

Company & Commercial - Switzerland

Voters say yes to 'fat cat' initiative

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Introduction

On March 3 2013 Switzerland voted in favour of an initiative against excessive salaries for board members and executives - the 'fat cat' or Minder initiative - with an overall majority of 68% and approval by voters in all 26 cantons and half-cantons.

Article 95(3) was added to the Federal Constitution, pursuant to which Switzerland must, within one year, enact new transparency rules and one of Europe's most rigid regimes on a full and binding say on the pay of board members and executives. The new article of the Constitution applies solely to Swiss public companies (ie, companies incorporated in Switzerland and listed either in Switzerland or on a foreign stock exchange). Swiss companies which are not listed and all foreign companies fall outside the scope of Article 95(3). In addition, voting by pension fund representatives for shares in Swiss listed companies held by pension funds will be addressed.

Key implications

On the enactment of Article 95(3), the following will become mandatory:

- Shareholders of Swiss listed companies must vote annually on aggregate compensation for the board, advisory board and executive management. Their vote will be binding. To enable shareholders to vote, the listed company must submit a special compensation report.
- It is uncertain what will happen if shareholders do not approve the aggregate compensation suggested. Some authors and practitioners argue that both the listed company and the board members or executives will get an extraordinary termination right in such case for the individual work or service contracts binding them.
- Severance or other compensation payments (golden parachutes), pre-payments (golden handshakes), bonuses for acquisitions or divestitures and additional employment or consulting agreements are now prohibited. However, the absolute amounts of board or executive pay will (unlike for bankers in the European Union) neither be set nor limited by the coming legislation.
- All members of the board and compensation committee of the listed company, as well as the independent shareholder proxy, must be elected and re-elected annually by the shareholders annual general meeting (AGM).
- Listed companies must offer their shareholders the opportunity for distance electronic voting without the need of being physically present at the AGM.
- Company representatives or depository institutions (eg, banks) are no longer authorised to vote by proxy for the shares in other listed companies held by them. Instead, such companies or bank clients must authorise third parties or the independent shareholder proxy to vote for their shares if they wish to participate.
- Additional employment or consulting agreements of board members and executive officers with any group companies of a Swiss listed company are prohibited. It is not possible to delegate the management of a Swiss listed company to another legal entity.
- Various listed company rules regarding bonus and incentive schemes, as well as the pension rights of board directors and executive board members, third-party mandates and the employment agreements of executive board members, must be incorporated in the articles of incorporation in order to be valid.
- Pension fund representatives must vote in the interest of their pension fund holders

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and make their voting transparent.

- Violations of the rules are punished under criminal law with imprisonment of up to three years and a monetary penalty of up to six years of annual compensation. However, Article 95(3) does not clarify who should be punished for a breach of this article - whether board members only, or executive officers and even pension fund representatives, may become subject to penal prosecution is unclear.

Implementation and transitional rules

Article 95(3) is not directly applicable. Instead, within one year (ie, by March 3 2014 at the latest) the Federal Council must adopt an interim ordinance to give direct effect to Article 95(3). Parliament will then debate and adopt a bill for the corresponding amendments of ordinary Swiss legislation with a view to replacing the governmental interim ordinance. According to the Federal Department of Justice, which is drafting the ordinance for the government, the transitional rules will be as follows:

- All parts which the addressed Swiss companies can apply without prior changes to the articles of incorporation shall become effective on January 1 2014 - 2013 AGMs (which take place in early 2014) must already adhere to them.
- All other parts will come into force on January 1 2015, with a view to enable the addressed Swiss listed companies to adapt their articles of incorporation accordingly before the 2014 AGM (in early 2015).

Comment

Swiss listed companies are advised to be proactive in order to gather first-hand experience before the transitional ordinance is adopted. A consultative voting on the annual compensation report at the forthcoming 2013 AGM will allow Swiss listed companies to learn about the possible concerns of major shareholders, institutional investors and pension funds.

In addition, distance electronic voting, annual elections and re-elections of board members and members of the compensation committee can already be practised (unless the existing articles of incorporation of a Swiss listed company explicitly disallow this). The existing compensation and corporate governance policies and practices, existing contractual agreements with the board of directors and executive board members can be reviewed, and existing and new board and executive appointments can be carefully managed (eg, by suitable contractual reservations as to payment adaptations).

On adoption of the interim ordinance (set to become effective on January 1 2014), listed companies must amend their articles of incorporation for the 2014 AGM to adapt to the new rules (with which they must comply fully from January 1 2015).

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