enforcement notice on the debtor. If the debtor does not object within 10 days, enforcement may proceed swiftly. If the debtor objects, however, the creditor must obtain an enforceable judgment or award, which may take years. The exact timescale depends on the jurisdiction involved, the levels of appeal available and, of course, the workload of the courts at the time.

(b) The enforcement of security

If the pledge agreement so provides, secured creditors may execute their security (with the exception of immovable property) by private sale before obtaining an enforceable judgment. It is up to the debtor (and/or the third-party owner of the security) to initiate legal proceedings against the creditor, should it wish to object to the creditor's course of action. Otherwise, the enforcement of security requires an enforceable judgment or award, pursuant to which the competent debt enforcement office sells the security through public auction. The net proceeds of the sale are distributed to the secured creditor(s) up to the amount of the judgment.

(c) Corporate bankruptcy/ liquidation processes

Liquidation of a company may result from a shareholders' decision in the form of a public deed recorded in the Commercial Register, or from the opening of bankruptcy proceedings on the petition of the debtor, a judgment creditor or the holder of a bill of exchange. Any creditor may request the court to open bankruptcy proceedings without prior enforcement proceedings if a debtor has ceased making payments. However, a court will not come to the conclusion lightly that the debtor has indeed ceased making payments. Liquidation may also result from a composition agreement with the assignment of assets.

(d) Formal corporate rescue processes

Rescue of a debtor may result from:

- recapitalisation by shareholders or lenders;
- an out-of-court agreement with creditors;
- the judge's postponement of bankruptcy; or
- a composition agreement under which the debtor pays all privileged claims, as well as an

agreed portion of its unsecured and non-priority claims, in return for a release from the remaining portion of such claims.

Rescue of a company must be distinguished from rescue of a business or part of a business. The company is the legal entity which owns assets and owes debts. As creditors rarely give up part of their rights voluntarily, the rescue of insolvent and over-indebted companies is an exception; in contrast, however, the rescue of a business or viable parts of a business is not unusual. Such a business is usually taken over by a new, solvent and – hopefully – properly financed company, with the insolvent company being liquidated thereafter.

If there is a substantial risk of over-indebtedness, the board of directors must prepare an interim balance sheet and submit it to the auditors for review. If this shows that the company's debts exceed the assets, as valued on both a going-concern and a liquidation basis, the board is under a statutory duty to notify the judge, who will pronounce the company bankrupt (see section 1.5 for further details of the directors' notification obligation). In exceptional cases the judge may postpone bankruptcy if he is presented with a restructuring proposal which he considers has sufficient chances of success. Postponing bankruptcy is a very flexible procedure: the judge may or may not appoint a curator, leave the existing management in power and publish the postponement of bankruptcy.

A company in financial difficulties which cannot obtain new capital from its shareholders may seek an out-of-court restructuring instead of requesting postponement of bankruptcy. To do this, the company must convince enough lenders – and possibly also trade creditors – to extend payment terms, forgive part of the debt or inject fresh money.

A company may also seek court protection from creditors with a view to reaching an agreement with its creditors in the course of composition proceedings. In practice, this alternative is pursued most often, because it suits both debtor and creditors reasonably well. On applying for court protection, the debtor receives a provisional moratorium of up to two months, followed by a moratorium of four to six months, which may be further extended to up to two years. During this time the debtor may continue its business activities under the supervision of a commissioner. In this situation the creditors are likely to end up with a higher dividend, even though composition agreements often result in the liquidation of the debtor's assets for the creditors' benefit.

In contrast to bankruptcy proceedings, upon applying for a moratorium the debtor may propose an experienced and properly staffed commissioner for appointment by the competent judge. There are no statutory qualifications that must be fulfilled in this regard; some judges favour accounting firms, while other judges prefer to appoint attorneys. Creditors may appeal against the appointment. Subsequently, the debtor and creditors that are party to a composition agreement involving an assignment of assets may elect an experienced and properly staffed professional liquidator. The liquidators are supervised and controlled by a creditors' committee. In composition proceedings liquidators have much more flexibility as to how to sell the debtor's assets than in bankruptcy proceedings: under composition agreements, disposal of assets can occur at any time and in any manner, as agreed upon between the liquidators and the creditors' committee, while in bankruptcy proceedings it can usually happen only after the second creditors' meeting and usually only through public auction. Exceptions apply for assets which are prone to swift depreciation, require costly maintenance or incur disproportionately high storage costs, as well as for assets with a stock exchange or market price. Such assets may also be realised immediately in bankruptcy proceedings.

Whatever insolvency proceedings apply, secured and unsecured creditors must file their claims, supported by evidence, to the bankruptcy administration (ie, the competent public bankruptcy office or the individual(s) elected by the creditors' assembly). The bankruptcy administration will then determine (subject to the veto powers of the creditors' committee) whether – and if so, to what

extent and in what class – each creditor is admitted to the schedule of claims. Creditors not fully admitted to the schedule of claims may contest this decision in court. Creditors may also challenge the admission of other creditors to the schedule of claims.

(e) Informal corporate rescue processes

As long as sufficient liquidity and equity are available, the owners and/or management may try to rescue a company in difficulties in any way they see fit. This usually involves a (partial) reduction of existing debt and equity, as well as the injection of fresh cash, whether by way of debt or equity or mezzanine financing, and other measures designed to restore the company's profitability.

1.2 What are the formal processes to effect a liquidation of the company's assets?

A judgment creditor or the debtor, acting through the board of directors or, if the board fails to act, the auditors, may request the competent judge to open bankruptcy proceedings or grant a moratorium which eventually results in the liquidation of the debtor's assets.

1.3 What is the effect on debt collection and the enforcement of security of:

(a) An adjudication of corporate bankruptcy/liquidation?

The opening of bankruptcy proceedings leads to a channelling of enforcement efforts: all assets owned by the debtor at the commencement of the bankruptcy proceedings and which are subject to seizure then form the bankruptcy estate. The management no longer has power to dispose of the debtor's assets and the competent public bankruptcy office takes control of the bankruptcy estate with effect from the opening of bankruptcy proceedings.

All other enforcement proceedings pending against the debtor cease and new enforcement proceedings relating to claims that arose before the bankruptcy began are barred. Civil court actions to which the debtor is a party and which affect the composition of the bankruptcy estate are stayed, and may only be resumed 10 days after the second creditors' meeting or, where there are no creditors' meetings (eg, in summary bankruptcy proceedings), 20 days after the schedule of claims is made available for inspection. In practice, such stays often last for years.

(b) The commencement of a formal corporate rescue process?

Almost identical results can be achieved where an insolvent company petitions for a moratorium in order to negotiate a composition agreement with its creditors. However, the insolvent company must still have the means to cover the costs of professional commissioners and liquidators – at least during the two-month period of a provisional moratorium.

A debtor seeking to reach an agreement with its creditors must submit a reasoned application and a draft agreement to the composition court. The court may immediately take measures to preserve the debtor, such as provisionally approving a moratorium for a maximum of two months, and appointing a provisional commissioner and entrusting him to examine the debtor's financial position, income basis and the prospects of recovery. If there are prospects of recovery, the composition court will grant the debtor a moratorium of four to six months and appoint one or more commissioners. Upon application of the commissioners, the moratorium may be extended to a maximum of two years.

During the moratorium, enforcement proceedings cannot be initiated or continued, with few exceptions. Periods of limitation and peremptory deadlines do not run. Interest ceases to accrue against the debtor on all unsecured debts, unless the composition agreement stipulates otherwise. The debtor may continue its business activities under the commissioner's supervision. The composition court may order that certain acts require the commissioner's participation in order to

be legally valid, or authorise the commissioner to take over the management from the debtor. The debtor needs the approval of the composition court to divest, encumber or pledge assets, to give guarantees or to make gifts during the moratorium; otherwise, such acts are null and void.

In bankruptcy, but not in composition proceedings, creditors secured by pledges of chattels are required to deliver up their collateral for sale by the bankruptcy administration. Where they do so, they maintain their priority status as privileged creditors. The bankruptcy administration will review the secured creditors' claims and ascertain whether:

- the claim is wholly or partially invalid; and
- the security rights claimed by the creditor are invalid or can be avoided.

If a claim is admitted to the schedule of claims as a secured claim, it will be satisfied first out of the proceeds of the collateral upon which the claim is secured. In composition proceedings, secured creditors are not required to deliver up to the commissioner the collateral in their possession. If the pledge agreement so provides, the creditor is entitled to liquidate the pledged chattels by private sale or on a stock exchange, as they see fit. In a composition agreement with assignment of assets, the commissioner may request the secured creditor to realise the pledged chattels within a certain timeframe (of at least six months). Alternatively, creditors with claims secured on chattels may initiate or resume enforcement proceedings for the realisation of their collateral after a composition agreement has been approved by the competent court and such approval has been duly published.

Towards the end of the moratorium, the commissioner submits a report and his recommendation to the composition court. Afterwards, the composition court holds a public confirmation hearing. Each creditor has the right to participate in this hearing and voice its concerns.

Confirmation of a composition agreement requires ratification by a qualified majority of the unsecured and non-priority creditors (see section 7.4).

To obtain confirmation of a composition agreement with assignment of assets by the composition court, the projected proceeds must exceed those that would likely result from bankruptcy. The decision of the composition court may be subject to appeal. The debtor's existing management loses its powers in favour of the liquidators only after the confirmation of a composition agreement with assignment of assets.

The only formal alternative to a composition agreement with assignment of assets is payment of a defined percentage of claims to all unsecured creditors. In such cases the court must be satisfied that the sum offered is proportionate to the debtor's means.

(c) The initiation of an informal rescue process?

Debtors not subject to bankruptcy proceedings (mainly individuals) can try to negotiate a (so-called) amicable private settlement of debts. The law provides that the composition court will appoint a commissioner and grant a moratorium of up to three months, which may be extended to a maximum of six months. Such semi-formal rescue proceedings are rare. In the case of insolvent corporations and other debtors subject to bankruptcy proceedings, no semi-formal rescue proceedings are provided by law. Truly informal rescue proceedings are common, but are only practical where at least the main creditors voluntarily agree to postpone individual enforcement efforts so as not to jeopardise the rescue proceedings.

1.4 Are insolvency procedures started in another jurisdiction in respect of a corporation incorporated in your jurisdiction recognised?

The 1987 Federal Act on International Private Law contains a chapter on bankruptcy and composition with creditors. A foreign order of bankruptcy or composition rendered by the courts of the debtor's domicile shall be recognised at the request of the foreign trustee or a creditor of the bankruptcy estate, provided that:

- the order is enforceable in the state in which it was rendered;
- reciprocity is granted by that state; and
- the order does not violate Swiss public policy.

Recognition of a foreign bankruptcy order leads to ancillary bankruptcy proceedings in Switzerland. Swiss assets of a foreign bankrupt are seized and liquidated in Switzerland and distributed to secured and privileged creditors domiciled in Switzerland, if any. The remaining proceeds are sent to the liquidators in the main proceedings for distribution to the creditors.

Chapter 11 proceedings opened in the United States against a company incorporated in Switzerland do not qualify for recognition and enforcement in Switzerland. They are therefore better initiated by the Swiss liquidators or administrators so that recognition in Switzerland is not required.

Chapter 11 proceedings opened in the United States against a US company may result in ancillary proceedings in Switzerland if the company has Swiss assets.

1.5 In what circumstances would the directors or officers of a company in financial difficulties face potential personal liability for continuing to trade?

The members of the board of directors and all persons engaged in the management or liquidation are liable not only to the company, but also to each shareholder and to the creditors for damage caused by intentional or negligent violation of their duties.

The duties of the board are very explicit in case of loss of capital or over-indebtedness. If the latest annual balance sheet shows that half the share capital and the legal reserves are no longer covered by the company's assets (loss of capital), the board of directors must call a general shareholders' meeting immediately and propose financial reorganisation. In case of a substantial risk of negative equity (over-indebtedness), the board must prepare an interim balance sheet and submit it to the auditors for review. If the assets, regardless of the valuation method applied (going-concern or break-up value), no longer cover the company's debts, the judge must be informed immediately, unless creditors with claims at least equal to the amount of over-indebtedness subordinate their claims to those of all other creditors. Failure to notify the judge exposes the board members to personal joint and several liability for damages.

The Federal Supreme Court has acknowledged that the board of directors may first examine the possibility of financial reorganisation. If the board concludes that reorganisation is feasible, it is entitled to postpone notification for a reasonably brief period. Mere hope or a vague expectation of a successful reorganisation does not justify postponement; there must be reasonable grounds for such expectations and a clear prospect of success.

The board of directors of an over-indebted company can petition the judge to postpone bankruptcy, but this is risky. In order to obtain a postponement, the board must formally notify the judge that the company's assets, irrespective of the valuation method applied (going-concern or break-up value), are insufficient to cover its debts. If the judge rejects the petition, the company will most likely be declared bankrupt (rather than granted a moratorium), and management will lose its powers.

Other non-transferable and inalienable duties of the board include:

- setting up a proper organisation;
- structuring the accounting system;
- installing financial planning and control systems; and
- providing an annual report.

Claims for damages arising out of negligent management against the directors and officers of an insolvent company are invariably recorded among the company's assets, and are often enforced in court or through out-of-court settlements.

If the creditors as a whole do not intend to pursue such a claim, each individual creditor admitted to the schedule of claims may request that it be assigned the right to enforce such a claim at its own risk and for its own benefit. It may use the proceeds to cover its costs

and satisfy its claim. The remainder of the proceeds, if any, must be paid into the estate.

Since the enforcement costs of such actions are high, the risk is usually taken only by large creditors that have a good chance of getting a substantially higher dividend on their claims than other ordinary creditors.

2 What are the advantages and disadvantages of triggering a formal procedure?

A company that needs protection from enforcement actions by its creditors can try to secure this through an agreement with and between the main creditors. If the company is unsuccessful, it must enter into formal composition proceedings and request a moratorium.

In contrast to an out-of-court-settlement, a composition agreement need not be approved by each individual creditor; it must only be endorsed by a qualified majority of creditors (see section 7.4), and requires court approval to become legally binding.

In a formal procedure control is transferred to the commissioner and the court, and subsequently to the liquidator, supervised by the creditors' committee and the court. The company and its creditors lose control. The commissioner may, but need not, enter into existing agreements between the company and its workforce, trade and finance creditors, and so on. Frequently, companies massively reduce their workforce and sell individual assets or entire businesses during a formal moratorium prior to going into liquidation.

The main advantage is the shielding of the company from (most) enforcement actions by individual creditors. The main disadvantages are that sales under distress rarely result in high prices and the necessary working capital tends to increase.

3 What are the practical options for out-of-court restructuring?

If a company in financial difficulties has a small number of major creditors – that is, most of its liabilities are owed to a small number of creditors – it can approach these creditors to seek to negotiate an out-of-court settlement. Banks are generally willing to enter into such discussions. They may, however, insist that the equity holders inject fresh capital, or that the company hire external management consultants or appoint new management with a view to selling the company or its businesses and/or assets. Private equity investors and traders in distressed debt increase the exit options for creditors of a company in need of restructuring.

Informal rescue processes often lead to an immediate change of executive management, while the commencement of formal rescue proceedings usually does not.

Venture capital companies commonly buy privately held companies facing financial difficulties, replace existing management with 'turnaround' management, refinance the companies and sell them when a restructuring and turnaround has been successfully completed.

There may be tax consequences of a write-down of liabilities in an informal restructuring. It is important that discussions take place with the tax authorities as part of such restructuring.

Out-of-court settlements need not be made public. However, listed companies must comply with the Listing Rules regarding *ad hoc* publicity, and the granting of a moratorium necessarily results in publicity.

The practical barrier to out-of-court restructuring is generally the availability of finance to continue the business while negotiations take place. As in most countries, lenders are unwilling to provide new money unless there is additional collateral available. If additional collateral is not available, creditors will need to be persuaded that the outcome of a bankruptcy will be much worse than the possible loss of the new money.

4 What is the effect on the management of a company of:

(a) An adjudication of corporate bankruptcy/liquidation?

Management loses its powers with the final and enforceable declaration of bankruptcy. A court order postponing bankruptcy may also include provisions for the removal of existing management.

(b) The commencement of a formal corporate rescue process?

The court's confirmation of an ordinary composition agreement does not adversely affect management's powers. Management usually retains (most of) its powers during any moratorium preceding a composition agreement. It loses its powers with the final and enforceable confirmation of a composition agreement with assignment of assets by the court. If the composition is in the form of the payment of a percentage of claims to all unsecured and non-privileged creditors, management will retain its powers.

(c) The initiation of an informal corporate rescue process?

This has no direct effect on management.

5 Parties in interest/key players

Who is responsible for the 'case management' control and administration of:

(a) A corporate bankruptcy/liquidation?

Bankruptcy administrator: In bankruptcy proceedings, the bankruptcy administrator, in lieu of prior management, has powers (subject to judicial review) to dispose of assets and to admit claims. The bankruptcy administrator does everything necessary for the maintenance and realisation of the bankruptcy estate, represents the estate in court proceedings and prepares a schedule of claims. The schedule of claims is submitted to the creditors' committee, if one has been appointed. The creditors' committee may reject claims admitted by the bankruptcy administrator within 10 days, but cannot admit claims rejected by the bankruptcy administrator. The bankruptcy administrator sells the assets and distributes the proceeds to the creditors admitted to the schedule of claims.

Creditors' committee: A creditors' committee may be elected in bankruptcy proceedings and must be elected in liquidation proceedings pursuant to a composition agreement. The election takes place at the first creditors' meeting. The committee usually:

- supervises the management activities of the bankruptcy administrator or liquidators;
- authorises the debtor to continue running its business;
- approves accounts;
- authorises initiation and continuation of court proceedings;
- approves entering into settlement or arbitration agreements;
- objects to claims admitted by the bankruptcy administrator or the liquidators; and
- orders payments on account to be made to creditors during the course of bankruptcy or liquidation proceedings.

(b) A formal rescue?

Provisional commissioner: Upon receiving an application for a moratorium, the court may grant a provisional moratorium for two months and appoint a provisional commissioner, who will examine the debtor's financial position, income basis and the prospects of recovery during the provisional moratorium.

Commissioner: If the court has granted a definitive moratorium, the commissioner must draw up an inventory and estimate of all the debtor's assets. The commissioner also advertises for claims,

convenes and chairs the creditors' meeting, and reports on the debtor's assets and income basis.

Privileged creditors: A composition agreement may be approved in court only if all privileged creditors that have not waived their privilege can be paid in full. Privileged creditors, such as employees, are therefore important players in restructuring proceedings.

Existing management: Subject to the powers of the commissioner and the need for court approval to divest, encumber or pledge assets, to give guarantees or to make gifts, existing management retains its powers until a composition agreement providing for the liquidation of assets becomes binding or the company is declared bankrupt.

(c) An informal rescue?

Lenders: Most large credit institutions have recovery departments that try to resolve problem situations with borrowers. Because of clauses often found in loan agreements, banks are entitled to receive more financial information than is publicly available. A loan may be called due immediately if a borrower is in breach of contract, often resulting in the borrower's insolvency and triggering formal restructuring or bankruptcy proceedings.

Accountants/lawyers and other advisers: Trust between creditors and debtors can often be enhanced by recognised experts in the field of recovery. They can act as intermediaries and take a neutral position. Advisers play an important role, particularly in large restructurings.

Auditors: The auditors are appointed by the general assembly. Audits for large and listed companies must be performed by specially qualified auditors (in terms of education and experience). If there is a substantial risk of over-indebtedness, an interim balance sheet must be prepared and audited. If the board of directors does not comply with its duty to inform the judge of the company's over-indebtedness, the auditors must do so if over-indebtedness is obvious. The auditors' inactivity in such situation exposes them to liability for damages. Auditors must not assume management responsibility for a company they audit, and must not assume the role of the commissioner or bankruptcy administrator in insolvency or composition proceedings.

Board of directors: The members of the board of directors must carry out their duties with due care and duly safeguard the company's interests over the possibly conflicting interests of the shareholders. This also applies to the members of a subsidiary's board of directors. The board must observe strict rules in case of loss of capital or over-indebtedness, as outlined in section 1.5.

Shareholders: Shareholders must vote in a general meeting on any restructuring plan submitted by the board of directors. Shareholders are often asked to contribute to the refinancing of a company, which frequently occurs through a reduction in capital and simultaneous increase in the original level of the share capital, with such increase to be fully paid up.

6 What financial information is available to creditors?

The Federal Code of Obligations requires all companies to prepare an annual report, comprising a business report, a profit-and-loss statement, a balance sheet and notes. If a company joins one or more companies under joint management and certain thresholds are exceeded, it must prepare consolidated accounts. An auditor must review the statutory accounts, but not the consolidated accounts. These accounts must be available for inspection by the shareholders. Separate rules apply to banks, insurance companies, securities dealers and the like.

Privately held Swiss companies not listed on a stock exchange are under no statutory obligation to publish their accounts. Companies listed on the Swiss Stock Exchange (SWX) must publish their audited annual reports and group reports. In addition,

interim statements, which need not be audited, must be published on at least a semi-annual basis.

The Code of Obligations allows accounting standards which are less detailed than comparable international guidelines, such as International Financial Reporting Standards or US Generally Accepted Accounting Principles. The code provides that the total amounts of contingent liabilities, pledged assets, assets under retention of title, leasing commitments, issued bonds, substantial participations, modifications of hidden reserves, revaluations, own shares and variations from the going-concern principle must be disclosed in the notes. It also stipulates that companies with shares listed on a stock exchange must disclose significant shareholders and their participations (over five per cent of the voting rights) in the notes.

Only the accounts of companies listed on the SWX must be 'true and fair'.

Listed companies must also publish *ad hoc* any price-sensitive information. Reorganisation efforts justify postponement of publication, as long as such information remains completely confidential and is not leaked.

Creditors of solvent companies have no statutory rights of privileged access to financial information. In composition proceedings, the commissioner must inform the creditors of the debtor's financial situation. At the latest, this must be done during the creditors' meeting towards the end of the moratorium (which may last for two years). In major composition proceedings, interim information by the commissioner through, for example, the Internet, has become customary. In informal proceedings, a creditor may condition its agreement to enter into restructuring negotiations on disclosure of adequate financial information.

7 Common questions

7.1 Funding and the priority given to new money

If an insolvent corporation requires urgent working capital funding, what difficulties are likely to be encountered in the provision of such funding?

If a debtor in financial difficulties needs additional funding, it may raise new money without incurring the risk of a voided transaction if the restructuring subsequently fails. Debts incurred by the bankruptcy estate or by a company under moratorium – with the commissioner's consent – must be paid first. The commissioner will be reluctant to approve significant new loan agreements because he might expose himself to liability and jeopardise payment of his fee. No statutory priority is given to lenders of new money under any other circumstances. This is one of the reasons why, in Switzerland, a new company is usually established to take over viable parts of a failing company's business.

Lender liability is sometimes discussed in Switzerland. In general, there is little risk of lender liability under insolvency laws. However, banks must be careful to avoid acting as quasi-directors of their borrowers lest they risk joint and several liability for damages like any other board member.

7.2 Ranking of creditors

In what order are creditors paid in a corporate bankruptcy/liquidation?

Secured claims are satisfied directly out of the proceeds of the collateral's realisation. Mortgage creditors are satisfied according to their rank, which, in the absence of contractual stipulations to the contrary, is determined by the time of entry in the Real Estate Register. The first rank is paid in full before the second rank receives any dividend, and so on.

Unsecured claims (including secured claims to the extent not covered by collateral) are ranked into

three classes. Creditors ranked in the first class are paid in full before creditors in the second class receive any dividend. Creditors in the second class must be paid in full before ordinary creditors ranked in the third class receive any dividend.

Employees' claims under the employment relationship which arose or became due in the six months prior to the opening of bankruptcy proceedings, and claims that arise from termination of the employment relationship due to the opening of bankruptcy proceedings, as well as claims concerning accident insurance, pension claims and claims of pension funds against employers, rank in the first class. Premium claims of social security systems (eg, old age, disability, accident, unemployment, health insurance) rank in the second class, while all other claims fall into the third class (including those claims of secured creditors which could not be satisfied through the sale of the security).

7.3 Avoidance of antecedent transactions

Are there any legal provisions that might operate to invalidate the creation of security, the disposal of an asset or the payment of a creditor by a company in financial difficulties?

One chapter in the Federal Act on Debt Enforcement and Bankruptcy relates to avoidance actions. Gifts made, collateral given for existing obligations which the debtor was not bound to secure, due debts settled by means other than payment and unmatured debts paid in the year prior to the opening of bankruptcy proceedings can all be voided.

Further, any transactions in the five years prior to the opening of bankruptcy proceedings can be voided if the debtor executed them with the apparent intention of disadvantaging its creditors or favouring certain creditors to the detriment of others.

Court practice has significantly expanded the scope of application of the provisions relating to the avoidance of actions for wrongful intent. It is now sufficient that the debtor could, and therefore should, have realised that the effect – if not the intent – of the action would disadvantage its creditors. For the avoidance action to succeed, it is sufficient that the beneficiary could, and therefore should, have realised that the debtor's actions would produce such an effect.

7.4 'Cram-downs'

What is the position of both unsecured and secured creditors that vote against, do not agree with or do not consent to a formal or informal rescue plan?

Parties that are against an informal rescue plan are free to enforce their claims as they see fit. Formal rescue plans (composition agreements) require acceptance by a majority of creditors representing two-thirds of total claims, or by one-quarter of creditors representing three-quarters of total claims. Composition agreements approved by the required majority of creditors become binding on all creditors once the composition court has approved the agreement in a final and enforceable order. This binding effect extends to all claims which arose before the publication of the moratorium or which have arisen since without the commissioner's consent, with the exception of secured creditors for the amount covered by the realisation of the collateral.

7.5 Creditor protection

What actions can creditors take if they are not satisfied with the conduct of either a formal rescue procedure or a corporate bankruptcy/liquidation?

Liquidators in composition proceedings are (and bankruptcy administrators can be) supervised and controlled by a creditors' committee. Almost all formal decisions taken by bankruptcy administrators, liquidators and creditors' committees can be challenged in court by dissatisfied parties. An elaborate statutory system of legal remedies exists. There are always two and often three levels of court review to cure procedural deficiencies and preserve and enforce the substantive rights of creditors and debtors alike.

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Firm profile

Hartmann Müller Partners was established in 1983. It provides a full range of legal services, with an emphasis on business and corporate law, and conducts work in German, English and French. The firm boasts advanced office automation systems, with access to national and international databases in the legal and economic fields. It benefits from an extensive network of correspondent national and international law firms.

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