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Family allowances

The current legislation in certain Swiss cantons on family allowances distinguishes between children living abroad and children living in Switzerland. This distinction is no longer permissible under the Agreement.

Changes in pension plan insurance (BVG)

The Agreement is only applicable to the mandatory part of the Swiss pension plan insurance (pillar 2a, "Säule 2a"). The Agreement does not affect the calculation of benefits, the funding of pension plans, the investment of their funds or the organisation of the pension plans.

Currently a person who permanently leaves Switzerland or becomes self employed may request a cash payment of his or her termination benefits under the pension plan. However, under the Agreement, such payment will no longer be possible if (1) the person is leaving Switzerland to an Agreement state or is exercising a self-employed activity in an Agreement state, and (2) in that Agreement state, is subject to a mandatory insurance for pension benefits. Instead, the termination benefits will need to be transferred to a vested benefit account or a vested benefit policy. The application of the Agreement is subject to a five-year transitional period. Therefore, the cash payment of termination benefits is possible until 31 May 2007. After the lapse of this transitional period, for the non-mandatory part of the pension plan insurance, and, generally if an insured is leaving Switzerland to a country other than an Agreement state, a cash payment is still possible.

The call for action for employers

Based on the conflict of law rules summarised above, employees working in different Agreement states are subject to social security insurance in one Agreement state which may not be the employer state. Therefore, the employer should carefully check the social security legislation applicable to its employees. As a result, employers may have to deduct social security contributions from their employees' gross salaries and transfer such contributions to social security authorities of another Agreement state according to the social security legislation of that Agreement state.

Employers entering into agreements with employees working in Agreement states where the employer has no place of business may agree with the employee that the employee pays the applicable social security contributions. However, the employer must notify the competent social security authorities about such an agreement. Additionally, the employer must take the appropriate security measures to ensure that the employee effectively pays the social security contributions as the employer is (according to the legislation and jurisprudence of most Agreement states) jointly and severally liable for the payment of social security contributions, even if an agreement is in place and notified to the competent social security authorities.

Finally, the employer should ensure that the pension plan regulations with regard to cash payments of termination benefits are amended before the lapse of the transitional period.

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Legal problems with rescue companies

When a rescue company takes over the viable parts of a financially distressed commercial organisation, there are various legal pitfalls to avoid.

Even if a company is in a financially distressed position so that it cannot be reorganised as a whole, it may well be that some parts of its business are viable on a standalone basis. In most cases, a liquidation in the context of bankruptcy proceedings will destroy its value. The transfer of such business to a rescue company may, therefore, be in the interest of the creditors. Moreover, by transferring the business to a rescue company, the jobs of the employees concerned can be saved. Many legal problems arise, however, when setting up a rescue company that subsequently takes over parts of the business of a financially distressed commercial organisation. In this article, we look at the most important issues to be dealt with in such cases.

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Preferential treatment of creditors

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 confirmation of a moratorium can be challenged by the bankruptcy administration. In particular, article 286 SchKG 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 confirmation of a moratorium (Bewilligung der Nachlassstundung). Furthermore, article 288 SchKG declares voidable all transactions in the five years prior to the opening of bankruptcy proceedings or the confirmation of a moratorium if these transactions were carried out with the intention, apparent to the other party, of disadvantaging its creditors or of favouring certain creditors to the disadvantage of others.

If the business is sold to a rescue company owned by a third party, the purchase price must not be below a fair market price. It may be difficult for the selling company to demonstrate that the price received was fair and adequate. In order to minimise the risk of a possible challenge, it is, therefore, important to receive several competing offers or at least to have an expert's opinion on the market price of the transferred business. These problems can be prevented if the business is transferred to a subsidiary of the financially distressed company. In such a case, their creditors are not deprived of the transferred assets as they still belong – at least indirectly – to the mother company. From a practical point of view, however, experience has shown that it is difficult to finance the business of a subsidiary of a financially distressed company.

Another possibility is to sell the business only after the initiation of a bankruptcy or composition procedure. However, a sale in the context of bankruptcy proceedings is normally not a realistic alternative as, in most cases, the opening of bankruptcy proceedings effectively destroys the value of the business to be transferred. The sale in the context of a *composition procedure,* on the other hand, can be an alternative if the transaction is conducted swiftly after the judge has granted a composition moratorium.

When transferring the business to the rescue company, any transfer of liabilities must be avoided. Otherwise, the creditors transferred to the rescue company will be treated preferentially and to the detriment of the creditors remaining with the financially distressed company.

Liability of directors and managers

According to article 754 of the Swiss Code of Obligations (CO), the members of the board of directors and all persons engaged in the management are liable to the company, to every shareholder and to the company's creditors for the damage caused by an intentional or negligent violation of their duties. Even though the defendant in the above-mentioned avoidance actions would be the third party receiving such voidable performance from the company, the Federal Supreme Court has held that the voidable transaction also constitutes a breach of obligations by the members of the board of directors (Decision 5C.29/2000). Moreover, the sale of assets below market price and the preferential treatment of creditors can, under certain circumstances, constitute a criminal offence under articles 164 and 167 of the Swiss Penal Code (StGB). Consequently, avoidance actions are not only a risk for the rescue company purchasing the business from a financially distressed company but also for the board of directors of the selling company, who face the possibility of civil as well as criminal liability.

Transfer of employees

If the employer transfers a business (or a part of it) to a third party, the employment relationship is transferred to the acquiring party including all rights and obligations as from the date of transfer unless the employees decline to transfer. The previous employer and the acquiring party are jointly and severally liable for all employees' claims that have become due prior to the transfer (article 333 CO). Such transfer of the employees is mandatory under Swiss law and the provision cannot be waived by the previous employer and the acquiring party. There are two major drawbacks to the current legal situation:

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- The rescue company must take over all employees of the business under the terms agreed with the transferring company. Any redundancies or adjustment of the terms of the employment relationships can only be made by respecting the original notice period. This means that all salaries earned during such notice period must be paid by the rescue company.
- The rescue company is liable for all salaries including social security payments that are not being paid by the previous employer. In workout situations, it is often unclear whether the company in financial distress has fulfilled its obligations under the employment relationships. Such a situation exposes the rescue company to incalculable and, hence, often unbearable risks.

A possible solution is that a portion of the purchase price is put in escrow to be released only when it is clear that all obligations under the employment agreements have been fulfilled by the previous employer.

There is a lively debate among Swiss jurists as to the scope of application of article 333 CO. While it is undisputed that article 333 will apply if the transfer of the business is conducted *before* the opening of bankruptcy proceedings or the confirmation of a moratorium, there is a controversy as to the applicability of article 333 if the transfer occurs after such date. In the case of bankruptcy proceedings, however, the predominant legal doctrine is in favour of a non-application of article 333 CO.

With regard to the composition procedure (Nachlassverfahren), views are divided. According to a recent opinion given by the Swiss Federal Department of Justice in the *Swissair* case, article 333 CO will not apply in the case of a composition procedure. It should be noted, however, that this opinion of the Swiss Federal Department of Justice is not binding on the courts. Therefore some uncertainty remains with regard to the application of article 333 CO in the context of a composition procedure as the Federal Supreme Court has not yet ruled on the issue.

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Pension plans with deficits

Directors of a pension plan that is in deficit have certain fiduciary duties. If they violate these obligations, then they – or, in certain circumstances, the employer – may be held liable for the shortfall.

Due to the unfavourable development of the security markets, many pension plans have suffered losses that have led to deficits because their assets no longer cover the accrued liabilities for future pension payments. When this occurs, the pension plan's board of directors has to take appropriate measures to remedy the deficit. Furthermore, the employer must ensure that its representatives on the board of directors fully comply with all legal and regulatory obligations to avoid facing liability for the deficit. This article discusses these issues.

Pension plans in Switzerland

In Switzerland, each employee whose salary surpasses a certain minimum must be covered by a pension plan [Pensionskasse/2. Säule]. Typically, such a pension plan requires the employee to contribute a percentage of his or her salary to the pension plan and the employer to match (at the very least) the employee's contribution.

Most small and mid-size companies do not run their own pension schemes. They have outsourced these functions to an insurance company that guarantees the payments of future pensions on the basis of current contributions. Many large companies, however, do run their own pension plans, which are structured as foundations that are legally independent from the employer. The foundations receive the contributions of the employers and the employees,