SIX

Securing Fair and Transparent Protection Offered by the Swiss Takeover Rules Through Being Listed on SIX

If a company lists its equity securities on a foreign exchange, this may have far-reaching implications with respect to takeover protection. The Swiss takeover rules only apply to companies respectively equity securities that have a primary listing on a Swiss exchange. Subsequently, a Swiss incorporated company being listed on a foreign exchange may be vulnerable to unsolicited takeovers.

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The Scope of the Swiss Takeover Rules

The Swiss takeover rules apply to Swiss and foreign companies whose equity securities have a primary listing on a Swiss exchange. Securities that are traded over-the-counter (OTC), debt instruments such as bonds (unless combined with options or convertible rights) or a merger through the exchange of equity securities do not fall within the scope of the Swiss takeover rules. In addition, the Swiss takeover rules stipulate that if a person (or a group of persons acting in concert) exceeds the threshold of 33⅓%[1] of the voting rights in a company, that person must make a public tender offer for all shares of that company. The offeror is further required to treat all shareholders of the target company equally.

The Negative Conflict

If a Swiss company lists its equity securities on a foreign exchange and assuming that the respective foreign law is limited to local companies only, the foreign takeover rules and the Swiss takeover rules do both not apply. Where foreign law is not applicable to foreign companies, a negative conflict of competences occurs. This may place a Swiss company in a defenseless situation in case of an unsolicited takeover and/or diminishes the negotiation power of the owners or the Board of Directors of the company in a Merger & Aquisition context. A negative conflict situation also generates legal uncertainties for all involved parties and could result in lengthy and costly legal proceedings.

The US Example

In the US, takeover laws are a matter of company (state) law and not of (federal) securities law. Therefore, if a Swiss company is listed on a US exchange and is subject to an unsolicited takeover bid, US law assumes that Swiss law makes it possible for a Swiss company to take adequate measures to protect its own interests and to guarantee freedom of choice and equal treatment to its shareholders. However, this is not the case as the takeover protection in Switzerland is a matter of securities law and not of company law (see also "The Scope of the Swiss Takeover Rules") and consequently, a negative conflict situation may occur (see also "The Negative Conflict"). Further, certain traditional US defense mechanisms (e.g. supermajority shareholder vote) are unavailable under Swiss company law and other mechanisms (e.g. poison pills) can only be imperfectly implemented.

Last but not least, it is hardly tested if such other defense mechanisms are also proven to secure the intended defense in front of Swiss or US courts.

A Negative Conflict Case Study

In 2010, Novartis exercised a call option to buy from Nestlé a stake of around 52% in Alcon[2] (increase of ownership to around 77%). Subsequently, Novartis wanted to merge with Alcon and made an offer to the minority shareholders of Alcon to receive Novartis shares in return. The merger met resistance from the Alcon minority shareholders and from its independent members of the Board of Directors. A class action was filed in the US which was subsequently dismissed due to a lack of jurisdiction in the US. As a consequence, the independent members of the Board of Directors set up a litigation trust with the aim that the Alcon minority shareholders receive equal and adequate terms. Finally, Novartis compensated the minority shareholders with the same price (in shares and in cash) as it paid for its stake purchased from Nestlé.

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[1] The Swiss takeover rules allow companies to opt-up (e.g. to a threshold of 49%) or to opt-out entirely from the mandatory offer regime by providing so in their articles of association. As per October 2018, 72 companies listed on SIX had made use of this option.

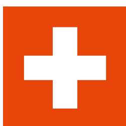
[2] Swiss incorporated company whose equity securities were listed on the NYSE.

What Are the Mitigating Choices?

Possible mitigating choices for a Swiss company being listed on a foreign exchange include:

A Risk Mitigating Case Study
In the beginning of 2017, the Geneva-based life science company ObsEva listed its equity securities on the NASDAQ and subsequently maneuvered the company in a potential negative conflict situation. Mid-2018, ObsEva conducted a dual primary listing on SIX and stated in public that one of the reasons why the company lists its equity shares on SIX was "to secure for its shareholders the protection offered by the Swiss takeover rules".

1. Restrictions
A company can try to prevent undesired influence from its shareholders by introducing share transfer or voting rights restrictions in its articles of association, or by creating dual classes of shares. Such mechanisms may however have unintended collateral effects, as they tend to be unpopular with shareholders.



3. Swiss Exchange Listing
A company can list its shares on a Swiss exchange, on top (or in replacement) of its foreign listing, to create the Swiss exchange listing required by the Swiss takeover rules. Such an additional Swiss exchange listing will be treated as a main listing for Swiss law purposes, as a secondary listing is only possible for foreign companies.

2. Voting Rights
Some companies try to replicate certain US takeover devices in their articles of association, by providing that any shareholder who acquires shares above a specified threshold can only exercise its voting rights if it submits an appropriate offer (under terms specified in the articles of association) to all shareholders or, alternatively, by making business combinations between an acquirer and the company subject to shareholder approval with high majority requirements. These restrictions are, however, complex and largely untested in practice.

Concluding Thoughts

The main requirement that the Swiss takeover rules apply is a primary listing on a Swiss exchange. If a Swiss company lists its equity securities on a foreign exchange, it accepts that it potentially enters into a negative conflict of competence situation and that a takeover situation may not be governed by any takeover laws and rules. This risk and potential consequences must be considered while a Swiss company evaluates the exchange for its IPO.

> **"In practice, the uncertainties surrounding the enforceability of takeover mechanisms that rely solely on provisions in the articles of association create a strong incentive for Swiss companies confronted with potential takeovers to consider listing their shares in Switzerland."**

Jacques Iffland, Partner, Lenz & Staehelin

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SIX Swiss Exchange Ltd
Pfingstweidstrasse 110
P.O. Box
CH-8021 Zurich

Primary Markets
T +41 58 399 2245
primarymarkets@six-group.com
www.six-group.com/primarymarkets

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