Europe

BAKER & MCKENZIE

European Legal Developments Bulletin

Summer 2009 **Volume 21 No. 2**

Courts crack down on preferential treatment of creditors

In four recently published landmark decisions, the Federal Supreme Court set out the limits to be observed when payments are made by a financially distressed debtor to its creditors. ***Florian Bommer*** reports.

According to articles 286 - 288 of the Swiss Debt Enforcement and Bankruptcy Law (SchKG), several types of transactions conducted during a prescribed period of time before the opening of bankruptcy proceedings or the grant of a moratorium can be challenged by the bankruptcy administration.

In particular, article 286 states that gifts and transactions accepted by the company by way of contractual consideration, but which are out of proportion to its own performance, are voidable if such gifts or transactions are made during the year before the opening of bankruptcy proceedings or the grant of a moratorium.

Furthermore, article 288 declares all transactions voidable in the five years prior to the opening of bankruptcy proceedings or the granting of a moratorium if these transactions were carried out with the intention, apparent to the other party, of disadvantaging its creditors or favouring certain creditors to the disadvantage of others.

The first case decided by the Federal Supreme Court was based on a lawsuit filed by the administrator of the Swissair estate against the Zürcher Kantonalbank. Swissair had paid back a loan to the Zürcher Kantonalbank in several tranches, with the last payment being paid to the Zürcher Kantonalbank only a few days before the grant of the moratorium in favour of Swissair. The Federal Supreme Court held that these payments were made to the detriment of Swissair's other creditors and that the favourable treatment was foreseeable by both Swissair and Zürcher Kantonalbank.

The court held that a repayment would have been permitted only if the loan had qualified as a restructuring loan. A loan is a restructuring loan if it is given to a financially distressed debtor with a justified assumption that the financial recovery of the debtor is not only possible but also probable. In this case, however, the payments by Swissair were not made on the basis of a restructuring loan. Consequently, the Federal Supreme Court decided that the payments could be challenged and that the Zürcher Kantonalbank had to pay back the amount of the loan to the Swissair estate.

The second case also concerned the Swissair estate. Only a few days before the grant of the moratorium, Swissair paid invoices for kerosene delivered by Total. Again, the Federal Supreme Court held that the payments made were detrimental to the other creditors of Swissair and that this fact was apparent to both Swissair and Total at the time Swissair made the payments. The Federal Supreme Court held that Total was not able to demonstrate that the payment of these invoices for kerosene deliveries were necessary in order to maintain the aviation business of Swissair which would have been beneficial for all of the creditors of Swissair. As a result, the Federal Supreme Court declared the payments made to Total contestable and ordered Total to repay the sums received to the Swissair estate.

The Swissair bankruptcy was also the background of the third case decided by the Federal Supreme Court. Only a few days before the moratorium had been granted, Swissair paid fees for air traffic control services at the Zurich Airport. The administrator successfully challenged these payments. The Federal Supreme Court was of the opinion that, given the well-known financial distress of Swissair, it was foreseeable that, by making these payments, Swissair treated Zurich Airport preferentially to the detriment of the other creditors. The Court also rejected Zurich Airport's argument that these

payments were necessary in order to maintain Swissair's aviation business as they were made for services rendered in the past and not for securing services to be rendered in the future.

The fourth case was based on payments made to pricewaterhouseCoopers (PWC) for auditing and advisory services associated with a corporate restructuring. The company made these payments to PWC shortly before the granting of the moratorium. The bankruptcy administrator was not successful in challenging these payments. The Federal Supreme Court held that the administrator was prohibited from challenging the payments made to PWC in their capacity as auditors because PWC accomplished a legal task by providing auditing services and because the services associated with a corporate restructuring would have been beneficial to all of the creditors had they been successful.

The strict position of the Federal Supreme Court in these cases shows that it has chosen a strict approach as to payments made to selected creditors by a financially distressed debtor in a pre-bankruptcy situation. As the avoidance actions are largely based on subjective factors, there is a considerable amount of uncertainty as to which payments and transactions are admissible in pre-bankruptcy situations. This is also demonstrated by the fact that in all three Swissair cases, the lower court decided differently, i.e., rejected the law suits filed by the administrator of the Swissair estate.

Among the lessons to be learned from the creditor's perspective is that when a third party delivers goods or provides services to a financially distressed company, it should insist on a prepayment or - when goods are delivered - on a strict delivery-versus-payment basis. Prepayments for future services (as opposed to services already rendered) cannot be challenged; the same is true for payments which are made at the same time as the delivery of the goods occurred.

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Economic slump forces changes to short time working

Marc Pascal Fischer examines the changes to the Swiss short time working regime, and how they will affect employers and employees.

Due to the recent deterioration of the economic situation short-time working in Switzerland has experienced a strong increase, as the most recent figures of the State Secretariat for Economic Affairs (SECO) prove. Almost all sectors are affected by short-time working: for instance, the hotel business, chemical industry and automotive industry have all introduced short-time working.

The Federal Council of Switzerland has amended the legal framework with regard to short-time allowance in two respects: the duration of short-time allowance and the cooling off period.

Short-time working is the temporary reduction or complete discontinuation of work in a company with the contractual relationships between employer and employee remaining in force. The purpose is to contain a temporary decline in orders as well as to preserve jobs. Therefore, short-time working constitutes a real alternative to dismissals, company shutdowns and associated unemployment.

The employer consequently is able to save costs of personnel fluctuations, such as the costs associated with new hire orientation or loss of internal know-how, while