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Persönliche Haftung nach Schweizer Aktienrecht

Risiken und ihre Minimierung

Personal Liability under Swiss Corporate Law

Associated risks and their avoidance

Schulthess §

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Preface

Due to well-publicised liability suits against board members and auditors, large sections of the public have, over the course of the last twenty years, become aware that accepting a corporate mandate can entail considerable risks. Even less well-known cases, often settled out of court, confirm that in Switzerland as compared to other countries the law of personal responsibility is very severe. A person who accepts a mandate to act as a board member or auditor nowadays often has, or should have, the unpleasant feeling of sitting on a keg of gunpowder without knowing whether the fuse has already been lit. In addition, there are numerous uncertainties as to the conditions of personal liability, even since the revision of corporate law in 1992.

The purpose of this book is to attempt to clarify the situation by presenting an overview of the law as it stands and as it is reflected by court practice by pointing out the potential risks to those who hold corporate office and by illustrating those risks with examples taken from the practice of the courts. We shall also make a number of suggestions for minimising such risks. We have tried to make the text easy to read and use, and for this reason we have refrained from theoretical ramifications and footnotes. We have, however, included a number of references to judgments of the Swiss Federal Tribunal.

In 1994 Peter Forstmoser, Markus A. Frey, Thomas Sprecher and Andreas C. Limburg published a book entitled *Persönliche Haftungsrisiken nach neuem Aktienrecht* («Personal liability risks under the new corporate law»). This book was based on numerous contributions on corporate liability by Peter Forstmoser. Further developments in legal theory and court practice along with new statutes such as the recent Merger Act necessitated a completely revised new edition.

This book too, though edited by all three authors working in close cooperation, draws heavily on Peter Forstmoser's work ranging back over three decades. With the help of a number of our colleagues in the law firm of Niederer Kraft & Frey who contributed useful comments, the text has been reviewed and brought up to date and new chapters have been added. In addition, for the first time, it is now completely bilingual German–English. The English version is based on British parlance.

The authors would like to thank Dr. Ernst Felix Schmid for reviewing the section on procedure and Daniela Schmucki-Fricker for reviewing the part on tax law. Marcel Fischer, a D&O underwriter with Swiss Re, provided valuable information on the insurability of corporate liability risk and in particular on D&O insurance. We would also like to thank Prof. Dr. Stephen V. Berti for translating the German text, Renée Zaytsev for editing the English version and the Swiss-American Chamber of Commerce for their permission to print a special annex (see p. 233 et seq.) with their translations of the relevant provisions, in order to also provide for American English translations thereof. Finally, many thanks to Cornelia Rupp for efficiently typing the text.

The law is stated as we understand it as of 1st September 2005.

Peter Forstmoser *Thomas Sprecher* *Gian Andri Töndury*

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Bibliography

Works on corporate liability under Swiss law are far too numerous to list here.

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RAVELLO Robertino Lei: La résponsabilité solidaire des organes de la société anonyme (Lausanne 1992)

Cases

In light of our prospective readership we shall confine ourselves to citing a few judgments of the Swiss Federal Tribunal (BGE). The text is, however, entirely based on court decisions, both reported and unreported, and reflects, where not otherwise stated, the position of the Swiss Federal Tribunal.

Statutory texts and abbreviations

The most important statutory provisions are reproduced in full in boxes at the appropriate point.

The following Federal Acts (cited «BG» for «Bundesgesetze») are cited according to their usual *German abbreviations:*

AFG	BG vom 18. März 1994 über die Anlagefonds (Investment Funds Act)
AHVG	BG vom 20. Dezember 1946 über die Alters- und Hinterlassenenversicherung (Old Age Pensions Act)
AVIG	BG vom 25. Juni 1982 über die obligatorische Arbeitslosenversicherung und die Insolvenzentschädigung (Unemployment Insurance Act)
BankG	BG vom 8. November 1934 über die Banken und Sparkassen (Banking Act)
BEHG	BG vom 24. März 1995 über die Börsen und den Effektenhandel (Stock Exchange Act)
BVG	BG vom 25. Juni 1982 über die berufliche Alters-, Hinterlassenen- und Invalidenvorsorge (Professional Pensions Act)
DBG	BG vom 14. Dezember 1990 über die direkte Bundessteuer (Direct Federal Tax Act)
FusG	BG vom 3. Oktober 2003 über Fusion, Spaltung, Umwandlung und Vermögensübertragung (Merger Act)
GestG	BG vom 24. März 2000 über den Gerichtsstand in Zivilsachen (Forum in Civil Matters Act)
IPRG	BG vom 18. Dezember 1987 über das Internationale Privatrecht (Private International Law Act)
LugÜ	Übereinkommen vom 16. September 1988 über die gerichtliche Zuständigkeit und die Vollstreckung gerichtlicher Entscheidungen in Zivil- und Handelssachen (Lugano Convention)
OR	BG vom 30. März 1911 betreffend die Ergänzung des Schweizerischen Zivilgesetzbuches, 5. Teil (Swiss Code of Obligations)
SchKG	BG vom 11. April 1889 betreffend Schuldbetreibung und Konkurs (Debt Collection and Bankruptcy Act)
StGB	Schweizerisches Strafgesetzbuch vom 21. Dezember 1937 (Penal Code)
VStrR	BG vom 22. März 1974 über das Verwaltungsstrafrecht (Penal Sanctions in Administrative Law Act)
ZGB	Schweizerisches Zivilgesetzbuch vom 10. Dezember 1907 (Swiss Civil Code)

Decisions of the Swiss Federal Tribunal are cited using their *German abbreviation* «BGE» (Bundesgerichtsentscheid). References in the text are to the numbered paragraphs.

I. Introduction

Personal corporate liability is primarily governed by articles 752–760 of the Swiss Code of Obligations (OR). These provisions apply to persons involved in *administration, management,* and *liquidation* (N 8 et seq.), *auditing* (N 35 et seq.), *incorporation* (N 43 et seq.) and the *issue of prospectuses* (N 49 et seq.). The categories of persons liable under these norms is widened by article 39 of the *Banking Act* (BankG) to include those involved in a bank which is organised as a corporation (BankG 39, Rz. 54), and by article 108 of the *Merger Act* (FusG) for mergers, demergers, conversions and transfers of assets and liabilities (N 52). The concept of corporate law as used hereinafter also includes the relevant liability norms contained in other acts such as the Banking Act and the Merger Act. We shall separately point out special characteristics of banks organised as corporations (N 54 et seq.) as well as liability under rules other than corporate law rules (N 58 et seq.). 1

In accordance with the general principles of tort law, the necessary conditions for liability are that *damage* must have been suffered (N 72 et seq.); that the persons responsible *violated*, in the exercise of their function, *a duty of care* (N 90 et seq.); that such persons were also at *fault* (N 133); and that an *adequate causal lien*, defined as a foreseeable connection between cause and effect, exists between the damage caused and the violation of the duty of care (N 154 et seq.). In addition, the claim cannot be *extinguished* or *unactionable* (N 164 et seq.). 2

Damages may be claimed by a *company* itself, its *shareholders* and *participants* as well as its *creditors*, in the latter case however only once the company has been declared bankrupt (N 209 et seq.). 3

The above-mentioned liability norms apply to all stock corporations (in this book usually referred to as companies) organised under *Swiss law*. In an international context special norms apply (N 307 et seq.). 4

The norms governing corporate liability are *mandatory*. Unlike some foreign laws, Swiss law does not permit liability to be waived or limited in a company's articles of association. 5

II. Who is subject to the rules of corporate law liability?

The following persons are subject to the rules of corporate law liability: 6

- Persons involved in *administration, management and liquidation* (see below *sub* 1, N 8 et seq.);
- Persons involved in *auditing* pursuant to corporate law (see below *sub* 2, N 35 et seq.);
- Persons involved in *incorporation* (see below *sub* 3, N 43 et seq.);
- Persons involved in the issuing of a *prospectus* (see below *sub* 4, N 9 et seq.);
- Persons involved in *restructuring* (see below *sub* 5, N 52 et seq.);
- *Auditors* pursuant to the Banking Act and *special mandataries* appointed by the Banking Commission such as persons responsible for investigations, restructuring, liquidation and special audits (see below *sub* 6, N 54 et seq.).

Corporate law liability may be incurred by both individuals and legal entities. Thus, for example, it is the legal entity appointed as auditor and not the individuals who act in its name which is liable *qua* auditor. However, as a corporate organ a board of directors as a whole cannot be held responsible; instead, each individual member is separately liable as, in principle, only individuals can be members of administration and management organs (but cf. also N 11). 7

1. Persons involved in administration, management and liquidation

a) In practice the most important liability norm, together with that concerning auditors' liability (cf. N 35 et seq.), is found in OR 754 I concerning organ liability. 8

OR 754 I	The members of the board of directors and all persons involved in management or liquidation are liable to the company, to the individual shareholders and to the company's creditors for damage caused by the intentional or negligent violation of their duties.

9 This provision applies not only to members of a board of directors but also to all other persons «involved» in management.

10 Thus, it is not only the *members of a board* and *further organs in a formal sense*, such as members of the management, that are liable under this norm but also all persons *who* de facto *perform a management function* (for a description of the tasks in question see N 16 et seq.), irrespective of whether they have been formally appointed to do so or simply perform the function *de facto.* In this connection a distinction is made between *material* and *de facto organs* (BGE 128 III 92, BGE 117 II 442).

11 Therefore, a *controlling* or *sole shareholder* may incur liability by not confining himself to exercising his rights as a shareholder, such as by interfering with a company's management or by giving instructions to the management. This applies in particular to the *parent company of a group of companies* which fails to confine itself to its role of shareholder, but – and this tends to be the rule rather than the exception – which actively interferes in the management and makes, at the very least, strategic and fundamental tactical decisions. (It is has been denied that the parent company can incur liability as a material organ. This contradicts the principle that only individuals can be administrative and managing organs [cf. N 7]. In any event, if one denies that the parent company is an organ, then those persons acting for it can be deemed to be [material] organs of the subsidiary, and this leads to the same result since their acts can be imputed to the parent company [cf. N 294 et seq.].)

12 An organ function which may incur liability may be found where an *impression of organ competence* is created and is thus perceived as such by outsiders by a person acting towards third parties as if he were an organ or declaring that he is an organ, for example a «sleeping» or undisclosed member of the board (cf. also N 25 for a so-called organ function through *declaration*).

13 b) In particular:

14 aa) Organs according to the meaning of the norms governing corporate law liability are *all members of a board of directors,* irrespective of which tasks they actually perform. It is the formal organ function entered in the Register of Commerce which is decisive. Thus, a so-called

«proforma» board member who accepted office purely as a favour, from whom no contribution is expected and who might not even receive any remuneration, is nevertheless fully subject to the norms governing corporate law liability. His actions and omissions are judged in the same manner as those of a member who fulfils his duties actively and diligently. This applies in all events to *liability to creditors*, which is by far the most important aspect in practice. Against a controlling or sole shareholder the *proforma*-member can plead that neither any activity at all nor the following of specific instructions was expected of him.

We believe that *officers as well as members of management and group management* provided they are registered in the Register of Commerce, should also be organs in the formal sense. Failure to qualify them as such will, however, hardly ever be of practical consequence; since they are involved in management they would be considered material organs (cf. N 16 et seq.) or, because third parties may assume that the title of director or member of management reflects organ competence, they would be considered organs through declaration (cf. N 25). 15

bb) All persons who in actuality make *decisions reserved by statute to organs in the formal sense* are also treated either *materially, functionally* or *de facto* as organs, and are therefore also liable under corporate law (BGE 117 II 572 et seq.). These include persons who manage the company and, accordingly, play a decisive role in forming its will. Since the practice of the Federal Tribunal is not uniform it is difficult to predict who it will consider a material organ. 16

We are of the opinion that the concept of an organ should be a restrictive one and that specific corporate law liability should only apply to the *highest management* of a company. This does not mean that other persons who influence the course of business on a lower level or acting as consultants cannot be held accountable for the non-fulfilment of their duties. Rather, in such instances other legal norms apply, for example: 17

- From *employee* to *employer*, there is a general duty of care pursuant to OR 321a I. 18

OR 321a I	The employee must carry out the work assigned to it diligently and respect in good faith the legitimate interests of its employer.

19 – This norm also applies to *mandataries* towards their *principal* by virtue of OR 398 I and II, which refer to OR 321a I.

OR 398 I, II	The mandatary is generally bound by the same duty of care as the employee owes its employer. It is liable to its principal for a proper and diligent execution of its task.

20 The Federal Tribunal has even gone one step further and also subjected persons who carry out transactions or make decisions which are part of the routine of everyday business to the norms of corporate law liability. Thus, the Tribunal held that *the holder of a procuration* of a small bank who had signed a balance sheet along with a delegate of the board of directors had acted as an organ and was, accordingly, liable under corporate law (BGE 117 II 441 et seq.). Authors have strongly criticised this decision and in our opinion rightly so. A more convincing ruling was the line drawn in a judgment rendered more or less at the same time where it was held that organs consist of only those persons who belong to the highest managerial level of a company (BGE 117 II 573).

21 cc) As opposed to organs in the formal sense which can, in principle, be held liable for all events concerning a company (but see N 97 et seq. as to the possibilities of restricting liability by virtue of delegation), it is our understanding that the liability of persons with a material organ function extends only to such functions or areas where they have *actually acted* and exercised influence. Within such functions or fields their liability is not confined to individual acts or omissions. Someone who is de facto, though perhaps not formally, responsible for ensuring that a company has liquidity cannot escape liability by claiming not to have been involved in a specific case.

22 dd) Organs in a *material* sense may, as already mentioned (supra N 11), be comprised not only of persons working in the company but also of *persons extraneous to the company's organisation*, in particular shareholders with large holdings or a parent company which exercises effective influence on the conduct of business.

23 Persons *lower in the company hierarchy* but having, de facto, the competence to make decisions – such as long-standing employees in a family concern who actually hold the fate of the company in their hands, may also be qualified as organs in a material sense. However, such in-

fluence must be the result of an *organ type of position*. Thus, an *assistant* who influences a decision by the persuasive force of his arguments is not an organ as long as somebody else has the last word, even though the latter might be influenced by the assistant's arguments and expertise.

The same applies to an *advisor* who generally is not an organ even if the formally competent organs take his advice uncritically and at face value. The situation is only different if the advisor exceeds his mandate and *participates actively in decisions*. In our opinion, the Federal Tribunal went too far in qualifying an advisor as an organ because he had exercised influence «through particularly intensive advice, coaching and supervision of the formal organs» (quoting the court below to BGE 107 II 349 et seq.). Rather, what is necessary is *participation in decisions* in a typical organ form, particularly through participation in votes (cf. BGE 128 III 92). 24

ee) Lastly, an opinion that has been adopted by the Federal Tribunal demonstrates that an organ function may be assumed when third parties can, in good faith, infer such a position from the circumstances, that is *where appearances create the impression that the person in question has an organ function* (BGE 117 II 572 et seq.). Thus, an advisor who had boasted to third parties that he was a «sleeping» or undisclosed member of the board of directors was held to be liable under corporate law. 25

c) Persons participating in shareholders' meetings are not organs, which is why *shareholders* who confine themselves to the exercise of their shareholders' rights without assuming a formal or material organ function *are not subject to corporate liability rules.* 26

d) The *courts* have held that the following persons may be liable under corporate law: 27

- *Members of a board of directors* who as formal organs are in all events subject to OR 754 et seq., including fiduciary board members who are responsible, like all other members, for their acts and omissions;
- *Officers and members of management or group management* who are qualified as formal organs provided that they are registered in the Register of Commerce, and in any event, as material organs due to their powers or as organs through declaration due to their title, for example «officer», «member of the management» or «member of the group management» which convey to third parties the impression that they have an organ function;

- Persons who act in the background (so-called eminences grises);
- The *principal shareholder* if he interferes in the management and thus assumes a material organ function, but not if he merely confines himself to exercising his rights as a shareholder, such as appointing the organs and exercising influence on the aims, organisation and financing of the company solely pursuant to the articles of association;
- *Clandestine or sleeping members of a board* of directors, that is members who are not registered in the Register of Commerce but who are de facto organs or hold themselves out as such to third parties;
- The *parent company and its representatives* to the extent that they directly influence the management of the affiliate company, but not when they confine themselves to exercising their rights as shareholders. To this extent responsibility within a group of companies is restricted in the same way as in the case of interference by the principal shareholder;
- *Legal entities* who as shareholders appoint a member of the board of directors, but only to the extent that they give such member instructions and thus influence the management;
- *Procurists, mandataries and other employees* to the extent that they *take independent, important decisions concerning the management of the company.* It should, however, be emphasised that neither signing authority nor registration in the Register of Commerce as such lead to an organ function; the latter must be materially exercised, though the Federal Tribunal does not always strictly follow this restriction;
- *Liquidators;*
- A *receiver* appointed when the opening of bankruptcy proceedings has been deferred.

28 e) *Organ function for formal organs* with its inherent liability risk generally begins at the time of appointment to a board of directors when the individual was active prior to entry in the Register of Commerce, and otherwise at the time of registration. For *material organs, organ function generally commences* when interference begins and for *organs through declaration, organ function begins* when the declaration is made.

29 Organ function, with its inherent risk of liability, generally lasts as long as the organ is in a position to influence a company's business.

30 f) There is a dispute as to exactly *when* a *formal* organ function ceases. We suggest that a distinction be drawn: responsibility for and liability to a *company* ends with resignation or removal, as it also does towards shareholders who are aware, or should be aware, of the termination of

the organ function. If the function was terminated by a shareholders' meeting, or notice of termination was addressed to a shareholders' meeting, then responsibility and liability towards all shareholders cease when the resolution is made or the shareholders' meeting receives the notice. On the other hand, liability may continue in principle towards third parties acting in good faith until the departing organ has been struck from the Register of Commerce. If the company does not attend to this, the persons concerned can do so instead (OR 711 II).

OR 711

> The company shall notify the Register of Commerce without delay of the removal or resignation of a member of the board of directors and request that the register be amended accordingly.
> If such notification is not made within 30 days, the person concerned can itself make the notification and request amendment of the Register.

The Federal Tribunal has held that in cases of a breach of obligations 31
under social insurance law, liability also ceases towards persons acting in good faith when the organ actually resigns from the board of directors and not only when he has been struck from the Register of Commerce (BGE 126 V 61).

g) *Resignation* from a board of directors is possible at all times without 32
a period of notice. Theoretically, resignation at an inopportune moment might be a breach of duty incurring obligation under OR 404 *per analogiam* which provides that the mandate can be terminated at any time but that untimely termination may incur liability (OR 404 II).

OR 404 II

> If [termination] is untimely, the terminating party is liable to the other for any damage caused.

To the best of our knowledge, liability due to untimely resignation has 33
never been alleged in a case and no court has ever held a person liable in this context. Therefore, an organ who no longer identifies with the way a company is managed is generally right to resign with immediate effect. It is, however, questionable whether resignation without having first attempted to address the difficulties which have arisen is appropriate, and resignation at the first sign of difficulties will certainly not enhance one's personal reputation. On the other hand, the rigid practice of the courts with regard to social insurance law makes it advisable to *resign too soon rather than too late* (cf. N 280 et seq.).

34 h) Where one's position as a member of a board of directors is governed by an *employment contract*, the contract may continue despite removal or resignation from the board. The former board member would no longer be liable as an organ unless his remaining function is also formally or materially that of an organ.

2. Persons involved in auditing (auditors' liability)

35 a) It is mandatory that every company have *auditors* whose primary task is to inspect the books and annual statements as to their conformity with the law and the articles of association. Auditors also have further statutory duties to inspect, report and notify (cf. OR 728–729c, 731a). Auditors are liable pursuant to principles similar to those applicable to persons involved in the administration, management and liquidation of a company.

OR 755

> All persons involved in the auditing of the annual and consolidated financial statements, the incorporation and increases or decreases of capital are liable not only to the company, but also to each shareholder and to the company's creditors for any damage caused by an intentional or negligent breach of their duties.

36 b) All *persons involved* in the auditing of a company are subject to the rules on auditors' liability. Thus, similar to liability for administration and management, *de facto* fulfilment of a task is conceivable and incurs liability. Consequently, the concept of *material organ function* also applies to auditors' liability (N 16), though it should be added that there has only been one court case to date in which the liability of a legal entity which acted as auditor without having been appointed to do so was discussed (and rejected) (BGE 119 II 255 et seq.). With regard to the beginning and end of personal liability see N 28 et seq.

37 c) Auditors are subject to the specific rules governing corporate liability as far as the *ordinary audit* is concerned, including the audit of the annual statement and, as the case may be, the consolidated statement. The same applies to their *extraordinary auditing activities* such as audits in the event of new incorporations, increases and decreases of capital, reports as a prerequisite of premature repayment of the liquidation result and *explanatory reports* for the attention of the board of directors.

By contrast, the rules on corporate liability do not, of course, apply to the fulfilment of *non-organ specific tasks*, for example estimating the value of a building. 38

d) If a *legal entity* is appointed as auditor it is subject to the rules of corporate liability, but this is not the case for the individual organs or their auxiliaries who actually carry out the audit. 39

e) *The future:* In its preparatory paper on the amendment of the Code of Obligations of 23 June 2004, the Federal Council proposed a revision of the law of auditors' liability, with uniform rules independent of the type of company but depending on the economic importance of the enterprise. While publicly-quoted and other economically significant companies remain mandatorily subject to a comprehensive audit, others are subject to less strenuous auditing requirements and OR 727a II of the draft even allows, in the case of small companies, a complete dispensation from audits if the shareholders agree thereto (see also N 125). 40

Draft OR 727a II	If all shareholders agree [...] the audit can be dispensed with provided the company employs not more than ten full-time employees per year.

It has also been proposed that in the future only the audit of the annual report be permitted to be waived. By contrast, extraordinary audits such as those for qualified incorporations or capital increases are still mandatory and auditors will remain liable for any breaches of duty in the execution of such audits. 41

In discussions of the revision proposals it was suggested that in the future auditors' liability no longer be governed by the Code of Obligations but by a separate statute. The aim of these proposals is to abrogate the parallel rules on the liability of executive organs, that is members of a board of directors and management, and auditors – a system which often has negative consequences for auditors (cf. N 319 below). 42

3. Persons involved in incorporation (founders' liability)

a) Founders' liability applies not only to all persons who *officially act as founders* but to everybody who plays a *decisive role* in the incorporation of a company, excluding, however, persons who only perform subordinate tasks. 43

OR 753

> Founders, members of the board of directors and all persons involved in the founding of the company are liable to the company, to the individual shareholders and the company's creditors for the damage caused if they:
> 1. intentionally or negligently incorrectly or misleadingly provide, withhold or disguise contributions in kind, acquisitions of assets or the granting of special benefits to shareholders or other recipients in the articles of association or a report on incorporation or on a capital increase or in the course of approving such measures in any other manner which is contrary to the law;
> 2. intentionally or negligently cause the company to be registered in the Register of Commerce based on a certificate or document which contains false particulars;
> 3. knowingly contribute to the acceptance of subscriptions from insolvent persons.

44 Those responsible include for instance:

- The *incorporating shareholders in a formal sense,* that is those who participated in the incorporation as shareholders, regardless of whether they participate economically in the company or merely act as fiduciaries so as to comply with the statutory requirement of having three founding shareholders (it is planned to abandon this requirement in the future so that, as in the EU, incorporation by a sole shareholder will be possible);
- Persons who act for a company in the process of being incorporated including, along with the official founding shareholders and future organs, *lawyers or fiduciaries* who prepare for the incorporation;
- Persons involved in the incorporation in a *fiduciary capacity* and their principals;
- The appointed *organs* and above all the future members of the board of directors;
- *Providers of capital* who knowingly grant the founders a short-term loan for the (simulated) subscription of the share capital;
- *Banks* as depositaries if they collude in a simulated subscription of the share capital;
- *Notaries public,* though it should be emphasised that they have only restricted duties and powers of inspection. It should also be noted that the extent of their liability is controversial;
- *The Commercial Registrar* who in addition is liable pursuant to OR 928 I, though in this case too the greatly restricted duties and powers of inspection should be emphasised. (We are not aware of any cases where a Commercial Registrar was held liable for defects in the incorporation of a company).

It is always a condition that those involved were *aware* or *should have been aware* that there were defects in the incorporation. 45

b) OR 753 is also applicable, despite its overly restrictive wording, to *capital increases.* 46

c) In addition to founders' liability pursuant to OR 753 which, like all liability under the rules concerning corporate responsibility, is liability for any damage caused by deliberate or negligent misconduct, persons who act in the name of a company at its incorporation stage are also *directly and personally liable for all liabilities incurred in the name of the company* and can only free themselves of such liability if the company takes over the liabilities once it has been incorporated. 47

OR 645

> Persons who have acted in the name of the company prior to registration in the Register of Commerce are personally and jointly and severally liable.
> Where commitments were incurred expressly in the name of the company which is in the process of being incorporated and are taken over by the company within three months of its registration in the Register of Commerce, the persons concerned are freed and it is exclusively the company which is liable.

Thus, where contracts are concluded for a company prior to incorporation, it is prudent to make such contracts under the condition that the incorporation is successfully completed and that the company ratifies the contracts once incorporated, unless the persons concerned control the company to be founded as is the case for one-shareholder companies or where the persons concerned are future members of the board of directors. 48

4. Persons involved in the issue of a prospectus (liability for a prospectus)

a) When a company turns to the public for a capital increase by offering bonds or other securities for public subscription, either at the incorporation stage or later, the Code of Obligations and the listing rules of the Swiss Stock Exchange (SWX) require that a *prospectus* be provided. OR 752 provides a specific statutory liability to protect the investors' trust in the information contained in such a prospectus. 49

OR 752	Where in connection with the incorporation of company or the issue of shares, bonds or other securities particulars were made or disseminated in a prospectus or similar notice which were incorrect, misleading or not in conformity with the statutory requirements, any person who intentionally or negligently contributed thereto is liable to the persons who acquired such securities for the damage caused.

50 The concept of «*similar notice*» in the sense of OR 752 is open to interpretation. A notice which is similar to a prospectus and which can therefore incur liability might also be found on a website, though the issue of the applicability of the rules on liability to a prospectus found on the internet or other new media is not yet fully settled. In our opinion, only «similar notices» which are intended to and capable of providing potential investors with information in connection with their purchase should fall under OR 752.

51 b) Such liability exists for all persons who «participate» in the drafting or dissemination of a prospectus or similar notice which includes, as already mentioned, all means of information and publicity capable of influencing an investment decision. The persons named in OR 752 therefore include:

- The formal founders;
- A company's *organs* and the organs appointed to a company which is in the process of being incorporated, in particular the board of directors and the auditors;
- *Persons who sign the prospectus* and similar notices;
- *Banks* and others who help to place the securities;
- *Advisors,* particularly lawyers;
- Notaries and depositaries (controversial);
- Any person who participates in the dissemination of information in connection with placing the new securities.

5. Persons involved in restructuring

52 Persons involved in restructuring are subject to statutory liability under the Merger Act. Such liability is similar to liability under corporate law, to which the Act partially refers.

FusG 108 I–III

> All persons involved in a merger, demerger, change of legal form or transfer of assets and liabilities are liable to the legal entities, their individual members and their creditors for any damage caused by the intentional or negligent breach of their duties. The responsibility of founders remains reserved.
> All persons involved in the audit of a merger, demerger or change of legal form are liable to the legal entities, their individual members and their creditors for any damage caused by the intentional or negligent breach of their duties.
> Articles 756, 759 and 760 of the Code of Obligations apply. In the case of a corporation or cooperative articles 757, 764 II, 827 and 920 of the Code of Obligations apply by analogy.

It should be added that according to the majority opinion, to which we also subscribe, the concept of «involved persons» does not include all persons who participate in the restructuring but *only those who have a prominent function*. This is in line with liability under the corporate law of officers and managers which only applies, or should only apply, to the highest level of company hierarchy (see N 17). It must also be a task pursuant to the Merger Act which is in question: Persons who perform audits in connection with a merger, in particular qualified auditing firms (see above all FusG 15, 40, 62, 81 and 92), are liable under Article 108 II of the Merger Act. By contrast, auditors who provide a so-called «fairness opinion» in connection with a merger do not exercise a typical organ function (see N 38), nor are they «auditors» according to the meaning of the Merger Act; they are, therefore, liable under the general rules of mandate and not under the rules governing corporate liability. 53

6. Special characteristics of banks organised as corporations

Under the law in force until 1992, there was no doubt that the norms governing liability under corporate law and banking law were identical. This situation changed with the reform of corporate law because Parliament neglected to adapt the provisions of the Banking Act to the revised provisions of corporate law, with the result that banks which are organised as corporations seem, at least in a formal sense, barred from invoking the new provisions. In the meantime, writers and courts have 54 been working on reducing the resulting differences by means of interpretation. Parliament has recently attempted to eliminate the remaining uncertainties by a revision of BankG 39 which came into force on 1 July 2004.

BankG 39	The liability of the founders of a bank and its managing, directing, supervising and controlling organs as well as for liquidators and auditors appointed by the bank is governed by the provisions of corporate law (Art. 752–760 of the Code of Obligations). The same applies to the following persons appointed by the Banking Commission: a. Special auditors, persons involved in restructuring and liquidators; b. auditors appointed to carry out a special audit.

55 In consequence, the statutory basis for liability claims against the organs of a bank is no longer found in the Banking Act but rather, due to the reference in BankG 39, in *corporate law*. The Banking Act does, however, still define the categories of *persons responsible*, and these have been widened by comparison with the former regime:

56 Since BankG 39 refers to the *rules of corporate law* with regard to all the persons it names, it is an innovation that special auditors, persons involved in restructuring, liquidators and other persons specially appointed by the Banking Commission are subject to corporate liability norms.

57 Writers have pointed out that the general reference to corporate liability norms leads to new problems. However, such problems should be surmountable by adjustments in conformity with the basic system.

7. Liability under corporate law rules for other types of companies

58 a) The corporate law provisions also apply to liability in connection with *banks* which are not organised as corporations (see the statutory text above in N 54).

59 b) Corporate law liability rules also apply to *Limited Liability Companies (GmbH), Credit Cooperatives and Concessioned Insurance Cooperatives*:

OR 827	The liability of persons who participated in the incorporation of the company, the managers, the auditors and the liquidators, is governed by the liability provisions of corporate law.

OR 920	Liability in connection with Credit Cooperations and to concessioned Insurance Cooperatives is governed by the liability provisions of corporate law.

c) As mentioned above (N 52), FusG 108 refers to corporate law provisions. Since FusG 1 applies to capital companies, partnerships, cooperatives, associations, foundations and individual businesses, corporate law provisions apply by reference to liability in relation to the restructuring of all these entities. 60

It is envisaged in the pending reform of the limited liability company that the reference to corporate law liability will be retained and that for «ordinary» cooperatives special rules will apply which are modelled on the corporate law provisions (OR 916–919). 61

8. Excursus I: Liability of special auditors

Special auditors mandated by a shareholders' resolution or court order to investigate specific matters are not subject to corporate law rules (cf. OR 697a–697g). Special auditors might, however, be liable to the company under the *law of mandate* (cf. OR 398 II: liability for proper and careful fulfilment of the mandate; see N 19). The question of liability to shareholders and creditors is not fully clear but as a rule there will probably be none. 62

9. Excursus II: Liability of external advisors

Apart from the persons liable under OR 754 there are also others who have, at least indirectly, an influence on administration and management, in particular external advisors who prepare decisions of organs without participating in the decision itself. 63

Such experts are, in principle, liable under the legal relationship existing between themselves and the company, which is usually a contract of mandate (cf. above N 19). Liability under corporate liability norms is 64 conceivable where an advisor does not confine himself to preparing a decision but also tries to influence it, thus becoming a *material organ* (cf. above N 16). A similar situation arises where the advisor creates the impression that he has an organ function, for instance by claiming to be a «sleeping» or undisclosed board member. This can lead to an *organ function through declaration* (cf. above N 25).

10. Excursus III: Liability of members of advisory boards

65 Liability for members of advisory boards is governed by the rules described in N 64: there is, in principle, (only) liability under the *law of mandate*, though liability can be contractually limited. Advisors who act as material organs will incur wider-reaching liability under corporate law norms. Divulging membership of an advisory board is *not tantamount to constituting an organ function through declaration,* since it is clear that advisory boards do not have the function of making decisions.

11. Excursus IV: Liability of assistants

66 Assistants are also not liable under corporate law even if they de facto have a large influence on the making of decisions. It is different if their influence is a result of an *organ type of position* and if for this reason they make decisions themselves, so that their influence is not confined to the persuasive force of their arguments. In this case they can become material organs (cf. N 23).

67 Assistants may also be liable under *labour law* (see above N 18).

III. Conditions of liability

Corporate law liability is *purely personal.* It does not affect, as already mentioned, the board or the management of a company as such, but rather the individual board members and managers. The following distinctions may be helpful: 68

It might be, as tends to be the case, that individual organs have caused damage while others have not, or at least not to the same extent. For example, auditors, who normally only examine a company's books once a year, cannot have caused or have helped to cause damage which was done prior to their audit. They are only liable for any increase in the damage which occurred since the date of their examination or report (see N 162-3). Further, the degree of fault and thus the extent of liability will often be greater for those persons who intentionally breach a duty of care. Thus, a manager who engages in criminal behaviour will generally be liable for the entire damage caused, while an honest member of the board or an auditor who is simply not up to the job and was unable to detect the criminal wrongdoings might successfully plead for a limitation of liability due to having been much less at fault (see below N 162). 69

The conditions of liability (see N 2 and in detail below) must therefore be examined *separately for every person involved,* including both individuals and legal entities, though legal entities are accountable for the conduct of their organs and their auxiliaries. 70

The following conditions must be *cumulatively fulfilled* for a person to be liable: 71

1. Damage

a) A precondition for liability is damage, that is *financial loss*. Liability claims are inconceivable in the absence of damage. 72

Lack of damage is the main reason why board members of group companies or companies which are controlled by a managing sole shareholder will often not have to account for financial loss even if they have criminally neglected their corporate duties; those responsible in the 73 group or the main shareholder himself will have shielded the company from damage.

74 Absence of damage is also the reason that amateur auditors, who are legally prohibited but in practice still commonly utilized, often do not face liability for their acts or omissions despite their incompetence.

75 A further explanation as to why in practice even the gravest breaches of duty are sometimes of no legal consequence is that the creditors of a company are only deemed to have suffered damage, and are therefore only entitled to sue, when the company is *indebted* (see also N 198). Beforehand, only the company and its shareholders are entitled to sue. Often, however, the latter will have countenanced the omission or laxness and are thus neither willing nor entitled to file suit (see N 180).

76 b) The concept of damage under the law of corporate liability is, in principle, the same as that under Swiss private law *generally*. The Federal Tribunal has, however, developed *special rules* for corporate law which, despite being virtually untenable from the point of view of legal theory, have nonetheless established themselves and are ultimately practicable. The following is based on the more recent case law of the Federal Tribunal which has been confirmed many times.

1.1. Concept

77 The damage is the *difference* between the *current status of the assets* of the damaged party and the *status which those assets would have had if the damaging event had not taken place* (BGE 127 III 76). Relevant under corporate law is any form of damage, including both *actual loss* (damnum emergens) and *thwarted profit* (lucrum cessans). By contrast, *tort moral* is not generally taken into consideration; we are not aware of any cases of corporate liability where compensation was paid for «immaterial damage».

78 It is irrelevant whether the person responsible profited or intended to profit from his damaging actions. It is also irrelevant whether the person responsible is himself a damaged party. Finally, it is further irrelevant whether the damage caused can be «set off» against particular benefits to the company.

1.2. Direct and indirect damage

Breaches of duty can damage the company, its shareholders and its creditors. The following distinctions must be drawn: 79

a) *Direct* damage is that which a company, shareholder or creditor *suffers individually* (BGE 110 II 393). This is for instance the case for a creditor who has given a company a loan based on a false balance sheet, or for a shareholder who has subscribed to a capital increase based on a misleading prospectus. 80

Direct damage to shareholders or creditors seldom occurs in practice. Generally, breaches of duty at first affect a company and it is the *latter's* assets which are directly affected. 81

b) If a company is *damaged directly,* its *shareholders* suffer *indirect* damage. Since the company has suffered financial loss, its shares are worth less. If the loss leads to insolvency and to bankruptcy proceedings, then the *creditors* will also suffer damage to the extent that they have to accept a shortfall. Direct damage to a company therefore always implies indirect damage to its shareholders. On the other hand, creditors are only indirectly damaged if a company becomes bankrupt and can no longer fulfil its obligations. 82

c) While a *company can only suffer direct damage*, *shareholders* and *creditors* can suffer *both direct and indirect damage.* Their possibilities to sue depend on the type of damage suffered (cf. IV, N 185 et seq.). 83

d) Pursuant to the concept described here, which was valid in the context of both the general law of torts and, until recently, the law of corporate liability, the distinction between direct and indirect damage should be drawn depending on *whether the damage has directly affected the damaged party's assets or whether the latter has only suffered indirect damage* due to the fact that the inner value of the company's shares has sunk because of the damage suffered by the company or if, because of the losses sustained, the company is no longer able to fulfil its obligations towards its creditors (cf. for example BGE 110 II 393). 84

In its more recent practice, the *Federal Tribunal has departed from this criterion* in cases where creditors in the bankruptcy of a company filed suits and held that the decisive criterion is no longer whether the assets of the company or the creditor have *diminished.* Instead, the Tribunal 85 has focused on the *legal basis* for the damage claim in question. The aim of this practice, which has now become consolidated, is to try to restrict as far as possible *individual suits* of creditors in the bankruptcy of a company in favour of a collective suit brought by the administrator in bankruptcy, from which the creditors will all benefit equally. In reality what is at stake, contrary to the inaccurate terminology adopted by the Federal Tribunal, is not a question of the type of damage but of having the proper *standing to sue* (Now supposably also the Federal Tribunal in the so-called Biber-case, 4C.111/2004). We will deal with this question in more detail below (see *sub* IV, N 185 et seq.).

1.3. Calculation of damages

86 a) *Preliminary remarks:* A distinction must be drawn between the *calculation of damages* and the *measure of damages*. The starting point is always the damage suffered and the damaged party never recovers more than full damages. (The situation is different under American law where damages can have an additional penal element and the responsible party may be ordered to pay multiple damages.) It may be that the responsible party only has to replace part of the damage suffered because the court can reduce the measure of damages for a number of reasons (cf. N 212 et seq. below).

87 b) A duty to pay damages exists only to the extent that someone has caused damage by *his own faulty acts* (cf. N 133 et seq. below). A person who had no influence on damage caused is not liable for it. This fact, which goes without saying, is inferred from OR 759 I:

OR 759 I	If several persons are responsible for damage caused, each of them is [only] liable to the extent that the damage can be [...] personally imputed to them.

88 This restriction is particularly relevant as far as the *relationship between the board of directors and the auditors* is concerned. Auditors only have to act once a year when they audit the books after the closing of the business year. They cannot, therefore, be held liable for damage which had already occurred when they made the audit or their audit report. This is particularly important where it is claimed that the auditors failed to notice in time that a company was indebted. The auditors cannot be held liable for the entire damage, but only for the extent that the dam-

age *increased* from the time at which the overindebtedness should have been noticed and notified, that is since the time of the audit or the audit report, at which point the damage might well have existed for some time while the company continued to decrease in value.

Liability between members of *a board of directors and management* may also differ because the board only meets occasionally while management is generally a full-time job. 89

2. Breach of a duty of care

A breach of a duty of care means the *neglect of duties* imposed on persons subject to corporate liability rules either by statute or by articles of association. 90

2.1. Liability of board members, managers and liquidators in general

The duties of the persons entrusted with the administration, management and liquidation are not set out in detail in corporate liability law. OR 754 I speaks generally of damage which such persons cause «through an intentional or negligent breach of their duties» and refers to duties set out elsewhere in statute or in articles of association (cf. OR 716 et seq. for the board of directors and the management ; cf. OR 742 et seq. for the liquidators). 91

a) OR 717 imposes, along with the duty to treat all shareholders equally, a *general duty of care and loyalty* on a board of directors. This duty of loyalty is dependent on a company's best interests which must be determined on a case by case basis based on the purpose of the company and the specific circumstances. Generally, members of a board of directors must not put the interests of others, whether their own, those of individual shareholders or those of third parties, before the interests of the company. 92

This duty of loyalty also applies in a *group of companies*, which can entail insoluble conflicts of loyalty for members of the boards of group companies. Characteristic of a group of companies is uniform management and thus the subordination of the individual companies to the interests of the group. This can run contrary to the duty of loyalty towards one's own company. 93

94 b) A list of particularly important duties is contained in OR 716a, which details non-transferable and inalienable duties of a board of directors (cf. below N 111). Each member of the board must have this catalogue in mind at all times.

95 c) The courts have held, and writers have suggested, that a board member breaches a duty of care if:

- He *removes corporate assets* without ensuring that proper consideration is received in return, or if he fails to claim the amount due for restitution because of a clandestine dividend;
- He pays back a loan which was used to effect *a simulated payment of the subscribed share capital;*
- He invests four-fifths of the company's assets in *a highly speculative investment.* This is a breach of duty even if reliance was placed on professional advisors, and it is of no avail that personal loss was also suffered through such investments;
- He fails to diversify risk. Such *cluster risks* are not justified even where the quality of the debtor is not in question;
- He fails to invest the company's assets, to the extent that they are not required for other purposes, so that they gain interest;
- He *transfers assets abroad* which are necessary for the fulfilment of domestic obligations. It is also a breach of duty where the transfer is made to a bank of dubious repute and in the sole interest of one of the shareholders;
- He conducts transactions with the majority shareholder which are disadvantageous for the company and the minority shareholders, for instance by taking into the balance sheet dubious debts of the majority shareholder;
- He *speculates* with credit granted to the company and fails to devote sufficient attention to the company's lines of credit;
- He takes out a *mortgage* on company real estate *for his personal debts;*
- He does *not pay for subscribed shares* at the time and in the amount provided for by the prospectus and articles of association and also allows that further shareholders, namely the directors, act similarly, so that from the onset the company only has half the means envisaged;
- He puts the interests of the parent company of *a group of companies* before the duties of the subsidiary for whom he acts (for more details see N 92 et seq. above);
- He fails to take measures, despite irregularities in the activities of individual members of the board, of which the other members should be aware;
- He does not order rigorous supervision of the manager of the company who is in a precarious situation, although the manager does not have impeccable credentials and is not subject to strict supervision and who, in particular, has neglected to draw up an accurate inventory of stock;

- He does not give notice of termination to a director who, by his breaches of duty, damages the company;
- He does not direct that the *necessary amounts be written off*, with the result that the statutory rules concerning the maximum permitted valuation of assets are massively violated;
- He neither prepares a *budget* nor provides for a professional financial plan and also fails to delegate such tasks to the management;
- He fails to provide for *proper accounts* including the annual report and its audit and keeping the books for at least ten years (OR 962 I);
- He *fails to notify the court in the event of overindebtedness* pursuant to OR 725 II although he is aware or should be aware of such overindebtedness. On the other hand, in the event of overindebtedness it is permissible first to examine where there are real prospects of recovery which justify postponing notification. We propose that postponement of notification further be allowed as long as promising negotiations are being conducted with the main creditors. This question is controversial;
- He enters into new obligations while aware of the company's overindebtedness;
- He fails to consult a specialist despite his own *inexperience* in a certain matter;
- He accepts a mandate although he does not have the necessary know-how for it (so-called *assumption of fault*);
- He fails to take and/or supervise the measures necessary to prevent *insider dealing;*
- He commits a criminal offence by making use of or divulging information from an insider transgression.

d) The courts have held that *liquidators* commit a breach of duty if they erroneously neglect to include a creditor in a distribution list or delay the realisation of assets. Liquidators are also liable for debts incurred during the course of a liquidation if such debts are not justified by sound business reasons. 96

2.2. Liability in the case of delegation

a) The board of directors is a company's organ entrusted by statute with *executive tasks*. In addition, there is a statutory *presumption of competence in favour of a board of directors*, which is competent for all tasks which do not fall by statute under the competence of the general shareholders' meeting or the auditors: 97

OR 716 I	The board of directors can make resolutions concerning all matters which statute or articles of association do not reserve to the general shareholders' meeting.

98 OR 716 I only mentions general shareholders' meetings. That the law also assigns certain tasks exclusively to auditors results from the fact that auditors also act in the interest of the public and, in particular, creditors (BGE 106 II 235).

99 b) The law does not, however, require that a board of directors attend to everything, and instead permits a *delegation of management*:

OR 716 II	The board of directors conducts the company's business to the extent that it has not delegated management.

100 The delegation of management competence is not only a *right* but, under certain circumstances, a *duty*, in particular when a board member is not himself in a position to properly perform the necessary management tasks.

101 However, the statute sets out *formal restrictions* to the delegation of tasks (see N 105 et seq.), and there are also *material limitations* (see N 111 et seq.). However, provided it complies with the formal prerequisites and the material limits, a board of directors can delegate competence both *internally* to certain of its members (*committees*) or individual members (*delegates*), or *externally* to third parties such as *directors*, members of *management or group management*.

102 c) Proper delegation can considerably reduce the *liability risk* of board members:

OR 754 II	A person who properly entrusts another organ with the fulfilment of a task is liable for any damage caused by the latter unless he can show that in the choice, instruction and supervision of such organ the diligence was exercised which circumstances required.

103 The wording of OR 754 II emphasises the *residual liability* which remains despite delegation. More important, however, is the *exemption* from liability which this provision permits: a person who properly delegates a task is *not liable* if he can prove that in the choice, instruction and supervision of such organ the necessary diligence was exercised under the circumstances, also known as *cura in eligendo, instruendo et custodiendo*. Such exemption from liability should also apply in the event that an auxiliary or a third person extraneous to a company is entrusted with a task and not only, as the statutory text too narrowly implies, when another organ is so entrusted.

The extent of the three residual duties of care is not only determined by the degree of difficulty and the significance of the delegated task, but there is also an *interdependence* between the three duties. For example, a highly qualified person with much more expertise than the members of the board of directors in the special matter with which he is entrusted hardly needs instruction and supervision and can be confined to periodic reports. If, on the other hand, it is questionable whether the delegated individual is suited to the task given his training and experience, then instruction and supervision are important. 104

d) OR 716b I governs the *formal conditions* for the delegation of competence. 105

OR 716b I	The articles of association can authorise the board of directors to fully or partially delegate the management to individual members or third parties pursuant to a set of organisational guidelines.

What is therefore necessary is: 106

- A *basis* in the *articles of association* empowering a board of directors to delegate management in general or within certain limits. In the absence of such a basis the board of directors must accomplish the executive tasks itself as a collective organ. 107

OR 716b III	To the extent that the management has not been delegated it vests collectively in all members of the board.

  If a board of directors delegates competences without a statutory basis, it remains liable in principle. It might be possible to argue that the delegation was in the best interest of careful management and that therefore the members of the board should not be held liable, however the issue is hardly of practical importance because the standard articles of association adopted by most companies contain a delegation clause; 108

- A *set of organisational guidelines* formulated by the board of directors which defines the delegation within the basis provided by the articles of association and the framework of the law (cf. N 111 et seq.). A board of directors can therefore not delegate competences informally or by tolerating their exercise by others, but only by formulating organisational guidelines. 109

110 Cooperation between the *general shareholders' meeting and the board of directors* of a company is necessary for a delegation of competences with the effect of a release from liability. The shareholders' meeting defines the limits of permissible delegation, but can neither perform the delegation itself nor oblige the board to delegate. It is for the board to freely decide to what extent it wishes to avail itself of its possibilities of delegation.

111 e) The management can be delegated wholly or partially (OR 716b I, cf. above N 105). However, a board of directors is *not free to dispose of all of its tasks simply by delegating them* and concentrating instead entirely on supervision, as does the German *«Aufsichtsrat»*. OR 716a I contains a substantial list of *non-transferable and inalienable tasks* of a board of directors:

OR 716a I

> The board of directors has the following non-transferable and inalienable tasks:
> 1. overall management of the company and the issuing of the necessary directives;
> 2. determination of the organisation;
> 3. structuring of the accounting system, financial controls and planning to the extent necessary for the management of the company;
> 4. appointment and removal of the persons responsible for the management and the representation;
> 5. overall supervision of the persons entrusted with the management, namely in view of compliance with the law, articles of association, guidelines and directives;
> 6. preparation of the business report and the annual general meeting and the implementation of resolutions taken at the latter;
> 7. notification of the court in the event of overindebtedness.

112 The list was intended to be exhaustive but it is not quite so since the *Code of Obligations at other points* allocates further inalienable tasks to a board of directors, for instance:

– demands that partially unpaid-for shares be fully paid up, OR 634a I:

OR 634a I

> The board of directors decides upon the subsequent payment of contributions on not fully paid up shares.

– ascertainment that an ordinary capital increase has been carried out, OR 652g I:

OR 652g I	When the report concerning the capital increase and, if necessary, the auditors' confirmation are at hand, the board of directors alters the articles of association and at the same time ascertains: [...]

– passing a resolution concerning an increase of the share capital in the case of an approved increase, OR 651 IV: 113

OR 651 IV	Within the limits of the authorisation the board of directors can carry out capital increases. To the extent that these are not already contained in the resolution of the general shareholders' meeting it issues the necessary provisions.

– alteration of the articles of association following a conditional capital increase, OR 653g I:

OR 653g I	Upon receipt of the audit confirmation the board of directors records in a notarised document the number, par value and type of the newly issued shares as well as any preferential rights attached to the various categories and the amount of the share capital at the end of the business year or at the time of the audit. It alters the articles of association as necessary.

– Appoint signatories, as provided by OR 721:

OR 721	The board of directors can appoint holders of procuration and other commercial mandate holders.

Pursuant to what is probably the predominant opinion, the appointment and dismissal of holders of procuration and other mandataries can be delegated despite the clear (but for companies with numerous employees hardly practical) statutory rule. The appointment of persons on a high level of hierarchy remains an inalienable competence of a board of directors (OR 716a I [4]).

– Measures if half the share capital has been lost, OR 725 I:

OR 725 I	If the last balance sheet shows that half of the share capital and the statutory reserves are no longer covered, the board of directors immediately calls a general shareholders' meeting and proposes financial measures.

– The challenge of resolutions passed by the general shareholders' meeting, OR 706 I:

OR 706 I	The board of directors and each shareholder can challenge resolutions passed by the general shareholders' meeting which violate the law of the articles of association by filing suit against the company.

- The examination of the qualifications of particularly qualified auditors pursuant to Article 3 I of the Ordinance concerning the professional qualifications of particularly qualified auditors of 15 June 1992:

Art. 3 I of the Ordinance concerning the professional qualifications of particularly qualified auditors of 15 June 1992: Where the general shareholders' meeting has to appoint one or more particularly qualified auditors, the board of directors establishes whether the proposed auditors comply with the requirements of the present ordinance. It reports thereon to the general shareholders' meeting.

The future: The duty to establish that auditors are adequately qualified will probably remain after the current revision of the law regarding auditing requirements (see also N 40).

- Dismissal or dissolution of committees, delegates, officers and other mandataries, OR 726 I:

OR 726 I	The board of directors can at any time dismiss the committees, delegates, directors and other mandataries which it has appointed.

114 f) The Stock Exchange Act (BEHG) prescribes further duties of a board of directors. In particular, a board has the inalienable duty of reporting in the event of a takeover bid (BEHG 29 I).

BEHG 29 I	The board of directors of the target company (Art. 22 Abs. 1) provides the holders of membership rights with a report in which it comments on the takeover bid. The information provided by the target company must be correct and complete. The board of directors of the target company publishes the report.

115 g) Additional inalienable tasks have been created by the *Merger Act* (FusG), although these tasks are controversial. Pursuant to Article 12 I of the Merger Act, the *merger* agreement must be concluded by the highest corporate management or administrative organ – in the case of a corporation by the board of directors. FusG 36 I provides the same for

demerger agreements, and FusG 59 I requires that the highest management or administrative organ devise the transformation plan in the event of a *transformation*. Finally, FusG 70 I requires that the so-called transfer agreement in the event of a *transfer of assets* must be concluded by the highest management or administrative organ.

FusG 12 I	The merger agreement must be concluded by the highest management or administration organ.

FusG 36 I	Where a company transfers assets to existing companies by demerger the highest management or administration organs of the companies concerned conclude a demerger agreement.

FusG 59 I	The most senior management or administration organ prepares a transfer plan.

FusG 70 I	The transfer agreement must be concluded by the most senior management or administration organ of the entities concerned.

h) These material limits on the possibilities of delegation must always be observed because within this framework the board of directors remains responsible and its members can be held personally liable if they fail to fulfil their duties of care. 116

However, it is also permissible, and where the members of a board of directors do not have the necessary time also advisable, to delegate preparatory, executory and supervisory functions to *individual members* or *committees*. 117

OR 716a II	The board of directors can delegate the preparation or execution of its resolutions to committees or individual members. It ensures that its members receive adequate reports.

There is no need for a basis for such delegation in the articles of association or in the organisational guidelines. 118

Furthermore, a board of directors is authorised, and in the best interests of a company sometimes even obliged, *to use third parties for auxiliary tasks* even in the absence of formal authorisation. 119

i) As mentioned above, the statutory limits on delegation create problems in *groups of companies* because it is hardly possible to manage a group of companies if the board members of the individual companies 120 insist on performing the non-transferable and inalienable tasks themselves (N 93).

2.3. Liability of auditors

121 a) The duties of auditors are also not explicitly set out in the rules on liability (cf. OR 755, above N 35); some are to be found in OR 728 et seq., where auditors' duties regarding auditing, reporting and, in the case of obvious overindebtedness of a company, notifying the court are enumerated.

122 b) The courts have held that auditors commit a breach of duty if they

- Neglect to *examine* whether the *declared corporate assets really exist*, the audit duty covering not only invested and current assets but also claims, though a material examination of the most important positions and random checks of the others must suffice;
- Fail to check that the statutory requirements concerning the *maximum valuation of fixed plant are adhered to*, that the necessary *amounts are written off* and that stocks are evaluated pursuant to the lowest-value principle contained in OR 666, and that the assets are properly evaluated;
- Fail to verify the *quality of the debtor* of a large loan (cluster risk) who is economically entwined with the company;
- Fail to verify whether a proposal of the board of directors to pay a *dividend* is in conformity with the law and the articles of association;
- Fail to *report the defects* discovered in the course of their audit and do not make a reservation in their report to the general meeting of shareholders and board of directors with regard to the dubious management practice of the board;
- Fail to draw up a *consolidated balance sheet* although they can only discharge their auditing duties in the context of a group of companies by so doing (this decision, which was rendered under former corporate law, is obsolete to the extent that there is a statutory duty to draw up a consolidated balance sheet since 1993, see OR 663e et seq.);
- Fail to *convoke a general shareholders' meeting* although the board of directors fails to do so without good reason (cf. OR 699 I which prescribes a subsidiary duty to convoke a meeting);
- Neglect to convoke an extraordinary shareholders' meeting after the death of the sole member of the board;
- Fail to draw up a balance sheet reflecting *realisable sale values* despite a critical financial situation and fail to inform the general shareholders' meeting thereof (this decision was rendered under former corporate law; under current law it should suffice that there is no overindebtedness if the company continues its business);

- Propose to the general shareholders' meeting *unconditional ratification of the balance sheet* despite having suspected or established valuation defects, or only mention in their report the omission to write off certain amounts without examining whether the book surplus would really exist were the appropriate amounts written off;
- Fail to inform the general shareholders' meeting that the board of directors has neglected to inform the court of existing *overindebtedness*, and fail to propose that an appropriate resolution be passed by the meeting (this decision is obsolete to the extent that under current law the auditors are also in breach of duty if they fail to notify the court themselves in the event of obvious overindebtedness where the board of directors has failed to make such notification, see OR 729b II);
- Fail to notify the court of overindebtedness pursuant to OR 725 in view of the existence of letters of comfort, which are not an alternative to subordination of debt agreements;
- Accept their mandate despite *lacking the necessary professional knowledge*, or fail to renounce their mandate while also failing to consult a professional;
- Accept their mandate although they are *not independent.*

c) It is important that an auditing mandate be *limited* (cf. OR 728 I): 123

OR 728 I

> The auditors examine whether the books and the annual statement and the proposal as to the utilisation of the profit are in conformity with the law and the articles of association.

Auditors do *not have a statutory duty* to examine a company's revenue position, liquidity, financial policy and *general ability to remain in business* and to report on these points. Investors and potential shareholders therefore often have exaggerated expectations with regard to audit reports, known as an *expectation gap*, and make unjustified accusations of breaches of duty. 124

d) *The future*: The provisions governing auditors are due to be revised in the foreseeable future, the aim being uniform rules for all types of business entities. If the Federal Council's proposal is accepted in principle, which is expected, the duties of auditors will be broadened with regard to listed companies and other economically significant companies, and reduced for other types of companies. Small companies with less than ten employees will be allowed to waive auditors altogether provided that all its shareholders agree. In the future the law might therefore lead to increased liability in the case of larger companies and to a relaxation of liability for smaller ones (see the Federal Council's Green 125

Paper of 23 June 2004). The House of Representatives approved the proposal unanimously on 2 March 2005. Because the Senate in its meeting of 15 march 2005 opposed to the proposal in some minor points, these points will need to be deliberated again by both Chambers. The adoption of this proposal can nevertheless be expected in fall 2005.

2.4. Liability of founders

126 a) The cases of founders' liability are listed in OR 753. In particular, founders must ensure a correct manner of proceeding in the case of so-called qualified incorporations, that is when the shares are not liberated in kind or where at the incorporation stage it is planned that a company will take over considerable assets, at the stage of registration in the Register of Commerce and in accepting subscriptions for shares:

OR 753

> Founders, members of the board of directors and all persons involved in the incorporation of the company are liable to the company, to the individual shareholders and to the company's creditors for the damage caused by the fact that they
> 1. intentionally or negligently provide in the articles of association, an incorporation report or a capital increase report incorrect or misleading information regarding contributions in kind, acquisition of assets or the granting of preferential rights to shareholders or other persons, or in approving such a document violate the law in some other way;
> 2. intentionally or negligently cause the company to be registered in the register of commerce based on an incorrect certification or document;
> 3. knowingly contribute to accepting subscriptions from insolvent persons.

127 b) The rules governing founders' liability are also applicable, at least by analogy, to *capital increases*, a fact which is inadequately reflected by the wording of OR 753, though reports on capital increases are expressly referred to in OR 753 (1).

128 Founders commit a breach of duty if they:

- Represent that the shares have been *paid up in cash*, whereas in fact the company has received assets in kind, for example when, immediately after incorporation and planned in advance, the received cash is used for the purchase of assets with the intention of avoiding the stricter requirements for qualified incorporation;

- *Conceal a planned takeover of assets*. Such takeovers are deemed planned when at the incorporation stage formal contracts have already been concluded and also where there is a firm intention to acquire considerable assets;
- Overvalue deposits in kind;
- Collude in a *simulated paying* up of shares;
- Take up a short term loan in order to simulate the paying up of shares. If the lendor is aware of the purpose of the loan, he will be liable in the same way as the founders since founders' liability extends not only to founders in a formal sense but to all persons involved in the incorporation process (see N 43 et seq. above).

A *notary public* who fails to notarise the fact that shares have been paid up by set-off is liable as a founder, as is the president of a board of directors who registers a capital increase in the Register of Commerce despite being aware that the increase was simulated (there is liability under OR 754, see N 8 above). 129

2.5. Liability for a prospectus

a) The breaches of duty leading to liability for prospectuses are listed in OR 752 (see N 49 above). The basis for liability is the provision or dissemination of incorrect, misleading or incomplete information in a prospectus or a similar notification. 130

b) This is for instance the case if: 131

- A prospectus, circular letter or other communication contains *incorrect information* or *fails to divulge important information* so that, taken as a whole, they are incomplete;
- The necessary information is correct but presented in a *misleadingly confusing* manner;
- The prospectus contains *exaggerated forecasts* of success;
- A «false» prospectus is used to induce potential purchasers to buy;
- No prospectus at all is issued despite a duty to do so. It has also been suggested that OR 752 presupposes active conduct, but in the event of capital increases such omissions can also lead to the liability of a board of directors due to a breach of duty pursuant to OR 754.

2.6. Liability under the Merger Act

Duties and breaches of duty under the Merger Act vary according to the type of restructuring taking place. To the best of our knowledge, we are not aware to date of any court decisions. 132

3. Fault

3.1. In General

133 a) Liability under corporate law is liability for *fault and is not no-fault liability*. If a person has acted without fault, he is not liable for any damage caused. However, for liability under the rules of OR 752 et seq., any form of fault is sufficient, including *slight negligence,* although minor fault can lead to a reduction of damages (cf. N 217 et seq.). The only provision requiring an intentional act is OR 753 (3) which deals with accepting subscriptions of insolvent persons at the incorporation stage or for a capital increase.

134 b) Negligence presupposes that the damaging event is *foreseeable* to the person causing the damage. It suffices that such person should have noticed, given the standard of care and awareness that can reasonably be expected of him, that there was a specific *risk of damage* being caused.

135 c) The question of fault cannot be answered generally but rather *individually for each potentially liable individual.*

136 The conduct in question must be judged bearing in mind the exponents' state of mind and the circumstances *at the time of the event.* It is, therefore, insufficient for liability that conduct appears *ex post* as incorrect.

3.2. Determination of the required care

137 a) In practice, the courts constantly apply an *objective standard of fault* so that whether a person is at fault is judged according to how a *reasonable and correct person* should have behaved under the given circumstances (cf. BGE 113 II 56, 99 II 180). Thus, the standard for auditors is how a diligent, independent and qualified auditor would have behaved, and the standard for a member of a board of directors is that applicable to a diligent person with business experience.

138 This objective standard has two consequences:

139 – The first is that there can be no subjective excuse, for example lack of time, ignorance or incompetence. Therefore, someone who takes on a mandate although he lacks the necessary expertise or time is at fault for this very reason (so-called *assumption of fault*).

- The second is that the *specific circumstances* must be considered, for instance the justification of incurring certain risks as a result of the purpose of a company, or on the contrary that particular caution would have been appropriate. 140

b) In this respect, writers and the courts have held that: 141

- The *more responsible* the activities of the persons involved, the *greater the degree of care* that applies to them.
- A special degree of care can be expected of organs with *special professional qualifications* as far as activities in their field are concerned.
- The complexity of an activity can necessitate the participation or the advice of third parties, and the failure to obtain advice can constitute fault. Conversely, one can normally rely on the advice of *recognised professionals*, unless under the circumstances particular scepticism is justified.
- The person responsible cannot exculpate himself by showing that he used the *same care as in his own affairs.*
- A particularly strict standard applies in the case of *conflicts of interest*, that is where the damage is caused by an act which an organ person performs for his own benefit or for the benefit of a third party.
- *Lack of time* is not a ground for exculpation.
- Unjustified *absence* does not reduce liability. (Writers are not in agreement as to the consequences of justified absence. Some propose that those who are excused should, if necessary, subsequently attempt to reverse incorrect decisions.)
- A mere *fiduciary activity* incurs full responsibility. Therefore, strawmen are liable as if they had acted sui juris. This is particularly true in groups of companies; a member of the board of a group subsidiary cannot exculpate himself by relying on directives of the parent company. On the other hand, he can stipulate that the parent company must indemnify him for any liability arising from compliance with such directives. Such indemnities are common in practice in fiduciary relationships and groups of companies, but are only effective provided the principal or the group of companies remains solvent (cf. below N 243 et seq.)
- Silence, abstention and other *passive forms of behaviour* do not by themselves preclude liability; active and manifest opposition to breaches of duty is necessary.
- In principle, a merely *internal attribution of competence*, for example to committees of the board of directors for the preparation, execution or supervision of tasks in the meaning of OR 716a II (cf. above N 117) does *not preclude liability*, as opposed to a formally and materially correct delegation of the competence to decide (cf. above N 102 et seq.). It might, however, prove to be a justified measure so that despite the fact that damage is caused, the members of the board as a whole cannot be reproached for negligence.

142 c) The objective standard of a careful businessman can cause problems with regard to persons who have been elected to a board of directors on account of their *special expertise,* such as for instance a recognised scientist who knows nothing about bookkeeping but performs useful services on the board of a pharmaceutical company. Although the wording of the law does not specifically address such circumstances, such specialisations should be taken into account. Under the law as it stands all members of a board must be expected to have a basic knowledge of bookkeeping. Persons who do not have such knowledge should confine themselves to acting in an *advisory capacity* and decline to sit on an executive board. This is also a reason that some companies have started to provide for an *advisory board* without competence to make any decisions.

143 d) If a *legal entity* has a mandate in a company, as is usual in the case of auditors (OR 727d I), it is liable for the fault of its *organs.*

OR 722

> The company is liable for the damage caused by wrongful acts which a person empowered to manage or to represent the company performs in the course of its business activities.

144 In addition to this the legal entity is also, in principle, liable for its auxiliaries, that is for persons who perform subordinate tasks. Certain possibilities of exculpation are conceivable, but to our knowledge none have hitherto been pleaded in practice.

3.3. No fault in the case of carefully deliberated but wrong management decisions

145 Business activities always involve taking *risks* for such risks are invariably linked with the exploitation of entrepreneurial *opportunities*. In consequence, it is important that no fault be imputed to those responsible if they made their decisions after careful deliberation, even if those decisions subsequently turn out to be wrong. In other words, it is necessary to recognise that a board of directors and management must be granted *wide discretion*.

3.4. The Business Judgment Rule as an objective standard in liability law

a) Recently more and more use has been made of the so-called *Business Judgment Rule* of American provenance to reduce liability and to protect organ persons who have made wrong decisions in good faith and using adequate care. The rule involves primarily *formal criteria*: 146

- There must be a *business decision,* that is a formal decision. Such decision may well consist of a decision to do nothing, but not just passive behaviour.
- Such decision must have been made by *unbiased* organs.
- The organs must have *exercised due care* in arriving at the decision. They must have gathered sufficient information and examined possible *alternatives*.
- The decision-making process must have been *correct,* for example the invitation to the meeting must have been formally announced, the meeting must have been properly conducted, and there must have been sufficient time for discussion of the decision.
- The organs must have acted in *good faith*, which is presumed not to be the case if a decision is «manifestly unreasonable». A particularly strict standard applies where conflicts of interest exist.

If these conditions are fulfilled, the courts should refrain from examining the contents of the decision of the organ in question. 147

b) The Business Judgment Rule is a useful instrument for an *objective test of decision-making* and has an effect both on assessments of compliance with duties of care as well as questions of possible fault. It should lead to acceptable results in most cases where OR 754 applies. 148

In practice, *fault* often goes hand in hand with a *failure to comply with formal duties*, such as when meetings are not held at all or only *pro forma*, when unambiguous accountancy rules are flouted, when the necessary documents in the case of qualified incorporations or capital increases are not prepared or are flawed, or when the measures to be taken in the event of capital loss are ignored. Such *formal misbehaviour* is the most frequent ground for the raising of liability claims. 149

c) It is to be hoped that in the future the Business Judgment Rule will be used even more often to assess the conduct of organs since it would 150 lead to a more objective and foreseeable court practice in questions of corporate liability. The fact that it has already found its way into decisions of the Federal Tribunal is grounds for optimism.

151 d) One *reservation* should be addressed to board of directors and management: The Business Judgment Rule must not degrade the work of executive organs to mere *box ticking* so that the focus becomes going through checklists and doing everything right in a formal sense only. *Substance* must remain at the centre of administration and management. But as a basis for rational decision-making and for an assessment of the decisions taken the objective approach provided by the Business Judgment Rule is welcome.

3.5. Fuzziness in the borderline between breach of duty and fault

152 a) The adoption of an objective standard of fault has made the theoretical line between the duty of care on the one hand and fault on the other virtually redundant. In practice, breaches of duty and fault are rarely distinguished. The Business Judgment Rule, which to a large extent relies on compliance with formal duties of care, strengthens this convergence. In practice it has *regularly been held that there was fault where there was a breach of duty.*

153 b) In consequence, it is no longer of relevance in litigation whether – and this depends on which category of person is raising a claim and is not completely clear – fault has to be proven by the plaintiff or, conversely, whether the respondent organ must prove that he was not at fault. A breach of duty is deemed, at least implicitly, to constitute a *presumption of fault.*

4. Adequate causal lien between the damage and the breach of duty

154 a) There must be a *causal lien* between a breach of duty and the damage. The act or omission in question must be a cause of the damage which has arisen, though not necessarily the sole cause. In other words, without the breach of duty no damage would have arisen.

A causal lien is lacking despite a breach of duty where it can be established that the damage would have occurred even had the duty been properly discharged. 155

In BGE 119 II 259, the Federal Tribunal held that there was no sufficient causal lien between the incorrect conduct of auditors who had failed to mention in their audit report discrepancies which they had discovered, and the damage suffered through the delay in the opening of bankruptcy proceedings. The Tribunal reasoned that the sole shareholder, who was fully aware of the discrepancies, would not have been influenced by a critical audit report. By contrast, in an older decision the Federal Tribunal had found that there was a sufficient causal lien between reporting omissions and damage suffered (BGE 86 II 183 et seq.). 156

b) There is only liability for damages where the damage is not too remote. As in the law of torts, a natural causal lien is insufficient – such lien must also be *adequate*. The standard test applied by the Federal Tribunal requires that the breach of duty be such that *in the normal course of events* and *according to general experience of life* it is capable of causing damage of the type which has occurred, so that the occurrence of such damage is generally furthered by such conduct (BGE 123 III 112, 113 II 57). 157

The necessity of an adequate causal link refines the scientific concept of *natural causality* for *legal purposes* so as to allow an equitable system of liability. 158

c) OR 759 makes it clear that a person is only liable for damage which an adequately causal effect of his own breach of duty and of his own fault (cf. OR 759 I), and not for that part of the overall damage (see OR 759 II), which was caused exclusively by others: 159

OR 759 I, II	Where several persons are liable for the same damage, each is jointly and severally liable with the others to the extent that the damage is attributable to their fault and their personal circumstances. The plaintiff can jointly sue several respondents for the entire damage and move that the court determine the individual liability of each respondent in the same proceedings.

The demarcation is particularly important in the relationship between the board of directors and the auditors. Where a company suffers loss 160 due to the inactivity of the board of directors and such loss eventually leads to bankruptcy, the auditors cannot be held liable for that part of the damage which had already arisen prior to the audit (cf. N 88 above).

161 d) Invoking *other causes* of the damage such as breaches of duty by other members of the board of directors does not free a person from liability for it is *typical that damage arises as a result of the misconduct of several persons*, as the following examples illustrate:

162 – An officer damages a company by criminal behaviour, but this goes unnoticed by the board of directors because it fails to properly fulfil its duties of supervision, and the auditors neglect a proper audit of the books and thus do not detect the damage caused by the officer. All involved are liable for damages, but not all in the same amount: The officer, who has intentionally damaged the company, is liable for the overall damage. The members of the board of directors are also liable but they can plead that even correct behaviour on their part could only have prevented a part of the damage. The auditors are only liable for that part the damage which arose after their audit, since they were unable to prevent that which had already arisen.

163 – Auditors who neglect to notify the court despite overindebtedness are not liable for the damage originally caused by the board of directors, but only for its continuation and increase due to their failure to notify the general shareholders' meeting.

5. Absence of grounds for the extinction of the claim or debarment of the suit

164 A claim for damages may be extinguished or the right of the damaged party to sue for damages may be debarred for a number of reasons. The most common reasons are release, court judgments and settlements, the passage of time such as by the running of a statute of limitations or debarment, and conduct countenanced by a resolution of the general shareholders' meeting or enjoying the approval of all shareholders.

5.1. Release

165 a) Release (*décharge*) leads under certain circumstances to the extinction of some, but not all, claims for damages:

OR 758	A resolution by the general shareholders' meeting granting release only covers facts of which the meeting was aware and is only effective towards the company and those shareholders who voted in favour of the resolution or who have since acquired the shares in awareness of the resolution. The other shareholders' right to sue is extinguished six months after the adoption of the resolution granting release.

b) Resolutions granting release fall in the inalienable competence of a *shareholders' meeting* and are normally made at the ordinary annual meeting: 166

OR 698	The supreme organ of the company is the general shareholders' meeting. It has the following, inalienable competences: ... 5. the release of the members of the board of directors; ...

With regard to release, «persons who have participated in any way in the management [of a company] have no vote» (OR 695 I). This norm should be interpreted broadly. It also applies to persons who are not directly affected by the vote to the extent that they were involved in management. The mutual release of shareholders who are also on the board of directors or involved in management, with reciprocal abstentions, is invalid. If a person is bound to abstain, then so must his representatives and heirs. 167

c) *Valid* resolutions granting release: 168

- extinguish any claims of a company for damages (OR 758 I);
- extinguish the claims of those shareholders who voted in favour of release to damages for indirect damage, as well of such claims of those shareholders who acquired their shares subsequent to the resolution but in awareness thereof (OR 758 I);
- limit the duration of the right of the remaining shareholders to sue for damages for indirect loss to six months (OR 758 III; cf. N 165 above);
- but have no effect on the right of creditors to sue for indirect damages;
- cannot be pleaded as a defence to an action by all the creditors after the opening of bankruptcy proceedings;
- and also have no influence on claims of shareholders and creditors for direct damages.

169 d) The effects of a resolution granting release are often *overestimated* for two reasons:

- The resolution granting release only covers «disclosed facts». An organ which has breached a duty will not generally emphasise such fact but rather attempt to conceal it, and because of this the release is without effect.
- Above all, the great majority of liability suits are brought after the opening of bankruptcy proceedings by the administrator in bankruptcy or pursuant to OR 757 II by individual creditors (cf. N 200), and a release offers no protection against such claims.

5.2. Judgments and settlements

170 The effects of judgments and settlements on liability claims are controversial among writers and have only been partially clarified by the courts. The question of whether claims are extinguished by judgment or settlement must be examined *on a case by case basis*. In particular, settlements, which are often not clear, must be interpreted with a view to determining whether it was the will of the parties to settle all claims for damages once and for all, or whether claims against persons who are not a party to the settlement are reserved.

171 Nevertheless, a court *judgment* in proceedings brought by the administrator in bankruptcy, which is by far the most frequent case, is binding on both shareholders and creditors and thus terminates the matter, except in the rare case of claims by shareholders and creditors for direct damages pursuant to the practice of the Federal Tribunal.

5.3. Statute of limitations and debarment

172 a) OR 760 contains a uniform rule governing the statute of limitations, regardless of the type of damage and the legal basis for damages. Claims become statute barred *five years* after a damaged party becomes aware of the existence and the quantum of the damage, the identity of the person who caused the damage and the facts giving rise to liability (relative statute of limitations), but at the latest *ten years* from the day of the damaging event (absolute statute of limitations).

If a suit is based on a criminal act, civil law claims do not become statute barred pursuant to OR 760 II before the penal action where the statute of limitation for the latter is longer. 173

OR 760

> Claims for damages against persons liable pursuant to the preceding provisions become statute barred five years from the day when the damaged person has become aware of the damage and the identity of the person liable, and in all events ten years after the day of the damaging event.
> Where the claim is based on a criminal act for which penal law provides a longer statute of limitations, the latter also applies to the civil claim.

The statute of limitations can be interrupted pursuant to OR 135 with or without the connivance of the liable party. 174

OR 135

> The statute of limitations is interrupted:
> 1. through the recognition of the debt by the debtor, for instance by payment of interest or of part instalments, and the provision of collateral or a guarantee;
> 2. through the introduction of debt collection proceedings, filing an action or putting in a defence before a court or an arbitral tribunal, filing of a claim in bankruptcy and an invitation to participate in an official conciliation hearing.

Although the statute of limitations blocks an action for damages, *it does not extinguish the underlying claim.* A statute-barred claim for damages can be set off against claims by the liable person, and this fact can be of relevance in the case of suits brought by a company against former organs who for their part allege claims of their own against the company arising, for instance, from an employment contract. 175

b) A release validly resolved by a general shareholders' meeting restricts the duration of the right of those shareholders who did not vote in favour of bringing an action to six months (OR 758 II, see above N 165). 176

This deadline can *neither be interrupted nor extended*, but only complied with through introduction of suit before a competent court within the six month period. Depending on the applicable cantonal law of civil procedure the deadline is complied with either by a filing with the competent official conciliation authority or directly with the court (as to the future Federal code of civil procedure see below N 261). 177

178 By contrast with the statute of limitations, the elapse of the six month deadline extinguishes not only the possibility to sue on the claim before the courts but also the claim itself. Such extinguished claims can also no longer be pleaded in set-off.

179 c) It should be noted that the deadline under OR 758 II, unlike the statute of limitations, never affects creditors' possibilities to sue.

5.4. Acts based on a shareholders' resolution or ratified by shareholders

180 a) Pursuant to the maxim *volenti non fit iniuria*, a *company* cannot claim damages where its organs caused damage by executing valid and unchallenged resolutions of the general shareholders' meeting. Even an invalid resolution of the latter in favour of which all the shareholders voted probably precludes the right of the company to sue. It may be assumed that informal consent by all the shareholders or the sole shareholder to acts which cause damage has the same effect, and the same applies where all the founders or all the shareholders caused the damage.

181 b) The right of *shareholders* who neither approved of damaging acts nor tolerated such nor voted in favour of invalid resolutions of the general shareholders' meeting to sue for reparation of indirect damage is not affected.

182 c) *Creditors'* claims are not affected by resolutions passed by the general shareholders' meeting nor by the consent of the shareholders or founders, not even where the administrator in bankruptcy raises such claims on their behalf.

183 d) The fact that shareholders have no standing to sue where they knowingly tolerated or even provoked breaches of duty is of particular relevance where *groups of companies* are concerned. The members of the board of a wholly owned subsidiary can comply with instructions from the parent company even where the duty of care owed to the subsidiary is thereby violated. The disregard of the statutory duty of care towards the subsidiary is of no significance as long as the subsidiary's solvency is not at stake. In this case neither the company itself nor the (sole) shareholder can sue, and the creditors only have standing to sue in the event of bankruptcy. Therefore, it is a rule of thumb that members of the board of a subsidiary within a group of companies ultimately only have

to ensure (but this they must do) the fulfilment of obligations towards third parties and that their acts do not contravene *bonos mores*.

The situation is different where third party *minority shareholders* have 184
a stake in a group company. Such shareholders have a right to insist that the interests of the company come first. However, it is often difficult to identify such interests of the group company clearly, for its fate is often inseparably connected with that of the group.

IV. Raising claims

Pursuant to OR 753 I, 754 1 and 755, a *company* itself, its individual *shareholders* and, in the rare cases where a company also has participation capital, its participants as well as the *company's creditors* have a claim for damages (see N 46, 8 and 35 above). 185

In the case of *liability for a prospectus* under OR 752 (cf. above N 49), subsequent holders of the securities have standing to sue along with the original subscribing shareholders and creditors, but only if they show that they acquired the securities based on incorrect or incomplete information and provided that only a short time has elapsed between the release of the information and the acquisition of the securities. The company and other shareholders or creditors have no cause of action under the norms governing liability for a prospectus because they have not suffered any damage. 186

The categories of claimants pursuant to the *Merger Act* encompass a company, its shareholders and its creditors in the same manner as for the liability of founders, administrators and auditors. 187

With regard to standing to sue, a distinction must be made between a solvent company (see sub 1, N 189 et seq.) and one in bankruptcy proceedings (see sub 2, N 200 et seq.). In practice, the Federal Tribunal treats a company which has entered into a composition agreement with its creditors with assignment of assets in the same manner, while for other types of insolvency proceedings and in particular those aiming for a turnaround, the following remarks apply (BGE 122 III 166). 188

1. Raising claims outside of bankruptcy proceedings

Suits against organs of solvent companies are very rare in practice. Conceivable are suits brought by a company for reparation of direct damage and suits brought by shareholders who have suffered indirect or direct damage. 189

1.1. Claims raised by the company

190 The decision to raise liable claims of a company lies, in principle, with a board of directors. If a suit is directed against all or the majority of the members of the board, a resolution of the general shareholders' meeting is necessary or should at least be sought. In such cases the general shareholders' meeting will usually appoint a new board.

1.2. Claims raised by shareholders (and participants)

191 a) Damages for *direct* damage, that is damage which directly affects the assets of an individual shareholder (cf. N 80), can be claimed within the limitation period pursuant to OR 760 by each affected person individually. Thus, each shareholder has an *individual* right to sue which is independent from any claims for damages of other shareholders or the company.

192 The action is based on the general provisions of OR 41 et seq.

OR 41 I	A person who causes another person unlawful damage, be it intentionally or negligently, is liable for damages.

193 Furthermore, special provisions of the Code of Obligations and the Forum in Civil Matters Act (GestG) relating to the statute of limitations (above N 172 et seq.) and forum (cf. below N 263 et seq.) apply.

194 A damaged party no longer needs to be a shareholder when an action is brought, and it is theoretically conceivable that a sequence of owners of the same shares may sue together for the damage which each has suffered directly. We are not, however, aware of any such case.

195 b) In cases of *indirect* damage, that is when a shareholder has only suffered damage because the company has suffered damage and its shares are therefore less valuable (cf. N 82), OR 756 applies:

OR 756 I	As well as the company the individual shareholders can also bring suit because of the damage caused to the company. The shareholder's claim is one for damages to be paid to the company.

196 This provision grants every shareholder, regardless of the size of his holding, an individual right to sue.

The alleged *indirect damage is replaced indirectly*, that is the proceeds of the action accrue to the company and do not find their way into the shareholder's pocket. The plaintiff thus only participates in the proceeds to the extent of his shareholding. For this reason, actions for the reparation of indirect damage are singularly unattractive for holders of only a few shares, and the few shareholder suits brought during the last three decades based on OR 756 I were, to our knowledge, all brought for motives other than that of obtaining damages. 197

1.3. Claims raised by creditors

a) As long as a company is solvent and can fulfil its obligations, its creditors suffer *neither direct nor indirect damage*. They therefore have *no right to sue*. 198

b) It might be argued that a creditor has suffered direct damage due to the fact that his claim is less valuable after a company's reputation takes a dent with regard to solvency. Theoretically, a suit might be contemplated for this reason; however, we are not aware of any practical cases and do not expect any to arise. 199

2. Raising claims in bankruptcy proceedings

200

OR 757

> In the bankruptcy of the company which has suffered damage the company's creditors are also entitled to claim damages to be paid to the company. Beforehand however it is the administrator in bankruptcy who is entitled to raise the claims of the shareholders and creditors.
> If the administrator in bankruptcy declines to raise such claims, each shareholder or creditor is entitled to do so. The proceeds are primarily used to cover the claims of the plaintiff creditors pursuant to the provisions of the Federal Debt Collection and Enforcement Act. The plaintiff shareholders participate in any excess proceeds to the extent of their holdings, and the rest accrue to the assets of the bankruptcy. The assignment of the right to sue pursuant to article 260 of the Federal Debt Collection and Enforcement Act remains reserved.

The law and the recent practice of the Federal Tribunal have made the following changes to the situation in the event of bankruptcy and of an agreement with creditors with assignment of assets, which is treated in the same way as bankruptcy: 201

2.1. Preliminary observation: Restriction of creditors' (and maybe also shareholders') right to sue in the recent practice of the Federal Tribunal

202 a) In the recent practice of the Federal Tribunal, which has become consolidated in spite of hefty criticism (cf. N 85), it is the concept of *entitlement of damaged creditors to sue* and not that of damage which is fundamental:

203 Such right, which in the terminology of the Federal Tribunal is referred to as direct damage, apparently only exists where the conduct of an organ violates corporate law *provisions designed exclusively to protect creditors*, or constitutes an unlawful act pursuant to OR 41 or in a case of *culpa in contrahendo*, that is conduct in violation of good faith in the course of contractual negotiations (BGE 125 III 88, 127 III 377).

204 The courts have held that there are few provisions which purportedly *exclusively* protect creditors. According to the practice of the Federal Tribunal, the provision of OR 725 for the protection of a company's capital, that is the duty to notify the court in the event of overindebtedness, is not exclusively for the protection of creditors, with the result that damage caused by a violation of this duty does not directly damage creditors and therefore confers no right to sue on the latter.

205 This practice, which was initiated in 1996, aims to bundle the various claims against a bankrupt company into a overall claim of all its creditors, thus assuring equal treatment of the creditors and thwarting «suit running» (cf. BGE 122 III 189 et seq., 125 III 88 and BGE 128 III 183). This practical aim is attained at the expense of coherence from the point of view of legal theory. In latest decisions the Federal Tribunal correctly found that this practice limits the proper standing to sue and shall only be applicable if there are competing claims raised by the company and its creditors (decision 4C.48/2005 and 4C.111/2004).

206 b) Legal writers assume that these restrictions apply similarly to shareholders' right to sue. However, we are not aware of any such cases since shareholder suits in bankruptcy are extremely rare (cf. N 208).

2.2. Claims raised by the company

207 When a company is in bankruptcy, the decision as to whether to file a liability suit lies with the administrator in bankruptcy and, if there is

one, the creditors' committee. The claim which the company could raise *sui juris* is absorbed in the claim of all its creditors, who are represented by the bankruptcy organs.

2.3. Claims raised by shareholders (and participants)

Alongside the situation of direct damage suffered by a shareholder, which in light of the recent practice of the Federal Tribunal is difficult to envisage but which can nonetheless still, even in bankruptcy, be the object of a suit brought by the individual shareholder, all claims are amalgamated into the overall claim to be raised by the administrator in bankruptcy (see N 205). If the latter declines to sue, «then every shareholder is entitled to do so» (OR 757 II, see N 200). The same provision states that the proceeds are primarily used to cover the claims of the plaintiff creditors. Only such excess as might remain after all the plaintiff creditors have been satisfied would fall to the plaintiff shareholders, and since this is generally not to be expected, shareholders are rarely interested in liability suits when a company is in bankruptcy. 208

2.4. Claims raised by creditors

Creditors have no standing to raise claims until bankruptcy proceedings have been opened against a company (cf. above N 198). 209

Apart from the few possible cases in which, even under the new practice of the Federal Tribunal, direct damage of creditors is conceivable (cf. N 203), all claims of creditors are amalgamated into an *overall claim of all the creditors* (cf. BGE 117 II 435 et seq., confirmed for instance in BGE 122 III 168 et seq., 189 et seq., 201). Such claim is pursued by the administrator in bankruptcy (OR 757 I, cf. N 200) and all damages obtained accrue to the estate in bankruptcy and are applied to the partial settlement of all creditors' claims pursuant to the rules of the Federal Act on Debt Collection and Bankruptcy (SchKG). Cf. SchKG 219 which governs the order of distribution to the creditors. First, secured claims are satisfied, then unsecured claims pursuant to the statutory classes of claim set out ibid. 210

If the creditors as a whole decline to raise the claims, then each individual creditor is entitled to do so (OR 757 II), and can request the assignment of the right to sue pursuant to SchKG 260. If there is more than 211 one such creditor, they must sue together (BGE 121 III 494). Each retains the right to plead separate facts and to present his own case as well as to decline to continue with the action without endangering the position of the other plaintiffs. Creditors who wish to pursue their claims in court must act in concert. If various *fora* are conceivable or if the various litigants are unable to agree on a joint strategy, it is for the administrator in bankruptcy to give the necessary directions at the request of one of the creditors so that joint litigation is possible. The Federal Tribunal has not yet given a ruling on the question of whether a creditor wishing to claim damages for indirect damage in the bankruptcy of a company can base his claim directly on OR 757 II, that is without an assignment in the meaning of SchKG 260 being necessary. Here again it will be for the administrator in bankruptcy to ensure that joint litigation is possible by giving directions at the request of one of the creditors.

V. Who is liable to replace what type of damage?

1. Calculation of damages

The basic principal of Swiss law, and particularly Swiss corporate liability law, is that persons responsible are liable to pay *full damages* (but not more, see N 86 above). There are, however, a number of factors which may lead to a *reduction of the measure of damages* or even a complete exclusion of liability. 212

a) Pursuant to OR 44 I, the court may *reduce a measure of damages* or *decline to award damages altogether* where «circumstances» for which a damaged party is responsible helped to cause or augment the damage suffered: 213

OR 44

> If the damaged party acquiesced in the damaging act, or if circumstances for which it is responsible helped cause or augment the damage or in some other manner prejudiced the position of the person who caused the damage, the court may reduce the measure of damages or award no damages at all.
> If the livelihood of a liable person who neither intentionally nor negligently caused the damage would be endangered were it ordered to pay damages, the court can reduce the measure of damages for this reason.

The primary ground for reduction pursuant to OR 44 I is *concurrent fault on the part of the damaged party.* 214

It may lead not only to a reduction of the measure of damages but also to a total exclusion of liability. Where a damaged party acquiesced to the damaging acts, an award of damages is generally excluded, an alternative justification being that someone who acquiesces does not suffer any damage at all (cf. above N 180). 215

- A person who is both a creditor and a shareholder, who as a material organ was aware that the share capital had only fictively been paid up, cannot claim damages.
- There is no liability towards creditors who encourage a company running at a loss to stay in business.

A measure of damages may also be reduced where a damaged party failed to do all in his power to hold damage to a minimum or to avoid it altogether, thereby breaching the *duty to mitigate damages.* 216

217 b) OR 43 I provides that when measuring damages the court shall take into account the extent of the *fault of the person who caused the damage*:

OR 43 I	The court determines type and measure of damages, taking into account all circumstances and the extent of fault.

218 In cases of *light negligence* the court may award damages for only part of the damage.

219 A respondent can plead slight fault regardless of whether or not he is jointly and severally liable. This rule, which should go without saying but which the Federal Tribunal formerly did not recognise, is now expressly contained in OR 759 I (cf. N 229).

220 c) Where a liable person received inappropriately small compensation or acted selflessly, his liability may also be reduced pursuant to general principles of the law of torts:

OR 99 II	Liability is determined according to the particular nature of the transaction and is judged in particular more mildly where the transaction involved no benefit to the debtor.

221 A reduction is further conceivable where a mandate as member of a board or as auditor was accepted as a favour to a friend, as might still be the case despite increased awareness of the risks involved. However, lack of compensation or the inadequacy of such compensation can only, if at all, be pleaded as a defence against claims by the company and those shareholders who are aware of the particular circumstances, but not against claims of other shareholders and of the creditors.

222 d) Also conceivable is a reduction of damages pursuant to OR 43 I (cf. N 217) due to *particular personal characteristics of the person who caused the damage,* for instance a member of the board or an auditor in breach of duty.

- A reduction is conceivable if the person liable is suffering from an illness which impaired his faculties.
- It is possible that where a person would face an emergency situation in the meaning of OR 44 II were he ordered to pay full damages, such fact can be taken into account. We are not aware of any such cases, but the criterion of financial potency is often decisive in settlements, where the amount to be paid is often determined so that it is bearable for the person responsible.

- Reductions should not be granted due to inexperience, lack of time or a fiduciary capacity (cf. N 138 et seq.), though an exception might be made in the relationship between a company and its sole shareholder since, or to the extent that, those involved were aware of the special circumstances.
- The principal in a fiduciary relationship has no claim for damages as long as the board member which acted for him in a fiduciary capacity merely followed his instructions (cf. N 141).

e) *Third party fault* and *concurrent chance* only constitute grounds for reduction in very exceptional cases under the general law of torts. Theoretically, they could be taken into account in the context of corporate law liability but this does not seem to have been the case in practice hitherto. 223

Concurrent fault of *another jointly and severally liable person* does not generally constitute grounds for reduction. Instead, each jointly and severally liable person is individually responsible for the damage which he caused and in consideration of his own fault. The possibility, discussed by writers, of denying liability completely because a third party was so much at fault that the adequate causal lien was broken has hitherto been confined to the realms of theory. 224

f) The possibilities of a reduction of liability to pay damages, as set out above, are important in theory but *do not often play a role in practice* because damage is normally so great that even a reduction of damages would not lead to a bearable solution. A measure of damages is consequently often determined less pursuant to the above-mentioned criteria and more according to financial potency. It is not rare, and in the case of auditors it is the rule, for the *amount for which a damaging party is insured* to play a central role. 225

2. Joint and several liability and right of recourse

The liability of several damaging persons towards a damaged person, that is *externally,* is determined pursuant to the rules governing *joint and several liability* (cf. sub 2.1, N 229). This must be distinguished from the definitive allocation of the damages *internally* between the several liable parties. It can lead to a correction of the amounts paid externally through *rights of recourse* (see sub N 234 et seq.). 226

227 Joint and several liability as provided for under corporate liability law has the aim of *protecting creditors as best as possible.* Creditors can seek out the most solvent person liable and demand reparation of the entire damage, to the extent that such person cannot invoke a reduction in liability pursuant to one of the rules described in N 213 et seq. The creditors can also proceed against one or more jointly and severally liable parties and demand payments from each of them, within their means, until the entire damage has been covered.

228 By means of *recourse*, those who have satisfied claims for damages can recover from the other liable persons those amounts which they have paid, to the extent that such amounts are in excess of the sum for which they are liable internally given their circumstances and the extent of their fault.

2.1. External joint and several liability

229 Where more than one person is responsible there is joint and several liability, which means that each is liable for the entire damage to the extent that he caused or helped to cause the damage, and for which there was an adequate causal lien, and provided he cannot plead slight fault.

OR 759	Where several persons are liable for the same damage, each is liable jointly and severally with the others to the extent that the damage is personally attributable to them as a result of their fault and the circumstances.

2.2. Claiming damages for the entire damage suffered

230 A further simplification of an action to recover damages specific to corporate liability law is found in OR 759 II:

OR 759 II	The plaintiff can sue several persons jointly for reparation of the entire damage and move that the court determine the liability of each respondent in the same proceedings.

231 A plaintiff, therefore, does not have to concern himself with the fact that the jointly and severally liable respondents may be liable to varying degrees due to differences in questions of causality and fault. He can sue the various persons involved jointly for reparation of the *entire damage*

which they have caused. It is then for the court to determine how much each party is liable to pay the plaintiff.

As a consequence of joint and several liability, it is possible that an amount exceeding the entire damage suffered is awarded. The plaintiff can then proceed against each liable party for the amount for which the court held such party liable, but may not demand more than the entire damage. Once the latter has been recovered, the plaintiff can raise no further claims. 232

Example: The entire damage is 100. The court determines that, in view of their fault and the causal lien between the fault and the damage, a criminal officer A is liable for 100, a member of the board of directors B who is not up to his job is liable for 60 and the likewise negligent auditors are liable for 40. Since the damaged party can only recuperate 100, it will, for simplicity's sake, only pursue the judgment claim against A alone, provided that the latter is solvent. If A is insolvent, the damaged party will proceed against B and C and demand from each the sum for which they have been found liable. If the solvency of all three is doubtful, the damaged party will attempt to obtain as much as it can from all three parties through debt collection proceedings. 233

2.3. Internal recourse

The system favouring a damaged party may result in certain liable parties having to pay more than the portion with which it would be fair to burden them within the group of those persons who caused the damage, whereas others have to pay nothing. This may be because the damaged party decided against suing them, because a judgment awarding damages was not executed or because the damage was already fully repaired by payments made by other liable parties. An internal compensation system is necessary and is assured by the right of *recourse*, with respect to which OR 759 III provides: 234

OR 759 III	Recourse between various liable parties is determined by the court in consideration of all circumstances.

The court thus has to determine the internal liability of each person concerned. If, based on the rules of joint and several liability, a liable party has *externally* paid more than the portion awarded against it *internally*, it can reclaim the excess from the other liable parties. 235

As in the general law of torts, the court has to decide while «taking all circumstances into consideration». Primary decisive factors are extent 236 of fault, amount of consideration received, position in the company hierarchy and the corresponding demands on the individual liable persons. The absolute limit is drawn by the rule that no party should have to pay more than the damage caused by his own acts (cf. N 229).

237 In the example given in N 233, the court will give B and C a right of recourse against A in the full amount of whatever they have paid, since they acted negligently while A acted intentionally. A will *under no circumstances be able to have recourse against B and C*, since it would not be appropriate if the latter were to be held internally liable for the damage caused by A's criminal acts. If A is insolvent or if his whereabouts are unknown, and B and C have externally paid 60 and 40 respectively, there will be no recourse since both have paid the maximum amounts.

238 If a jointly and severally liable party is insolvent, the others must cover the shortfall in proportion to the amounts for which they have each respectively been found liable (cf. the example in the preceding N).

2.4. Analysis

239 In the final analysis, the interplay between joint and several liability and recourse theoretically leads to the situation that each liable party must replace that part of the damage which corresponds to the circumstances and in particular to the extent of his fault. However, the damaged parties are favoured in two respects:

240 – They need not concern themselves with the internal situation between the various liable persons. They are at liberty to sue all or only one of them for reparation of the entire damage, with the risk in the latter case being that the respondent might successfully plead a reduction of his personal liability.

241 – The risk of insolvency of individual liable parties is shifted to the group of liable parties (cf. the example in N 233).

3. Excursus: Binding over liability risk

242 Meanwhile, it has become well-known, at least in interested circles, that a mandate as member of a board of directors or auditor is not a sinecure, but entails considerable risks. This increased sensibility corresponds to an increased need for security. In particular there are two possibilities:

- Indemnity clauses (cf. sub 3.1, N 243 et seq.), and
- Insurance cover (cf. sub 3.2, N 249 et seq.).

3.1. Indemnity clauses

a) In practice fiduciary agreements are often concluded – particular by board members acting in a fiduciary capacity – containing an *indemnity clause* wherein the principal, for instance the parent company in a group of companies or the sole shareholder in a one-person company, undertakes to indemnify the organ for any damage for which it might be held liable. 243

Example: «In the exercise of its mandate as member of the board of directors of company XY, the mandatary shall follow the instructions given by the principal, unless such instructions violate the law or *boni mores*. 244
The principal will indemnify the mandatary completely with respect to all claims raised against the mandatary in connection with its activity as member of the board of directors of company XY, and will replace all costs, losses and expenses incurred by the mandatary in the course of the proper fulfilment of the mandate.»

b) Such indemnity undertakings are, in principle, only effective between the parties to the agreement. In the case of one-person companies and in particular of 100% controlled subsidiaries of a group of companies, such undertakings should provide protection against claims of the companies (see above *sub* N 180, 183). On the other hand they have no external effect, that is towards shareholders who do not belong to the group and in particular towards creditors, who remain free to raise claims in the event of intentional or negligent breaches of duty (cf. N 181 et seq.). 245

Thus, the organ remains responsible and, in the event of intentional or negligent breaches of care, liable for damages, but can demand from their principal based on the indemnity undertaking that the principal satisfy such claims and restitute the legal costs of warding off the claims. It is therefore obvious that such an undertaking only helps if the *guarantor himself is solvent*. In the bankruptcy of a company, during which liability claims are generally raised, the principal itself is often insolvent. The indemnity undertaking is then worthless. 246

c) In isolated cases, an indemnity undertaking is made *by the company itself* for which the organ acts. Such undertakings are invalid since they violate mandatory corporate liability law (cf. N 5). 247

What is valid, although it too has been denied, is an undertaking on the part of a company to ward off claims from third parties. It is a general- 248 ly accepted opinion that companies can insure their organs against liability suits:

3.2. Insurance coverage

249 a) Due to increased liability risks and, above all, of the increased *awareness* of such risks, the demand for insurance coverage has greatly increased over the past two decades.

250 b) There are various possibilities of covering liability risks by taking out *insurance against pecuniary damage*:

- A company can take out blanket «Directors' and Officers' Liability Insurance» (D&O insurance) for all its managing organs. Such policies are characterised by flexibility and wide-ranging insurance coverage. The Swiss insurance market alone can offer international groups of companies insurance coverage of over CHF 100 million.
- Individual mandates can be covered by *individual agreements*. These agreements are mostly extensions of professional insurance for lawyers, notaries public or fiduciaries. The coverage is normally a one-figure million sum and the policies contain restrictions which are not contained in blanket D&O insurance policies.
- Auditors can insure themselves against risk by taking out comprehensive *professional insurance policies*. International auditing firms might have coverage exceeding CHF 100 million.

In recent years, members of foundation councils of pension funds pursuant to the Professional Pensions Act (BVG) have also taken out insurance more frequently due to the fact that increased risk is associated with the sinking cover ratio of pension funds. They can either have themselves covered by the fund's D&O insurance or take out an individual blanket insurance.

251 *D&O insurance* is the most common form of insurance for covering corporate law liability risks. The following remarks are confined to this type of insurance:

252 c) D&O insurance is taken out by a *company*. The company is the *insured* and pays the premiums, and this is also the focus of sometimes heard criticism.

The doubts surrounding D&O insurance are theoretical in nature and concern the fact that the concept of such insurance ultimately means that shareholders bear the financial consequences of an organs' corporate law liability, although such organs are personally responsible by law. However, it is widely recognised today that financing the transfer of risk by a company, and thus indirectly by its shareholders, also benefits the company and the shareholders and that therefore the *criticism levelled at taking out D&O insurance is ill-founded*: 253

- Highly qualified persons may only accept a mandate as a member of management or of a board of directors provided that they are given insurance coverage. This applies above all to companies engaged in international business, where there is the risk of being sued under an unfamiliar foreign law. Without adequate risk coverage it may also be difficult to find suitable persons for mandates on boards of directors and management of foreign subsidiaries.
- If a company does not provide insurance coverage, the members of the board of directors and possibly also of management or group management might protect themselves by taking out individual insurance. This is expensive and the costs involved are ultimately, through an increase in the compensation paid to such persons, *passed on to the company*. Such insurance is generally not available.
- Where a company offers no protection against what are often felt to be unfair risks, the management and the board of directors might be *overly risk averse* and thus for personal reasons fail to grasp attractive profit opportunities.

d) It has sometimes also been doubted whether organs acting for a company have the authority to conclude D&O insurance for themselves. Critics have suggested that such action may *not be covered by the purpose of a company* or that it ultimately constitutes a *prohibited self-transaction*. 254

We believe that the competence to conclude D&O insurance is contained in the competence of a board of directors to determine the compensation due to its members. It is true that the articles of association can provide that the general shareholders' meeting determines the compensation due to the members of the board, but it is rare that any use is made of this competence so that the presumption of competence in favour of the board of directors applies (see above sub N 97). Payment 255 of insurance premiums can be deemed to be part of compensation since in the absence of insurance cover a «risk premium» would have to be paid, and as long as the D&O insurance covers the members of management or group management, this would not be a case of self-contracting. It should be a matter of course that the provision of adequate protection against risk falls under the purpose of a company and that such purpose should, as is undisputed, be given a broad interpretation.

256 e) The characteristics of D&O insurance are:

- Usually all *former, current and future members* of the board of directors and of management along with «de facto» organs of the parent company and all subsidiaries worldwide are insured.
- The contract is based on the *«Claims-made»* principle, that is that all claims raised for the duration of the insurance cover are insured. Provided the insured ensures continuity of the contract, the time of the damaging act or omission is irrelevant.
- *The costs of warding off claims* are mostly advanced by the insurer.
- All claims based on an intentional or wilful violation of statutory provisions or the illicit acquisition of benefits are, in principle, excluded from the insurance.

  Further individual exclusions concern environmental risks, pension funds or claims in connection with discrimination or unfair dismissal.
- Depending on the concept, either the insurer undertakes to ward off the claim or the insured is bound to do so. The insured are, in any event, bound to work in close cooperation with the insurer and to discuss how to proceed when a claim for damages has been raised.
- Factors for calculating premiums include size and activity of a company, its exposure in the USA with regard to US subsidiaries and any securities issued by the company in the USA. Of great importance are also liquidity, profitability and stability of the company. Furthermore, the ownership situation and the organisation of the company play a role.

257 The following practical remarks should also be noted:

- What is often neglected in practice but is of great importance is the careful filling out of the application form and the submission of all documents of relevance for the insurance. If the particulars or documents are incomplete or untrue, the insurer can declare the policy partially or fully invalid. The business report as an annex to the application form is of central importance in this respect.

- The insured organs should insist on their right to notify claims themselves, since in cases of damage the company which has taken out the insurance might have an interest in avoiding notification because such notification can lead to increased premiums.
- It is helpful prior to entering into an insurance agreement to consult one of (the few) *broker* specialising in D&O insurance. Independently thereof the contractual terms should be subjected to *careful legal scrutiny.*
- It has become increasingly common that insurance companies insist on annual meetings with the Chief Executive Officer or Chief Financial Officer of the insured in order to obtain information on important business aspects such as corporate governance, accounting and strategic position.

h) Despite D&O insurance there remain residual risks due to exclusion 258
clauses, of which the insured may not be aware. These risks are not insured and must therefore be borne by the persons liable. In particular, classic «business risk» is not insurable. Nevertheless, taking out D&O insurance is without a doubt in the interest of the managing organs and usually also of the company and its shareholders.

i) The *costs of insurance coverage* reflect today's increased risk and 259
premiums have risen massively during the past few years. Some large enterprises might have difficulty in obtaining even minimum insurance cover.

VI. Procedural aspects

Procedural norms relating to corporate liability law are to be found in the Code of Obligations and the Federal Act on the Forum in Civil Matters (GestG). 260

Other questions are governed, pending the entry into force of a Federal Code of Civil Procedure, by the Cantonal codes of civil procedure. 261

In cases with an international element, the provisions of the Federal Private International Law Act (IPRG) and of the Lugano Convention apply. 262

1. Forum

1.1. Domestic

a) GestG 29 replaced the former OR 761 and allows a plaintiff suing under corporate liability law the choice to do so before the courts of either the domicile or seat of the liable person or of the seat of the company. 263

GestG 29	The courts of the domicile or seat of the respondent or of the seat of the company have jurisdiction over company law liability suits.

In practice, suits before the courts of the seat of a company are most common, particularly where there are several respondents, although the Forum in Civil Matters Act opens new possibilities. 264

GestG 7 I	Where several defendants are sued jointly, any court having jurisdiction over one respondent has jurisdiction over all respondents.

GestG 7 I, in addition to the possibilities offered by GestG 29, allows a plaintiff to sue further liable parties before the courts of the domicile or seat of one of the liable parties. 265

b) GestG 29 is not mandatory law. It is therefore admissible, according to the articles of association or in a jurisdiction agreement, to choose a different forum. It is, however, controversial to what extent such jurisdiction agreements are binding on shareholders, creditors and administrators in bankruptcy. 266

267 c) Corporate law liability suits can, under certain circumstances, be submitted to *arbitration*.

268 d) There is a special rule for claims derived from restructuring:

GestG 29a	For suits based on the Merger Act of 3rd October 2003 the courts of the seat of one of the entities involved have jurisdiction.

1.2. International

269 a) Where no relevant European element is involved, that is in cases where the Lugano Convention does not apply, the Swiss courts of the seat of a company or of the domicile (or usual residence) of a respondent have jurisdiction over corporate law liability suits (IPRG 151 I and II). Since the IPRG does not provide for a forum where several respondents are sued jointly, it is not possible to join further respondents domiciled abroad before the Swiss forum.

270 b) The Lugano Convention, which applies where a European element is involved, does not provide for a mandatory forum at the seat of a company. Consequently, the general jurisdiction rules of Articles 2 et seq. of the Convention apply. Unlike the IPRG, Lugano Convention 6 (1) provides a joint forum where several respondents are sued so that generally there is a uniform forum in Switzerland for a suit against all liable persons.

2. Litigious value and costs

271 a) Since the costs of a procedure depend on the *litigious value,* and therefore on the entire damages claimed and not the ultimate economic result in favour of the plaintiff in suits for reparation of indirect damage (see above N 197), the cost risk for small shareholders is considerable and often in no reasonable proportion to their chances of success. The law tries to correct this by granting the courts discretion to award costs against a company, contrary to the general rule that costs are borne by the losing party, even if the action is dismissed:

OR 756 II	Where given the factual and legal circumstances the shareholder had sufficient grounds to sue, the court may at its discretion award the costs against the plaintiff and the company, to the extent that they are not to be borne by the respondent.

This provision only applies to suits for the reparation of indirect damage by an award of damages to a company. The predominant but not uncontested opinion is that it not only applies to court costs but also to the parties' legal fees. A shareholder only has «sufficient grounds to sue» where he first properly exhausted the corporate law remedies and in particular his right to information (OR 696 et seq.). 272

b) The exception to the general rule governing costs is well-meaning but of little significance in practice. Since the court has discretion but has not yet established a uniform practice, there is uncertainty as to how costs will be allocated. In addition, there is still a misproportion between the cost risk and chances of success for minority shareholders. 273

For a shareholder with one-thousandth of the shares, which in the case of large companies implies an investment of millions, who therefore only indirectly participates in one-thousandth of the result of the proceedings, it is of little help that there is the hope in the event of failure to only have to bear one half or one third of the costs or even no cost at all. 274

As a result, it is to be presumed that also in the future liability suits will probably be brought by minority shareholders for reasons other than for reparation of damages (cf. above N 197). This is probably correct in order to avoid what would be, both for businesses and for the economy, an undesirable shift of emphasis from the business to the legal sphere. 275

c) Where a company is bankrupt, which is the case in the vast majority of liability suits, OR 756 II is without significance. 276

VII. Excursus I: Liability under criminal law, social insurance law and tax law

In practice, the highest liability risk for members of boards of directors and possibly also for auditors of small and medium sized companies, which are in the majority, most likely derives not from private but from public law liability norms, particularly from those providing liability for social insurance contributions and taxes. Organs might also incur additional penal sanctions. 277

The filing of a penal complaint against former organs is not uncommon, although the complaint is generally not an end in itself but a means of putting pressure on those concerned in hopes of eliciting payment of damages. If a private settlement is reached, the penal authorities are informed that the party who filed the penal complaint no longer has any interest in the matter and usually the proceedings are then closed. Nevertheless, the question of penal responsibility (too) must be taken seriously. 278

1. Liability under criminal law

The law also sanctions the violation of particularly important corporate law duties with penal measures. These are to be found primarily in the Penal Code (StGB), but also in special statutes. In particular, the following points should be noted: 279

- A violation of the duty of a board of directors to organise an accounting system and financial planning can lead to penal sanctions for illoyal business conduct (StGB 158 [1]), mismanagement (StGB 165 [1]), failure to keep accounts (StGB 166), incorrect accounting (StGB 325 I) and crimes in connection with the falsification of documents (StGB 251).
- In connection with the annual report and the auditors' report, a board of directors may incur penal sanctions for making false statements with regard to a business (StGB 152), the falsification of documents (StGB 251) and for incorrect accounting (StGB 325 I).
- It is incumbent on a board of directors to notify the Commercial Registry of facts which have to be registered by law. Discrepancies in

this connection can lead to an indictment for obtaining a false registration (StGB 253) or for making untrue statements to the Commercial Registry (StGB 153). Auditors may also incur penal sanctions in this respect.

- When a company is in bankruptcy, penal sanctions may be imposed against the board of directors and the auditors may be jointly liable pursuant to special norms (StGB 163–167).
- By violating confidentiality duties, the auditors and the board of directors may incur penal sanctions pursuant to a number of norms (cf. in particular StGB 162, 321 and BankG 47).
- Organs of companies listed on the stock exchange may incur penal sanctions pursuant to a number of further penal norms. The responsible organs may incur penal sanctions due to insider trading (StGB 161), share price manipulation (StGB 161bis), failure to comply with notification requirements (BEHG 41), violation of professional secrecy (BEHG 43) and violation of duties in connection with public bids (BEHG 42). In addition, the initial listing prospectus is deemed to be «a document» in the meaning of penal law so that further penal sanctions for falsification of documents or fraud are conceivable in this respect.
- The Banking Act sanctions with penal measures violations of banking secrecy and of further duties (cf. BankG 46 et seq.).
- Various penal norms of relevance to company organs in the fulfilment of their duties are to be found in separate statutes, for example pursuant to AFG 69 et seq. and in the field of tax law and social insurance law.

2. Liability under social insurance law

280 a) The central liability norm in social insurance law is Article 52 of the Federal Old Age Pensions Act (AHVG). This norm also applies by reference in the areas of invalidity insurance, income compensation, family farming supplements and employment insurance.

AHVG 52 I	An employer is liable for any damage caused by intentional or grossly negligent violation of insurance provisions.

The Federal Insurance Tribunal has applied this norm to develop a practice which is, in our opinion, unrealistic and incompatible with the letter of the law but which has been constantly confirmed and tantamount to *no-fault liability for members of boards of directors and further persons,* since it widens the statutory rule in two respects: 281

- With regard to the addressees of the norm (cf. sub b, N 282 et seq.), and
- With regard to the limitation of liability to that for gross negligence (cf. sub c, N 284 et seq.).

b) Pursuant to the practice of the Federal Insurance Tribunal, an *employer,* and thus a *person liable* under the statute, includes a member of a board of directors registered in the Register of Commerce, a manager with signing authority and even a majority shareholder who gives instructions to the board of directors. Under this practice, the liability of a holder of *procura* would also theoretically be conceivable depending on his specific internal duties, but it is unlikely that the Federal Insurance Tribunal would in practice hold him liable. Auditors are not liable. 282

Without having examined the question in detail, the Federal Insurance Tribunal thus qualifies organs as employers although employment contracts are not concluded individually with such persons but with the company. 283

c) Although the letter of AHVG 52 I only provides for liability in the case of *intentional* and *grossly negligent* conduct, the Federal Insurance Tribunal applies the norm as if it provided for *no-fault liability* (cf. BGE 108 V 203, BGE 112 V 159). In practice, it has held that there was gross negligence in the following circumstances: 284

- Where the sole member of a board of directors of a small company, with a simple administrative structure, failed to personally supervise the payment of social insurance contributions;
- Where the president of a board of directors failed to ensure that social security contributions were paid along with wages. The Tribunal has rejected the argument that the competence regarding social security contributions lies elsewhere;
- Where social insurance contributions were deducted from wages but not forwarded;
- In the case of failure to inquire about the duty to pay contributions, although this should have been done under the given circumstances;

- Where a strawman on a board of directors neglected his duties and failed to ensure compliance with the statutory duties, including the duty to forward social security contributions;
- Where a member of a board was, due to his function as secretary of the board, aware of the state of the business and thus was in a position to realise the implications of invoices and returns;
- Where a person was at the same time an officer and a member of the board of directors of a bankrupt corporation, a situation which requires a minimum of attention and awareness, did not attend to pay the social insurance contributions;
- Where a member of the board of a company in bankruptcy, who was solely responsible for financial aspects, failed to take any steps towards paying the social security contributions.

285 At least some of the above-mentioned decisions reveal a false understanding of business reality and of the duties of the members of a board of directors. However, one has to live with the practice of the courts, which has been confirmed by statements from the Federal Council and a commission of the House of Representatives, although Parliament has not incorporated this practice into the law (cf. BGE 129 V 11). At the very least, a recent judgment shows a tendency towards a certain limitation and back to general principles of tort law. It is to be hoped that this is not just an isolated case and that the Federal Insurance Tribunal will rethink what is, in our opinion, an untenable practice (Judgment H 273/03 of 4 October 2004).

286 d) Finally, it should be mentioned that apart from this extremely rigorous liability, which is not covered by the letter of the law, penal sanctions are also possible (cf. AHVG 87 et seq., BVG 75 et seq. and AVIG 105 et seq.).

3. Liability under tax law

287 a) In order to secure tax claims in cases where the latter appear endangered, some Federal acts provide, in certain cases, for joint and several liability of organs for outstanding tax debts of a company. In particular:

- When a legal entity is liquidated, the liquidators are liable for the tax due up to the amount of the liquidation surplus;
- When a company transfers its seat abroad, its organs are liable up to the amount of the company's net assets.

Such joint and several liability is provided for in the following statutes: 288

- Federal Act on Direct Federal Tax, Article 55 I;
- Federal Act on Withholding Tax, Article 15;
- Federal Act on Value Added Tax, Article 32;
- Automobile Tax Act, Article 11;
- Decree on Heavy Transport Duties depending on Capacity, Article 36;
- Mineral Oil Act, Article 11;
- Federal Tobacco Tax Act, Article 8.

Apart from these Federal acts, a number of Cantonal tax statutes provide for a similar system, for example the Tax Act of the Canton of Zurich in § 60. 289

The above-mentioned provisions are to a large extent identical. There are differences in that often, but not always, administrators in bankruptcy and liquidators in bankruptcy and composition proceedings are jointly liable, while in other cases such liability is confined in cases of the transfer of the seat to its managing organs. 290

These liability norms all provide for *no-fault liability.* Liable persons can, under some of the norms, exculpate themselves by showing that they did everything in their power to fulfil their fiscal obligations. 291

Article 10 I of the Federal Act on Stamp Duty also provides for the joint and several liability of the seller of shares in a company which has been *de facto* but not *de jure* liquidated, that is which is bereft of economic substance (so-called «shell company»); such an act is treated fiscally as a new incorporation. 292

b) In addition to this joint and several liability for outstanding taxes, responsible persons may under all fiscal statutes incur *penal* liability. 293

VIII. Excursus II: The relationship between the personal liability of organs and the liability of a company itself

Sometimes there is uncertainty with regard to the relationship between the obligations of a company itself and the liability of its organs. In this respect the following brief remarks should be noted: 294

1. Liability under civil law

a) Legal entities are bound by the acts of their organs. This goes without saying provided the organs act *legally*, in which case their acts are deemed to be the *acts of the legal entity itself*. 295

Pursuant to the so-called *reality theory*, that is that organs are part of the legal entity itself and not just its representatives, this norm also applies to *illicit* acts of organs. Provided the organs act «in the exercise of their business activities» and thus within the framework of their duties as understood in a broad sense, they bind the legal entity directly, OR 722: 296

OR 722	The company is liable for any damage called by illicit acts performed in the course of business by a person authorised to manage or represent it.

Based on this provision, a company has, for instance, been held liable for bills of exchange forged in the company's name by a chief financial officer (BGE 105 II 291 et seq.) and for the fraudulent activities of an assistant officer (BGE 121 III 179 et seq.). 297

b) The fact that a company is legally bound towards third parties does not change the fact that miscreant organs are *liable to the company*; indeed, this is a typical case of corporate law liability because the company has to meet obligations due to the illicit act and thus suffers loss. Pursuant to the general rules, shareholders can also bring a suit but creditors can only do so if the company has become bankrupt as a result of the illicit act (for more details see above sub IV, N 185 et seq.). 298

2. Liability for social insurance contributions and taxes

299 The personal liability of organs for public law contributions is subsidiary to the resources of the company itself, and as long as the latter can meet its obligations the organs are not liable. If a company cannot pay and due to bankruptcy or a transfer of its seat abroad it is difficult to claim payment from it, claims may be brought against its organs (cf. above sub 287).

3. Liability under criminal law

300 a) The traditional view is that only natural persons who are at fault can be punished.

301 b) However, for some time provisions outside of the Penal Code, which embodies the main mass of penal norms, have existed which provide for *penal sanctions against legal entities.*

302 Thus, the Federal Act on Penal Sanctions in Administrative Law of 22 March 1974 (VStrR) provides that a legal entity can be punished in place of the natural person responsible, provided that the maximum punishment is a fine of CHF 5,000 and that the identification of the natural persons responsible would involve disproportionate effort.

VStrR 7 I	Where the maximum conceivable sanction is a fine of not more than CHF 5,000 and where the identification of [...] the persons penally liable would entail investigations which would be disproportionate in view of the sanction, an investigation may be waived and the legal entity [...] condemned to pay the fine instead.

303 A further example is the Direct Federal Tax Act of 14 December 1990 (DBG).

DBG 181 I	Where procedural provisions are violated, taxes evaded or attempted to be evaded with effect for a legal entity, it is the legal entity which is fined.

304 c) A revision of the Penal Code which came into force on 1 October 2003 introduced a general subsidiary, and in exceptional cases a primary, penal liability of businesses.

StGB 100^{quater} I, II

> Where a criminal offence is committed in a business during the course of business activities and where due to inadequate organisation of the business such offence cannot be imputed to a particular natural person, the offence is imputed to the business. In such cases the business shall be fined up to CHF 5 million.
> Where the criminal offence falls under articles 260^{ter}, $260^{quinquies}$, 305^{bis}, 322^{ter}, $322^{quinquies}$ or $322^{septies}$ the business shall be punished irrespective of the penal liability of any natural persons, if it can be reproached for having failed to take all necessary and reasonable organisational measures to prevent such criminal offence.

The provisions to which StGB 100^{quater} II refers, that is those within the framework of the primary penal liability of the business or the company, concern offences such as money laundering and corruption. 305

d) Generally, natural persons who participate in illicit acts remain liable. 306

IX. International cases

1. General remarks

This book deals, as reflected by its title, with cases where *Swiss* corporate law applies. What has been said therefore primarily applies to companies incorporated under Swiss law or – a different criterion which however leads to the same result – which are registered as corporations in the Swiss Register of Commerce (but see N 309 et seq.). In international matters Swiss courts (as to their jurisdiction see N 260 et seq.) in principle apply to companies the law under which they were incorporated, for example Swiss law to Swiss companies only. 307

IPRG 154 I

> Companies are subjected to the law of the country pursuant to the law of which they are organised provided they fulfil the publicity or registration requirements of such law or, in the absence of such requirements, provided they are organised pursuant to the law of that country.

Pursuant to this so-called *foundation or incorporation theory* it is, in principle, the law of the country under which a company has been founded which applies, regardless of where it carries out its business activities. 308

2. Personal liability in the case of activities on behalf of a foreign company

Pursuant to the principle described above, personal liability with regards to companies incorporated abroad should be subject to the law of the country in question. However, in order to protect the domestic market, the law has departed from the general rule and made an *exception in favour of Swiss law.* 309

IPRG 159

> Where the business of a company incorporated under the law of a foreign country is conducted in or from Switzerland, liability of persons acting for such company is governed by Swiss law.

The wording of this provision raises numerous questions which cannot be addressed here. However, it should be mentioned that under what is 310 probably the predominant opinion, the provision only applies where the following conditions are cumulatively fulfilled:

- The company was incorporated under the law of a foreign country and is in principle governed by foreign law;
- The company regularly conducts transactions or administrative activities in or from Switzerland, and these constitute a significant portion of its entire activities; and
- By its business demeanour, the company gives creditors the impression (this it cannot do towards shareholders and the company itself) that it is a Swiss company.

311 If these three conditions are fulfilled, an exception is made to the incorporation theory and *Swiss law* applies to the liability of persons who were active for a *foreign company*. According to the protective character of this provision the plaintiff has the *right to choose* the applicable law. Where the seised Swiss court has jurisdiction both under IPRG 151 and under IPRG 152, the foreign law in question might be chosen to apply where it is more favourable, while the plaintiff will choose Swiss law if the latter is more favourable to its cause.

312 Where organs of Swiss companies act abroad their liability is governed by Swiss law, at least in proceedings before Swiss courts.

3. Liability of foreign issuers for prospectuses

313 A special norm applies to liability claims derived from the public issue of shares or bonds by a foreign issuer. Damaged parties have a choice:

IPRG 156

> Claims derived from the public issue of shares and bonds based on prospectuses, circular notifications and similar publications can be brought under the law applicable to the company or under the law of the country in which the issue took place.

314 Thus in cases where shares or bonds were issued in Switzerland, the damaged party can choose either the *foreign law* under which the issuing company is incorporated or *Swiss law*.

315 The place of issue is in Switzerland if the shares or bonds were open for subscription in Switzerland or if they were publicly placed there.

X. Practical significance and assessment of liability suits

a) A look at legal reality reveals an *ambiguous picture*. 316

Where a company is *solvent,* liability suits are a *rare exception*. Numerous cases of gross negligence remain without consequence and liability of organs is of no help for the following reasons: 317

- *Shareholders* often do not have the necessary information to discover breaches of duty, or they refrain from suing in light of the considerable effort required and risk entailed.
- A *company* itself will not sue for the simple reason that a culpable board member will not proceed against himself, nor against the auditors for having failed to point out his deficiencies, nor against the management whose deficiencies he overlooked.
- *Creditors* have no standing to sue as long as a company is solvent.

If, however, a company becomes *bankrupt,* it has become *a matter of routine* to seek reparation of damages from the members of the board of directors and the auditors and, although more rarely, from members of the management. Those involved are often treated with unusual rigour. The published court decisions present an incomplete picture since the majority of cases are settled out of court, sometime prior to a suit being filed and often after the first, second or third exchange of briefs, and therefore do not become public. 318

b) Contrary to general perceptions of justice and also contrary to the intentions of the legislator, *damages* awarded against individually liable persons often do not reflect the *extent of fault attributable to those persons*. In many cases the *opposite* is true. 319

- Those who are primarily liable due to gross negligence or intent and possibly criminal conduct have either fled abroad or still lead a luxurious life, even though they are supposedly without means. There is nothing to be recovered from them.
- Members of a board of directors who performed their duties honestly but with insufficient care have little to contribute to the reparation of damages due to the meagreness of their funds.

– It is the auditors who have to pay the most although they are the last in the chain of persons responsible for the damage. As legal entities they do not arouse the sympathy of the courts or receivers and, above all, they are generally insured and therefore perceived to have *deep pockets*.

320 c) Liability suits are *costly* and often *of above-average duration*. Proceedings lasting five or even ten years are not rare although, as mentioned, most proceedings are settled out of court. Thus, too much time passes before the damaged parties receive even partial compensation and the lives of the respondents are overshadowed for far too long by proceedings which threaten their economic existence. The lengthiness of the proceedings often means that judges and counsel change and that on both sides the parties who were the persons really involved are replaced by heirs.

321 d) The current regime also has *negative macroeconomic effects,* for example:

– The high costs of insurance (it is said that today for large auditing companies these represent the third highest cost point after salaries and rent) are passed on and thus make products and services more expensive;
– Above all, because of the high risks and the aleatory character of corporate law liability, it is becoming increasingly more difficult to find experienced persons prepared to assume the responsibility of being a board member and, in particular, the president of a board of directors of a corporation in trouble.

322 e) There is, therefore, a *malaise* in addition to the deficits attributed to corporate liability law as it stands from the point of view of *legal theory*. Such deficits can only partially be rectified by the somewhat bold practice of the Federal Tribunal.

323 Both in legal writings and statements from potentially affected individuals there has been a call for a *reform of corporate liability law* because, despite the corrections brought by the last corporate law reform, though helpful, many questions remain unanswered and uncertainty remains. Some proposals are:

- To improve clarity and foreseeability through a more precise description of the duties of organs, and in particular for auditors with regard to the concept of overindebtedness;
- To free auditors from joint and several liability with the board of directors and management, though since court suits are often for very large sums such joint and several liability seldom plays a role in practice, or to limit liability to a specific sum, for example to a certain multiplied factor of the fee received;
- To introduce measures to accelerate proceedings, though in this respect good ideas are hard to come by; and
- To rectify the defects of legal theory inherent in the current regime.

As far as we can see, politicians do not seem to have taken up the matter and, after the spectacular losses and collapses also affecting Swiss public companies during the past few years, it would probably be difficult to find backing for proposals which would benefit those who hold the reins of economic power in their hands. 324

* * *

Consequently, we will have to live with the law as it stands for the foreseeable future. In light of this, it is all the more important to considerably mitigate risk by observing a number of solid, comprehensible rules. In this respect members of a board of directors and similarly members of the management of a company or group of companies would be well advised to consider the advice which is to follow. 325

XI. Twelve golden rules for avoiding personal liability as member of a board of directors

The following advice is based on an analysis of reported and unreported court decisions and on the authors' experience. Following such advice should provide fairly reliable protection against liability suits. Above all, there is a negative guarantee: disregarding the rules makes liability suits very probable, particularly in the event of bankruptcy. 326

1. Play the corporation game

a) The corporation game must be played consistently, meaning that the *formal rules of corporate law must be strictly observed*. Anybody who founds a company should not only profit from the associated advantages but must also live with the disadvantages and the additional formalities. 327

- Resolutions must be passed by the competent organs and proper minutes kept. It also makes sense to record opposition to resolutions and in general it is important to put emphasis on documenting business events and resolutions;
- General shareholders' meetings must be correctly convoked and conducted and formally valid resolutions must be passed concerning all questions reserved to the shareholders by statute or by the articles of association;
- Profits may only be paid out of a company based on resolutions to such effect and these in turn must be based on an audited balance sheet;
- A board of directors must hold meetings. Lone decisions by the sole or majority shareholder are insufficient; and
- Auditors who comply with the statutory requirements as to professional competence and independence must be appointed.

b) Particular emphasis must be placed on one basic rule as far as a company controlled by a single natural person is concerned: *sole shareholders* often show little understanding of the fact that a company's assets do not legally belong to them and that they can only remove assets from the company by complying with legal requirements: 328

- as *salary* (but only in conformity with market standards);
- as *out of pocket expenses,* but only for expenditures made in the company's interest; or
- as *a dividend,* which presupposes a balance sheet profit, confirmation by the auditors that a dividend may be paid and a duly-minuted resolution of the general shareholders' meeting.

329 If majority or sole shareholders fail to separate their assets from the company's, resulting in a so-called *mixing of spheres,* they cannot expect creditors to accept the separation of their business and private assets in the event of bankruptcy. The limitation of liability which may have been the main reason for founding a company will no longer hold good and creditors can seek satisfaction from their private assets, not only through a liability suit but also by *piercing the corporate veil*, that is when the «shield» between the assets of the corporation and the shareholder is no longer respected.

330 The corporation game rules include a principle deriving from tax law that agreements between a company and its shareholders, or persons closely connected with the latter, must be concluded *at arm's length*, that is in the same way as they would be concluded with a third party: kept at a distance and with due caution to safeguard the company's interests.

331 c) It is ultimately impossible to play the corporation game in every respect in a *subsidiary company within a group of companies.* If the group is to be uniformly managed, members of the boards of the subsidiaries cannot strictly follow the individual interests of their companies. Even where the leeway for board members of subsidiaries is narrow, there are a number of measures which can be taken to avoid personal liability:

- *Formal requirements* must be complied with and in particular the necessary resolutions must be passed by the competent organs (the general shareholders' meeting or the board of directors) in the correct form and be minuted, even where the contents are dictated by the parent company.
- It must be ensured that the subsidiary remains *solvent.*
- The remaining risk must be met by concluding *fiduciary agreements* (cf. rule no. 9, N 346 et seq.) and taking out *insurance* (cf. rule no. 11, N 350).

In subsidiary companies which are 100% owned by the group, these rules should offer the necessary protection. The situation of the managing organs is more difficult where a company also has minority shareholders (cf. sub rule no. 3; N 336). 332

d) The game rules are basically identical to the *Business Judgment Rule* (cf. above N 146 et seq.). 333

2. Behave like a responsible businessman

A further basic rule is that each member of a board of directors of a company should act as a *careful and conscientious businessman* would. This includes making full use of information rights with a view to making informed decisions. 334

As a guideline, one should treat a company's assets with the same consideration as one's own. However, this is not always sufficient; a person who has invested the company's assets speculatively will not be excused merely by showing that he has been equally irresponsible with his own. 335

3. Let the minority live

In particular, where the shareholders are split into a majority and a minority group, the majority and its representatives on the board of directors will do well to take the interests of the minority into account. This also applies to groups of companies with regard to the external minority shareholders. 336

4. Ensure that there is adequate organisation

Adequate organisation must be implemented and maintained. 337

Where *management is correctly delegated* based on an authorisation in the articles of association and the details are set out in organisational guidelines (cf. N 106 et seq.), liability is restricted to careful selection of the persons chosen along with their adequate instruction and supervision. There is a correlation between these duties in that the more qualified such persons are, the less detailed their instructions need be. Con- 338 versely, more detailed instructions and more intensive supervision will be necessary where persons entrusted with management are inexperienced or where there are other question marks, for instance due to dubious credentials.

5. Really attend to the tasks which cannot be delegated

339 To the extent that a board of directors has tasks which are non-transferable and inalienable (cf. N 111 et seq.), these must be carried out and the members of the board cannot avoid liability by delegation or passivity.

6. Be reluctant to grant powers of attorney

340 It is advisable to not only select representatives carefully but also to *avoid single signing authority* and only register collective signing authority in the Register of Commerce.

341 Caution should be exercised in granting powers of attorney to persons who are not formal organs, particularly the sole shareholder or persons of the latter's confidence, all the more so if such persons are domiciled abroad.

342 *Powers of attorney* by a company to a bank should be limited to an appropriate maximum amount.

7. Ensure that accounting rules are adhered to and appoint capable auditors

343 The *norms regarding accounting* must be carefully complied with. It should be noted that recently the standard has been raised not only by the reform of corporate law but also by practical requirements.

344 *Auditors* must show that they have the necessary *qualifications and independence* to ensure a thorough and professional audit. *Amateur audits* by friends or relations should be avoided at all costs.

8. Consult experts

In case of doubt, experts should be consulted. Members of a board of directors should reserve the right, in the organisational guidelines or in a fiduciary agreement, to consult *outside* experts when internal information, which can generally be relied upon, is not completely convincing. 345

9. Make clear fiduciary arrangements

In the case of fiduciary activities it is particularly important to make sure that *formalities are complied with.* 346

It is helpful to conclude *fiduciary agreements* but one should be aware that these do not protect from third party claims. Such agreements open a right of recourse against the principal but such right will be worthless if the principal is insolvent, as is often the case on the day of reckoning. 347

Persons acting in a fiduciary capacity as an organ must reserve the right, in cases of doubt, to act in conformity with the *law* and *bonos mores* rather than in accordance with the instructions of the principal, and exercise this right. 348

10. Check that public law contributions have been paid

Since the courts have an extremely strict practice with regard to the liability of members of a board of directors and management for *social security contributions* (cf. N 280 et seq.), and since there might be a direct statutory liability of organs for outstanding *tax claims* (cf. N 287 et seq.), special care should be devoted to the payment of such public law contributions. In particular, in small organisations more is expected of the members of the board and the management than common sense would suggest. 349

11. Take out insurance (or have it taken out)

Personal liability risk can be effectively limited by insurance coverage, either in the form of an individual policy or by D&O insurance taken 350 out by a company (cf. N 249 et seq.). However, it should be kept in mind that insurance coverage is always limited and that it is necessary to carefully examine the insurance coverage chosen. Some liability suits will exceed the amount of the insurance coverage. Finally, even an impeccable insurance policy will offer no protection against the loss of time, the *nerve strain* and the *damage to reputation* which a liability suit can entail.

12. Exercise your right to resign and from the onset do not accept mandates for which you have neither the training, experience nor time

351 The *ultima ratio* for the limitation of risk is the possibility of resigning. Of course, as the organ of a legal entity it is irresponsible to throw in the towel too soon. As long as one actively remedies deficiencies, risk of liability is small. However, the risk of being sued along with other culpable and guiltless parties, even without material consequences, is not negligible! If deficiencies cannot be remedied despite a formal and minuted objection and if one is no longer able to identify with the structure and the policy of the business, loyalty and wistfulness at losing the fee are misplaced.

352 It is wise not to accept from the onset a mandate to sit on a board of directors if one lacks the professional qualifications or the time necessary for the proper fulfilment of the mandate. Sometimes one only becomes aware of such weaknesses after the event and in such case the preceding rules should be of help.

* * *

353 The twelve rules show that, with the exception of the fields of social insurance contributions and taxes, nothing superhuman is required of a board of directors. It should merely act as a careful businessman would. It is also required that main or sole shareholders and their fiduciaries respect the fact that a company is a separate legal entity whose assets must not be mixed with private or group assets.

354 Compliance with formalities and, above all, properly documented decision-making are required (cf. the Business Judgment Rule).

Finally, a member of a board of directors must really exercise the highest function in the company and not confine himself to lending his name, for money or for free, as an advertisement.

Annex

With the kind permission of the Swiss-American Chamber of Commerce we herewith print its translation of most of the previously cited provisions:

Code of Obligations

A. Liability in general
I. Prerequisites for liability

Art. 41

[1] Whoever unlawfully causes damage to another, whether willfully or negligently, shall be liable for damages.

[2] Equally liable for damages is any person who willfully causes damage to another in violation of bonos mores.

III. Determination of compensation

Art. 43

[1] The judge shall determine the nature and amount of compensation for the damage sustained, taking into account the circumstances as well as the degree of fault.

[1bis] In the event of injury or death of an animal that is kept in a domestic environment, and is not kept for pecuniary or profit-making purposes, the judge may take into account to a reasonable degree the emotional value of such animal to the keeper or the persons close to him.

[2] If compensation is awarded by way of an annuity, the party liable shall be simultaneously required to give security.

IV. Reasons for reduction

Art. 44

[1] The judge may reduce or completely deny any liability for damages if the damaged party consented to the act causing the damage, or if circumstances for which he is responsible have caused or aggravated the damage, or have otherwise adversely affected the position of the person liable.

[2] If a liable person has caused the damage neither willfully nor by gross negligence, and would be subject to distress as a result of his payment of damages, the judge may also, for this reason, reduce the obligation to compensate.

II. Extent of liability and scope of damages
1. In general

Art. 99

[1] In general the obligor is liable for any fault.

[2] The extent of such liability shall be governed by the special nature of the transaction, and will, in particular, be judged less severely if the transaction is not intended in any way to benefit the obligor.

[3] The provisions concerning the extent of liability in case of tort also apply by analogy to acts in breach of contract.

IV. Interruption of the running of the statute of limitations
1. Reasons for interruption

Art. 135

The running of the statute of limitations is interrupted:

1. by acknowledgment of the claim by the obligor, in particular also by making interest and installment payments, by giving a pledge or mortgage, or by giving a guarantee;
2. by prosecution for debt, or by bringing suit or by raising a defense in court or in arbitration, as well as by filing a claim in a bankruptcy, or by a summons to appear in an official conciliation proceeding.

II. Duty of care and loyalty

Art. 321a

[1] The employee must carefully perform the work assigned to him, and loyally safeguard the employer's legitimate interests.

[2] He shall operate the employer's machinery, tools, technical equipment, installations, and vehicles in a workmanlike manner, and handle them carefully, as well as any materials given to him for the performance of his work.

[3] During the employment relationship, the employee shall not perform work for third parties against compensation to the extent such work violates his duty of loyalty, and, in particular, to the extent it competes with his employer.

[4] In the course of an employment relationship, the employee shall not make use of or inform others of any facts to be kept secret, such as, in particular, manufacturing or business secrets that come to his knowledge while in the employer's service. Also, after termination of the employment relationship, he shall continue to be bound to secrecy

to the extent required to safeguard the employer's legitimate interests.

2. Liability for faithful performance
a. In general

Art. 398

[1] The agent is obligated, in general, to use the same care as the employee under an employment contract.

[2] He is liable towards the principal for the faithful and careful performance of the mandate.

[3] He shall personally perform his obligations unless he is duly authorized, or compelled by the circumstances, to entrust a third person with their performance, or if the right of substitution is considered permitted customarily.

D. Termination
I. Reasons
1. Revocation and notice of termination

Art. 404

[1] A mandate may be terminated at any time by either party revoking or giving notice.

[2] If termination is effected at an improper time, however, the party terminating is liable to the other party for the damages caused.

c. Subsequent performance

Art. 634a

[1] The board of directors decides upon the subsequent performance of contributions on shares not fully paid in.

[2] The subsequent performance may be made in cash, by contributions in kind, or by set-off.

III. Obligations entered into prior to entry

Art. 645

[1] Persons acting in the name of the Company prior to its entry in the Commercial Register shall personally be liable jointly and severally.

[2] If such obligations have been entered into explicitly in the name of the Company to be formed and are assumed by the Company within a period of three months after entry in the Commercial Register, the persons having acted shall be released and the Company shall be solely liable.

2. Authorized increase of capital
a. Based on the articles of incorporation

Art. 651

[1] The general meeting of shareholders may, by amendment to the articles of incorporation, authorize the board of directors to increase the share capital within a period of no longer than two years.

[2] The articles of incorporation indicate the par value by which the board of directors may increase the share capital; the capital authorized shall not exceed half of the current share capital.
[3] The articles of incorporation must, moreover, contain the details which are required for the ordinary increase of capital, except for the details on the amount of the issue, the type of contributions, the acquisition of assets, and the beginning of the period of dividend entitlement.
[4] Within the scope of the authorization, the board of directors may implement the increases of the share capital. At the same time, it issues the necessary provisions to the extent these are not already contained in the resolution of the general meeting of shareholders.

h. Amendments of the articles of incorporation and ascertainments

Art. 652g

[1] If the report of the capital increase and, if required, the confirmation of verification are in hand, the board of directors shall amend the articles of incorporation after ascertaining:

1. that all shares have been validly subscribed;
2. that the promised contributions correspond to the total amount of the issue;
3. that the contributions have been performed in compliance with the requirements of the law, the articles of incorporation, or the resolution of the general meeting of shareholders.

[2] The resolution and the ascertainments shall be made in the form of a notarized deed. The public official issuing the deed shall name all documents supporting the capital increase individually and confirm that they were submitted to the board of directors.
[3] The amended articles of incorporation, the report of the capital increase and the confirmation of verification, as well as contracts concerning contributions in kind and already existing contracts concerning acquisition of assets shall be attached to the notarized deed.

c. Adaptation of the articles of incorporation

Art. 653g

[1] Upon receipt of the confirmation of examination, the board of directors shall establish in the

form of a notarized deed, the number, par value and type of the newly issued shares, as well as preferential rights of individual classes of shares and the amount of the share capital at the end of the business year, or at the time of the examination. It shall make the necessary adaptations of the articles of incorporation.

[2] The public official issuing the deed shall state in the notarized deed that the confirmation of examination contains the required indications.

I. Powers

Art. 698

[1] The supreme corporate body of the Corporation is the general meeting of shareholders.

[2] It has the following powers which are inalienable:

1. the adoption and the amending of the articles of incorporation;
2. the election of members of the board of directors and of the auditors;
3. the approval of the annual report and of the consolidated financial statements;
4. the approval of the annual financial statement as well as the resolution on the use of the balance sheet profit, in particular, the declaration of dividends and of profit sharing by directors;
5. the release of the members of the board of directors;
6. passing resolutions on matters which are by law or by the articles of incorporation reserved to the general meeting of shareholders.

VI. Challenging of resolutions of the general meeting of shareholders
1. Standing and grounds

Art. 706

[1] The board of directors and any shareholder may take legal action against the Company to challenge resolutions of the general meeting of shareholders which violate the law or the articles of incorporation.

[2] In particular, resolutions are challengeable which:

1. withdraw or limit shareholders' rights thereby violating the law or the articles of incorporation;
2. withdraw or limit shareholders' rights without proper reason;

3. discriminate against or disadvantage shareholders in a manner not justified by the company purpose;
4. withdraw the profit orientation of the Company without the consent of all shareholders.

[3–4] *repealed.*

[5] A judgment annulling a resolution of the general meeting is binding both in favor of and against all shareholders.

5. Departure from the board of directors

Art. 711

[1] The Company shall, without delay, apply to the Commercial Registry for entry of the departure of a member of the board of directors.

[2] If such application is not filed within 30 days, the departing board member may himself request the deletion.

III. Duties
1. In general

Art. 716

[1] The board of directors may take decisions on all matters which by law or the articles of incorporation are not allocated to the general meeting of shareholders.

[2] The board of directors shall manage the business of the Company insofar as it has not delegated it to the management.

2. Nontransferable duties

Art. 716a

[1] The board of directors has the following nontransferable and inalienable duties:

1. the ultimate management of the Company and the giving of the necessary directives;
2. the establishment of the organization;
3. the structuring of the accounting system and of the financial controls as well as the financial planning insofar as this is necessary to manage the Company;
4. the appointment and removal of the persons entrusted with the management and the representation;
5. the ultimate supervision of the persons entrusted with the management, in particular, in view of compliance with the law, the articles of incorporation, regulations, and directives;

6. the preparation of the business report as well as the preparation of the general meeting of shareholders, and the implementing of its resolutions;
7. the notification of the judge in the case of overindebtedness.

2 The board of directors may assign the preparation and the implementation of its resolutions or the supervision of business transactions to committees or individual members. It shall provide for adequate reporting to its members.

3. Delegation of the management

Art. 716b

1 The articles of incorporation may authorize the board of directors to fully or partially delegate the management to individual members or third parties in accordance with an organizational regulation.

2 This regulation organizes the management, determines the positions required therefor, defines their duties, and regulates, in particular, the reporting. Upon request, the board of directors informs those shareholders and Company obligees who make a credible showing of an interest worthy of being protected in writing about the organization of the management.

3 To the extent the management has not been delegated, it shall be vested jointly in the members of the board of directors.

5. Holders of procuration and commercial mandate holders

Art. 721

The board of directors may appoint holders of procuration and other commercial mandate holders.

VI. Company liability for its corporate bodies

Art. 722

The Company is liable for any damage resulting from tort committed by a person empowered to manage or to represent the Company in the course of its business activities.

VII. Loss of capital and overindebtedness
1. Duty to notify

Art. 725

1 If the last annual balance sheet shows that half of the share capital and the legal reserves are no longer covered, the board of directors shall with-

out delay call a general meeting of shareholders and propose a financial reorganization.

[2] In case of a substantiated concern of overindebtedness, an interim balance sheet must be prepared and submitted to the auditors for examination. If the interim balance sheet shows that the claims of the Company's obligees are neither covered if the assets are appraised at on-going business values nor at liquidation values, then the board of directors shall notify the judge unless obligees of the Company subordinate their claims to those of all other Company obligees to the extent of such insufficient coverage.

VIII. Removal and suspension

Art. 726

[1] The board of directors may, at any time, remove from office any committees, managing directors, managers, and other holders of powers of attorney and mandatories it has appointed.

[2] Holders of powers of attorney and mandatories appointed by the general meeting of shareholders may be suspended from their functions at any time by the board of directors who immediately calls a general meeting of shareholders.

[3] Damage claims of those removed or suspended from their functions remain reserved.

2. Qualifications
a. In general

Art. 727a

Auditors must be qualified to fulfill their duties with the company to be audited.

IV. Duties
1. Examination

Art. 728

[1] The auditors shall examine whether the bookkeeping and the annual accounts, as well as the proposal concerning the use of the balance sheet profit, comply with the law and the articles of incorporation.

[2] The board of directors shall deliver to the auditors all required documents and provide them with the necessary information, upon request also in writing.

A. Liability
I. For the issue prospectus

Art. 752

If, upon the founding of a Company, or upon the issue of shares, bonds, or other securities, statements have been made or disseminated which are incorrect, misleading or not complying with the legal requirements in issue prospectuses or similar instruments, anyone having intentionally or negligently contributed thereto is liable to the acquirers of the security for any damage caused thereby.

II. Liability resulting from foundation

Art. 753

Founders, members of the board of directors, and all persons who participated in the foundation become liable to the Company, as well as to the shareholders and the Company's obligees, for any damage caused if they:

1. intentionally or negligently indicate in an incorrect or misleading manner, conceal, or disguise contributions in kind, acquisition of assets or the granting of special benefits to the shareholders or to other persons in the articles of incorporation, in a founders' report, or in a report on a capital increase, or if the approval of such measures violates the law in any other manner;
2. intentionally or negligently cause the entry of the Company in the Commercial Register on the basis of a confirmation or a deed containing incorrect statements;
3. knowingly contribute to the acceptance of subscriptions from insolvent persons.

III. Liability for administration, management and liquidation

Art. 754

1 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 Company's obligees for the damage caused by an intentional or negligent violation of their duties.

2 Whoever rightfully delegates the fulfillment of a duty to another corporate body is liable for any damage caused by it unless he proves that he applied the necessary care in selection, instruction and supervision under the circumstances.

IV. Audit liability

Art. 755

All persons engaged in the audit of the annual accounts and the consolidated financial statements, the foundation, a capital increase, or a capital reduction are liable not only to the Company but also to each shareholder and the Company's obligees for the damage caused by an intentional or negligent violation of their duties.

B. Damage to the Company
I. Claims outside bankruptcy

Art. 756

[1] In addition to the Company, each shareholder is entitled to file an action for damage caused to the Company. The claim of the shareholder is for performance to the Company.

[2] If the shareholder, based upon the factual and legal situation, had sufficient cause to file an action, the judge shall divide the costs in his discretion between the plaintiff and the Company to the extent they are not imposed upon the defendant.

II. Claims in bankruptcy

Art. 757

[1] In the case of bankruptcy of the damaged Company, also the obligees of the Company are entitled to request that the damage to the Company be compensated. In the first instance, however, the trustee in bankruptcy may assert the claims of shareholders and obligees of the Company.

[2] If the trustee in bankruptcy waives the right to assert these claims, any shareholder or obligee shall be entitled to do so. The proceeds shall be used in the first instance to cover the claims of the obligees filing suit in accordance with the provisions of the Federal Act on Debt Enforcement and Bankruptcy. The shareholders filing suit shall participate in the surplus in proportion to their participation in the Company; the remainder falls into the bankruptcy estate.

[3] The assignment of Company claims according to Article 260 of the Federal Act on Debt Enforcement and Bankruptcy remains reserved.

III. Effect of the resolution of release

Art. 758

[1] The resolution of release passed by the general meeting of shareholders is effective only for facts that have been disclosed and only vis-à-vis the Company and those shareholders who consented to the resolution, or who acquired shares subsequently with knowledge of the resolution.

[2] The right of the other shareholders to file an action is extinguished six months after the resolution of release.

C. Joint and several liability and recourse

Art. 759

[1] If several persons are liable for a damage, any one of them is liable jointly and severally with the others to the extent the damage is attributable to such person based on his own fault and the circumstances.

[2] The plaintiff may sue several participants jointly for the total damage and request that the judge set the liability of each individual defendant in the same proceeding.

[3] The recourse to several participants shall be determined by the judge considering all circumstances.

D. Statute of limitations

Art. 760

[1] The claim to compensation for damages against any persons responsible according to the above provisions is barred after five years calculated from the day the injured party received knowledge of the damage and of the person liable, but in any case after expiration of ten years calculated from the day of the act causing the damage.

[2] If the claim stems from a criminal act for which the criminal law provides for a longer statute of limitations, the latter is also valid for the civil claim.

E. Credit and insurance cooperatives

Art. 827

The provisions of the Corporation Law regarding responsibility shall apply by analogy to the responsibility of persons participating in the founding of the company or of those entrusted with the management, the auditing, or the liquidation.

Art. 920

In the case of credit and licensed insurance cooperatives, responsibility is governed by the provisions applicable to corporations.
Merger Law

Conclusion of the merger contract

Art. 12

[1] The merger contract must be concluded by the supreme managing or administrative bodies of the merging companies.

[2] It must be in written form and must be approved by the general meeting, or by the partners of the merging companies respectively. (Art. 18).

Demerger contract and demerger plan

Art. 36

[1] If, by demerger, a company transfers parts of its assets and liabilities to existing companies, the supreme managing or administrative bodies of the companies involved shall conclude a demerger contract.

[2] If, by demerger, a company intends to transfer parts of its assets and liabilities to companies that will be newly established, its supreme managing or administrative body shall prepare a demerger plan.

[3] The demerger contract and the demerger plan must be in writing and must be approved by the general meeting (Art. 43).

Establishment of the conversion plan

Art. 59

[1] The supreme management and administrative body shall establish a conversion plan.

[2] The conversion plan must be in written form and must be approved by the general meeting, or by the partners, respectively, according to Article 64.

Conclusion of the transfer contract

Art. 70

[1] The transfer contract shall be concluded by the supreme managing or administrative bodies of the subjects participating in the transfer of assets and liabilities.

[2] The transfer contract shall be in written form; if parcels of real estate are transferred, the respective parts of the contract require a public deed. A single public deed shall also be sufficient even if parcels of real estate are located in different cantons. The public deed shall be issued by a public official at the domicile of the transferring subject.

Art. 108

1 All persons involved in the merger, the demerger, the conversion, or the transfer of assets and liabilities shall be liable towards the subjects as well as towards all individual partners and creditors for damage they cause by intentional or negligent violation of their duties. The responsibility of the founders remains reserved.

2 All persons involved in the examination of the merger, demerger, or conversion are liable towards the subjects as well as towards the individual partners and creditors for damage they cause by intentionally or negligently violating their duties.

3 Articles 756, 759, and 760 of the Code of Obligations shall apply. In the case of bankruptcy of a company with stated capital or a cooperative, Articles 757, 764, paragraph 2, 827, and 920 of the Code of Obligations shall apply by analogy.

4 The responsibility of the persons who act for an institution under public law is governed by public law.

Penal Code

Punishability

Art. 100^{quater}

1 A crime or offense shall be attributed to the enterprise if committed while it exercises a business activity within the scope of the enterprise and if, due to the deficient organization of the enterprise, such act cannot be attributed to a natural person. In such case, the enterprise shall be punished with a fine of up to 5 million francs.

2 In the case of a punishable act according to Articles 260^{ter}, $260^{\text{quinquies}}$, 305^{bis}, 322^{ter}, $322^{\text{quinquies}}$, or 322^{septies}, the enterprise shall be punished independently from the punishability of natural persons if the enterprise is accused of not having taken all necessary and reasonable organizational measures to prevent such offense.

3 The judge shall set the fine in particular based upon the seriousness of the offense and the seriousness of the organizational deficiency and of

the damage caused, as well as upon the economic capability of the enterprise.

[4] Enterprises in the sense of this Title are:

a. legal entities under private law,
b. legal entities under public law with the exception of regional corporations,
c. companies,
d. sole proprietorships.

International Private Law

III. Governing law
1. Principle

Art. 154

[1] Companies shall be subject to the law of the state the law of which governs their organization, provided they fulfill the publicity or registration provisions of such law or, in the absence of such provisions, provided they are organized in accordance with the law of that state.

[2] If a company does not fulfill these prerequisites, it shall be subject to the law of the state in which it is actually managed.

IV. Special connection factors
1. Claims arising out of the public issue of equity and debt instruments

Art. 156

Claims based upon the public issue of equity and debt instruments by means of prospectuses, offering memoranda and similar notices may be asserted either under the law governing the company or under the law of the state in which the issue took place.

4. Liability for foreign companies

Art. 159

If the activities of a company founded under foreign law are managed in or from Switzerland, the liability of the persons acting in its name shall be subject to Swiss law.

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References are to the numbered paragraphs.