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Real Estate in Switzerland

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by

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Abbreviations

This text uses the following abbreviations:

ATF	Official Collection of the Decisions of the Swiss Federal Supreme Court (German citation: *BGE*)
CA	Swiss Copyright Act (German citation: *URG*)
CC	Swiss Civil Code (German citation: *ZGB*)
CO	Swiss Code of Obligations (German citation: *OR*)
F CPC	Federal Civil Procedure Code (German citation: *BZPO*)
FDTL	Federal Law on Direct Taxes (German citation: *DBG)*
FLH	Federal Law on Harmonization of Taxes (German citation: *StHG*)
LDCB	Federal Law on Debt Collection and Bankruptcy (German citation: *SchKG*)
OFJ	Federal Statute on the Organization of the Federal Judiciary (German citation: *OG*)
PA	Swiss Patent Act (German citation: *PatG*)
PIL	Federal Private International Law Statute (German citation: *IPRG*)
SJZ	*Schweizerische Juristenzeitung*
TA	Swiss Trademark and Denominations of Origin Act (German citation: *MSchG*)
VAT	Value Added Tax (German citation: *MWSt*)
ZH COC	Code on the Organization of the Courts of Zurich (German citation: *GVG*)
ZH CPC	Civil Procedure Code of Zurich (German citation: *ZPO*)
ZR	*Blätter für Zürcherische Rechtsprechung* (Official Collection of Decisions of the Courts of Zurich)

A. Introduction

It was Ralph Waldo Emerson who said that "if a man owns land, the land owns him". Property has had mixed reviews over the years. In an inflationary period, politicians rail against speculators. In a deflationary environment they complain about negative equity. Tax privileges for property owners are constantly being debated (and seemingly never resolved).

Land has always had not just a political element to it but also an emotional one. On the one hand, the holding of land has always been an expression of status in a society and, at times, of independence. People still talk today of an Englishman's home being his castle (however different the reality is). Land, and the buildings that stand upon it, is by its very nature part of the make-up of the nation. In Britain, great importance is attached to the home-owning democracy. In Switzerland detailed rules have been introduced to prevent non-residents buying real estate. Only recently government proposals to ease the restrictions have been rejected by the electorate, and this has become a key problem in resolving the bilateral EU/Switzerland trading relationship currently being negotiated.

Swiss land law is very different to its British counterpart. It is in many respects more current than in Britain. "Flying Freeholds" are still at the planning stage in Britain; they exist under Swiss Law. Interestingly, land law itself is predominantly federal and not cantonal, although many procedures as well as taxation are regulated on a cantonal basis. Whilst this has no parallel in Britain, the most obvious distinction between the two legal systems is the concept of equity. In Britain, equity and land law developed hand in hand; in Switzerland a concept of equity does not exist. This perhaps explains the more regularised legal environment. Swiss law legislates to be fair whereas British law has, traditionally, left fairness to the judges.

Real estate law is one of the oldest elements of domestic law in many jurisdictions. Its development as a specific part of the legal system, with its own rules, has generally been recognized in most jurisdictions, although an American President earlier this century (Calvin Coolidge) boldly stated that "ultimately property rights and

personal rights are the same thing". As a lawyer he was probably being provocative. Of course he was wrong. As this and countless other publications have shown, they are not.

We first discussed producing this booklet before the vote last year on the relaxation of *Lex Friedrich* (the law restricting ownership of real estate in Switzerland by non residents). We assumed that the changes would be accepted (having the backing of all of the main political parties and the cabinet) and thought that a publication in English stating the revised legal position would be urgently needed. The Swiss voters thought otherwise, however, and the proposal was rejected. Ironically therefore, although the availability of property in Switzerland is still restricted, the restrictions still need elucidation. Moreover property is still being bought and sold, and so this booklet retains its relevance.

Peter Hänseler and Daniel Hochstrasser have produced an excellent and concise review of Swiss land law. The British Swiss Chamber of Commerce is proud to be associated with this venture. We are much indebted to the Swiss law firm Bär & Karrer and particularly to Nedim Peter Vogt, the *eminence grise* of the project.

Howard Rosen

Vice President,
Chairman, Legal & Tax Chapter
British Swiss Chamber of Commerce
Zug, July 1996

B. Interests in Land and Their Protection

1. Preliminary Remarks

Property law in Switzerland is governed by comprehensive regulations contained in the Federal Swiss Civil Code[1] (hereinafter referred to as "CC"). In addition, the private law aspects of transactions involving property are governed by the Federal Code of Obligations[2] (hereinafter referred to as "CO"). These two statutes constitute the federal codification of Swiss private law. The cantons have retained only very limited legislative powers in that area of the law. This, however, contrasts with other areas, especially insofar as procedural and tax matters are concerned, as will be demonstrated in the respective chapters hereinafter.

2. Ownership

a) Sole Ownership

Sole Ownership (*Eigentum/propriété*)[3] is the most common and frequent form of legal title in land. The sole owner has complete control over the land and buildings which he owns, subject only to general restrictions imposed by law or rights of third parties. His rights are in most aspects identical to those of an owner in fee simple as defined in common law. The rights of a sole owner of land include the space above and below the surface of the land, including in particular all buildings on that land. He is not entitled, however, to prevent any interference above or below his land, if his legitimate interests are not affected.

[1] *Zivilgesetzbuch/Code Civil Suisse.*
[2] *Obligationenrecht/Code des Obligations.*
[3] Art. 641 et seq. CC.

b) Joint Ownership

Joint Ownership (*Gesamteigentum/propriété commune*)[4] is ownership by several persons based on a special legal relationship among these persons, such as marriage, community among heirs or partnership. The rights and duties of these persons are governed by the provisions applicable to the institution upon which their relationship is based. In the absence of any contrary regulation, they may only dispose of the property unanimously. Due to the fact that joint ownership exists only in specially defined cases, it is of limited importance.

c) Co-Ownership

Co-ownership (*Miteigentum/copropriété*)[5] exists in all other situations where property is owned by more than one person or legal entity. In the absence of contrary regulations, co-owners own equal share of the property. Each co-owner has the same rights and duties of any (sole) ordinary owner for his share of the property, and may therefore convey or encumber that share without the consent of his co-owners. However, a co-owner's right to use his share is limited by the rights of the other co-owners, which must be respected. The applicable statutory provisions contain detailed regulations on the relation between co-owners, governing, in particular, the decision-making process in the management of the property in the absence of a specific agreement among the co-owners. A distinction is made between (i) regular management activities, in which every co-owner is entitled to participate, (ii) important, necessary and useful management activities, which need the consent of the majority of the co-owners, who must represent at least half the interest in the property, and (iii) those actions that serve only cosmetic and comfort purposes, which must be based on a unanimous decision. The Civil Code also provides for the possibility of the exclusion of a co-owner; such exclusion must be sought with the competent judge, who has the power to order a co-owner to sell his share if he finds that the behaviour of that co-owner amounts to such violations of his duties that the other co-owners cannot reasonably be expected to tolerate such violations any longer.

[4] Art. 652 et seq. CC.
[5] Articles 646 et seq. CC.

d) Condominium

The ownership of one apartment or one floor in a building, similar to condominiums under U.S. law, is governed by special regulations (*Stockwerkeigentum/propriété par étages*)[6]. Under these provisions, the owners of a condominium are co-owners of the land and have the right to the exclusive use of a particular part of the building as sole owners. The provisions of Article 712 CC regulate in detail the rights and duties of the parties, especially insofar as maintenance of the building is concerned. However, as far as that part of the building in co-ownership is concerned, the relevant provisions of co-ownership apply analogously.

e) Legal and Beneficial Ownership

Beneficial ownership cannot be based on property law provisions, because Swiss law does not know a legal principle comparable to the common law concept of trust. Any beneficial ownership is therefore of a purely contractual nature, which means, in particular, that the right of the beneficiary is not based on an *in rem* title to the property, but only on a contractual claim against the holder of the property rights. If that holder disposes of the property in violation of the contractual provisions, the beneficiary is limited to a claim in damages. Although a purchase of property on a fiduciary basis is considered to be valid, such fiduciary purchase is void where the parties intended to circumvent legal provisions; this may especially be the case if a non-resident foreigner intends to acquire property without having the necessary permit[7]. A common method of acquiring a beneficial interest in land is by purchasing shares or the majority of shares in a real estate company; the ownership of the property in an economical sense is transferred simply by conveying the shares of the company owning the property.

[6] Article 712 CC.
[7] See *infra*, chapter M.

3. Restrictions on Ownership of Land

The most important restrictions on ownership of land presently in force concern foreign persons or entities dominated by foreigners (see chapter M). Otherwise, there are few legal restrictions on land ownership. Minors and mentally incapacitated persons may be owners of land, but their rights must be exercised by their legal representatives according to the applicable provisions of the Civil Code.

4. Restrictions on Disposal of Land

There are specific statutory restrictions on the disposal of land by entities under public law. They are described in more detail in chapters L and M hereinafter.

5. Possession

A person who has property under his control, whether or not he is the actual owner of that property, is considered to be in possession[8] (*Besitz/possession*) of that property. Possession entitles that person to certain legal advantages which are particularly important in the context of chattel; however, due to the rather limited importance of the concept of possession in connection with real property, it will not be discussed in any further detail herein.

6. Servitudes and Easements

The owner of real property may agree with any third party (very often the owner of an adjacent plot of land) to a servitude or easement in favor of that third party or property as described in the Civil Code. To be valid and enforceable some types of servitudes are required by law to be not only in the form of a written agreement (*causa*) and notarized but are also required to be registered in the file of the relevant

[8] Articles 919 et seq. CC.

property in the land register[9]. The following most important types of servitudes are defined in the Civil Code:

a) Usufruct

Usufruct (*Nutzniessung/usufruit*)[10] conveys to the beneficiary the right to possess and use the property, including its fruits, but not to dispose of it in such a manner that could adversely affect the substance of the owner's core ownership rights. Its term is limited to a maximum period of 100 years.

b) Right of Residence

A right of residence (*Wohnrecht/droit d'habitation*)[11] entitles the beneficiary (which must be a person) to occupy a building or an apartment for residential purposes. The right of residence is not transferable and cannot be inherited; however, in the absence of contrary regulations, such right may be extended to the beneficiary's family.

c) Right to Build

A right to build (*Baurecht/droit de superficie*)[12] entitles the beneficiary to construct buildings on the property in accordance with an agreement between the parties and to possess and enjoy it for a definate period of time, which may be up to 100 years. The right is – in the absence of a contrary agreement – transferable and inheritable. Any agreement which establishes a right to build must be in writing and notarized. Upon expiration of the term, any existing buildings belong to the owner, who is obliged to pay the beneficiary a reasonable price for those buildings. The parties may (and mostly do) agree on a method of determining that price when they establish the right to build. The right to build has gained significance in recent years as an

[9] Articles 731/732 CC; see *infra* C.1.
[10] Articles 745 et seq. CC.
[11] Articles 776 et seq. CC.
[12] Articles 779 et seq. CC.

increasing number of communities have used it as a means of offering undeveloped land under favorable conditions to the public for the construction of residential housing or to start new businesses. The fact that the land was not sold but only a right to build, granted usually for 99 years, gave the communities the right to exercise greater influence on the character of the construction projects than if they had sold it. In addition, there is a strong policy argument made against the irrevocable sale of publicly owned land to private entities.

7. Restrictions on Use and other Restrictions

The owner's freedom to use his property in whatever manner he wishes is, in addition to the servitudes or easements as discussed *supra*, restricted by (i) public law provisions such as zoning and building laws, sanitary and safety regulations, and (ii) the provisions of the Civil Code regulating the relations between neighbouring properties[13]. These provisions govern issues such as the restrictions placed on activities which result in amount to an unreasonable interference on adjacent properties, plants, wells and water, rights of passage etc.

8. Private Mortgages

With respect to providing security for loans by mortgaging property, the Civil Code provides for two slightly different types of mortgages, namely the actual mortgage *per se* (*Grundpfandverschreibung/hypothèque*)[14] and the mortgage note (*Schuldbrief/cédule hypothecaire*)[15]. Both types are discussed in more detail in chapter I.

[13] Articles 684 et seq. CC.
[14] Articles 824 et seq. CC.
[15] Articles 842 et seq. CC.

9. Public Rights and Charges

It is sufficient to mention here that public authorities are entitled to impose a statutory mortgage on a property in cases of non-payment of taxes and/or fees. The Registration of such a mortgage is, however, not a requirement for validity, as it is for any other mortgage.

10. Options and Pre-Emption Rights

Options to buy or repurchase (*Kaufsrecht, Rückkaufsrecht/droit d'emption, droit de réméré*)[16] or the right of pre-emption (*Vorkaufsrecht/droit de préemption*)[17] can be registered in the land register and thus acquire *in rem* character. The fact that they are registered renders them enforceable against any later transaction, whether that transaction has already been entered into the register or not. For the law applicable to such contracts, see the applicable provision, Article 216 CO.

11. Leases

Lease contracts may be entered in the land register only upon mutual agreement of the parties[18]. Such an entry has the effect of binding any subsequent acquirer to the provisions of the lease contract and he, therefore, cannot claim that the acquisition of the property has had an effect on the lease such as giving him any special (additional) rights which he may otherwise have had, vis-à-vis the existing tenant (see *infra* chapter E).

[16] Article 683 CC.
[17] Article 681 CC.
[18] Article 261 (b) CO/Article 959 CC.

C. Title to Land

1. Land Register

In Switzerland, all plots of land must be surveyed and details recorded on cadastral maps. Cadastral units are pieces of land which are registered under a certain plot number in the land survey register, which is kept by the cantonal authorities responsible. These authorities are also responsible for surveying the land and for determining the boundaries of individual plots.

Every distinct piece of land has its own file in the land register (*Grundbuch/registre foncier*), which must have the following information recorded: Ownership; easements and usufructs; rights of pre-emption and options to buy or repurchase; land charges granting a right to recurrent payments or services to the beneficiary; priority notices; leases; mortgages; order of priorities of rights.

For the provisions governing the maintenance of the land registers, see Article 942 et seq. CC and, more specifically, the more detailed Federal Regulation (*Grundbuchverordnung/ordonnance sur le registre foncier)*. The law of the (individual) cantons determines the authorities which are responsible for maintaining the registers and their respective area of responsibility.

2. Proof of Title

There is a legal presumption that the entries in the land register are true and correct[19]. If there is a false entry in the land register or if for any reason an entry is incomplete, any party relying in good faith on such entry is fully protected. As far as that party is concerned, the only encumbrances which exist are those registered in the land register and ownership is deemed to lie with the person registered therein.

[19] Articles 971 et seq. CC.

3. Passing of Title

Transfer of ownership of land is effected only by the registration of the new owner in the land register. The prerequisite for registration is a notarized agreement between the seller and the purchaser, which constitutes the underlying legal ground (*causa*) for acquisition of ownership or any other rights *in rem* on real property. Only such an agreement grants an obligatory right of entry into the land register. In exceptional cases, the entry in the land register has mere declaratory function, where, for instance, the ownership is acquired *ipso iure*, such as in cases of hereditary acquisition, transfer by judgement or transfer in a debt collection and enforcement procedure under the applicable provisions of the Federal Statute on Debt Collection and Bankruptcy (*Schuldbetreibungs- und Konkursgesetz/Loi fédérale sur la poursuite pour dettes et la faillite*).

4. Adverse Possession

The concept of acquisitive prescription creating title in the possessor after a certain period of time has very limited practical importance due to the existence of the land register. Nevertheless, there are provisions in the Civil Code (*Ersitzung/prescription*)[20] that grant ownership to a non-owner, who is listed in the land register, as owner in good faith after a period of 10 years if there has been no challenge as to this person's ownership. If a person has been in possession of a plot of land for a period of 30 years and the owner of such plot is not listed in the land register or is dead, then this person may request a court to order the entry of his name in the land register as owner.

[20] See Articles 661 et seq. CC.

D. Transactions in Land

1. Types of Transaction

The most common transactions in respect of real property under Swiss law are the sale and purchase of land, the granting of a building right, and the creation of a mortgage in favor of a bank.

2. Procedures and Formalities

a) Contract

Contracts for the transfer of ownership or any other *in rem* rights in real property must fulfil strict formal requirements as a prerequisite for their validity: Such contracts must always be in writing and require, in most cases, public authentication (transfer of ownership, establishment of servitudes, rights of residence and building rights etc.). Such authentication can only be made by notaries who have been so empowered under the laws of the canton in which the relevant property is situated. While some cantons recognize only acts authenticated by the official notary public of the district in which the property is located, other cantons provide for more liberal solutions.

b) Enquiries and Searches

Due to the existence and legal implications of the land register, a potential purchaser can obtain most of the required information about a particular tract of land from the relevant file. Any further enquiries must focus on information that can not be obtained from the file (see *supra* chapter C). If the construction of buildings is intended, the prospective buyer should endeavour to ensure that the planned construction and use of the buildings is in conformity with the applicable zoning and building laws and other regulations of public law (see *infra* chapter N).

c) Transfer and Completion

With the exception of circumstances that are specifically mentioned in the Civil Code, any transfer or granting of *in rem* rights is effected by the registration of the new situation in the land register.

3. Fees, Costs and Taxes

The fees charged by the land register authority for the registration of transactions in the land register vary from canton to canton. They are usually calculated either as a percentage of the sales price or the objective value of the transferred right and may range between 0.1% and 0.3% of the market value or be a flat fee of approx. CHF 100 to CHF 10'000 per transaction, taking into account the value of the transferred right and/or the necessary paper work connected with the registration.

4. Contract Terms

a) Warranties

Very often contracts contain a disclaimer to all warranties, so that the purchaser is left with the statutory warranty provisions contained in the Code of Obligations, which cannot be waived[21].

b) Deposit

It is common practice for the purchaser to pay a small percentage of the purchase price at the signing of the declaration of intent, which precedes the actual signing of the actual (sale and purchase) contract in front of a notary public. The declaration of intent usually contains a provision which permits the seller to keep this amount in the event that the transaction cannot be completed due to circumstances for which the purchaser is responsible, e.g. if he cannot obtain sufficient financing for the acquisition.

[21] See *infra* 4.h and i.

c) Payment of Price

The entire purchase price usually becomes payable at the time the transaction is registered in the land register; such payment might be made by a certified bankers' check, or by the confirmation of a bank that it has taken over certain loan or loans secured by a mortgage(s) on the property and thereby releasing the seller from its obligations towards the bank which granted those loans.

d) Timetable

The time required between the date the parties agree on the transaction, the signing of the contract and the entry of the transaction in the land register varies depending mainly on the workload of the notary public (who in some cantons is also the keeper of the land register). It is therefore rather difficult to make a reliable statement. However, a time-frame of about four weeks for the completion of the whole transaction would be reasonable.

e) Default

The seller has the right to attach a statutory mortgage on the property sold for the amount of the purchase price so long as he has not received full payment; he must file a request for registration of that mortgage within three months after the transfer of the ownership[22].

f) Interest and Penalties

In cases where the purchaser assumes the obligations arising from an existing loan which has been secured by a mortgage on the property (which is a very common form of payment of at least part of the purchase price), the purchaser is liable for the interest payments starting from the date he is entered as owner in the land register. If the transaction cannot be completed due to circumstances for which one of the parties is responsible, the other party may be entitled to damages under the general provisions of the Code of Obligations or to liqui-

[22] Articles 837 et seq. CC.

dated damages, if this has been agreed up on in the declaration of intent.

g) Possession, Completion, Risk and Insurance

The purchaser is entitled to assume possession of the property as soon as he is entered as the new owner in the land register. At this point, the transaction is considered to be completed. In the absence of any contrary provisions in the contract, the risk passes to the purchaser on the date he is given possession of the property. The protection by the mandatory and government-owned building insurance which exist in most of the cantons, is not affected by the transaction; the new owner becomes liable for its premiums from the date the transaction is completion.

h) Physical Defects

Claims for physical defects of the property must be brought against the seller within five years after the closing of the transaction. Exclusion and limitation of liability clauses are valid only if the seller did not deceive the purchaser as to defects.

i) Title Defects

The land register protects a purchaser's good faith, that is, the trust he places in the entries made into its files, so that ownership or title defects are no longer an issue so long as a purchaser has exercised (reasonable) care in verifying the identity of his contract partner. Once the purchaser is registered as owner in the land register, he is protected from any claims of third parties so long as such claims were not listed in the land register alleging any overriding right in the property.

5. Protection of Contract Prior to Completion

a) Generally

As long as a contract on a transaction of real property is not notarized, it is not valid as such, and does not entitle the intended purchaser to

any specific performance, i.e. the transfer of ownership. Only if there is a notarized agreement, can the purchaser, in the event that the seller refuses to comply with his duty to effect the transfer in the land register, request a court to order the relevant land register to inscribe the purchaser as the new owner. In all cases where this is not possible, the purchaser is limited to damages based on principles such as *culpa in contrahendo*.

b) Registration

Parties considering or negotiating a transaction in real property may agree on an option to buy or repurchase (*Kaufsrecht, Rückkaufsrecht/ droit d'emption, droit de réméré*)[23] or a right of pre-emption (*Vorkaufsrecht/droit de préemption*)[24]. Such rights can be registered in the land register and thus acquire *in rem* character.

6. Professionals, their Roles and Fees

a) Notary Publics

The notary public is needed for the mandatory notarization of the underlying contract in a transaction in land. His fee is determined by cantonal law, and may be calculated either as a percentage of the market value of the property, e.g. 0.1% of the market value, or as a flat fee, which usually ranges between CHF 100 and CHF 3'000 per transaction.

b) Estate Agents and Realty Brokers

Although estate agents and realty brokers play an important practical role, their involvement in a transaction is not a requirement. Brokerage contracts are governed by special provisions contained in the Code of Obligations (*Mäklervertrag/courtage*)[25], which lay down the essential duties of the parties to such agreements, especially when

[23] Article 683 CC.
[24] Article 681 CC; Article 216 CO.
[25] Article 412–418 CO.

and under what circumstances a broker is entitled to a fee. In some cantons, their fees are regulated by and set out in statutes, and usually lie between 1 and 3% of the contract price; they are slightly higher for undeveloped land than for houses and apartments. However, the parties are free to negotiate these fees when they enter into a brokerage agreement. In cantons without specific regulations, the judge has to decide on the brokerage fees in the absence of an agreement between/by the parties; fees of 2% of the purchase price for houses and 3% or more for building land are considered customary, with a tendency towards lower percentages in large transactions. The tariffs set by organizations such as the Swiss Association of Real-Estate Brokers (SVIT) are not binding, but are usually referred to in brokerage contracts.

c) Lawyers

For transactions in real property, the services of a lawyer are not absolutely necessary as such, because contracts for real estate are usually standard contracts that might just as well be drafted by a competent notary public. The involvement of lawyers may be important in cases there the intended use of the property requires development of the land; in such cases; here must be some certainty that the applicable zoning and building laws permit the intended use of the land. In addition, foreign persons or entities wishing to acquire real estate should, in any case, contact a lawyer first, due to the complex applicable legal provisions (see *infra*, chapter M).

E. Leases and Occupational Rights

1. Leasehold: The Rental Agreement

The granting of the right to occupy buildings or land over a certain period of time for residential or business purposes in return for the payment of consideration is governed by the provisions of Articles 253 et seq. CO on rental agreements (*Miete, bail*). Due to the fact that a large majority of Swiss residents (depending on the source between 60 and 70%) rent rather than own their apartment or house, the rental agreement is the single most important type of contract and thus very narrowly regulated by mandatory provisions and, as far as its termination and modification are concerned, strict formal requirements must be adhered to. As a detailed discussion of the (all) applicable provisions would extend beyond the scope of this overview, the following is only a brief outline of the more relevant provisions.

2. Usual Terms

a) Length

Rental agreements may either be concluded for an indefinite term, which is more common, especially for residential purposes, or a fixed term. If the rental agreement is made for an indefinite term, it can be terminated by either party giving the other party at least three months' notice with effect from the next local "customary date" for giving such notice. In most areas of Switzerland, such customary dates are at the end of each of the first three quarters, i.e. 31 March, 30 June and 30 September. For the notice to be effective, an official form must be used and sent separately to each spouse, if an apartment is occupied by a married couple; if these formal requirements are not observed, the notice of termination is void. If the rental agreement is concluded for a fixed term, it expires without any further formality. In both cases, however, the tenant may apply to the judge for an extension of the term of the lease (see *infra*).

b) Extension of Terms

A tenant has the right to be granted an extension of the term of the lease by the competent court at the place in which the property is situated if he can demonstrate that the termination would result for the tenant or his family in undue hardship, which cannot be justified when weighed against the interests of the landlord. The court has to take into account the circumstances of the case, especially the duration of the lease, the personal and financial situation of the parties, the landlord's need for the apartment for his own purposes and the local housing market situation. If the tenant seeks a second extension, he has to demonstrate that he undertook reasonable efforts to find an alternative apartment[26]. An extension is excluded only if (i) the tenant failed to pay the rent, (ii) the tenant violated his contractual duties, (iii) the tenant becomes bankrupt, or (iv) the contract was made expressly for a limited time only due to a planned demolition of the building[27]. The maximum extension is for a period of four years for residential leases and six years for business leases.

c) Renewal and Improvement Works

During the term of the rental agreement, the landlord has the duty to limit renovation works or carry them out in a reasonable manner so as to respect the tenant's interests. The rights of the tenant for a reduction in the rent and damages due to disturbances resulting from such works are reserved. During the notice period, the landlord may not carry out any renovation works. If the tenant wants to undertake any improvements of the rented property, he has to request the landlord for his written permission; otherwise, the tenant has to reinstate the former situation when he moves out of the property. If the landlord agrees and the tenant's works result in a substantial improvement of the property, the tenant is entitled to a reasonable remuneration for his work.

[26] Article 272 CO.
[27] Article 272 (a) CO.

d) Repair

Small repairs that form part of the regular maintenance of the property must be paid by the tenant, regardless of whether he is liable for the damages or not. The extent of this duty is determined by local customs; it would therefore be more expedient to define the scope of the tenant's duty to undertake such small repairs in the rental agreement. If there are other repairs to be made, the tenant has the right to request the landlord to either effect them or to reduce the rent and/or to pay damages. If the landlord refuses to comply, the tenant may terminate the rental agreement without notice, if residing in the apartment is no longer reasonably possible or carry out the repair at the landlord's costs, if the usability of the apartment is only reduced to a lesser extent[28].

e) Insurances

The tenant has no legal duty to provide insurance for the property. In order to safeguard himself against any claims, should he destroy or damage the property, it is nevertheless advisable for a tenant to take out a third party liability insurance.

f) Services and Service Charges

The communal fees and taxes attached to property may, depending on the applicable statute, be levied on the tenant as occupier of the property. It must be borne in mind, however, that such public fees entitle the public authority to inscribe a statutory mortgage on the property, which ultimately involves the responsibility of the owner of the property.

g) Rent

Rent for residential property is usually paid monthly in advance. It is common practice among professional real estate brokers in particular to request a deposit from the tenant at the beginning of the term,

[28] See Article 259 (a) and (b) CO.

which may not be more than three months' rent[29]. The rent according to commercial rental agreements might be payable quarterly, annually or semi-annually.

h) Indexation and Automatic Increase Clauses

Indexation is a very common feature for commercial rental agreements. It is only permissible, however, if the agreement is concluded for a term of at least five years and the parties have agreed on the official federal consumer price index. In the case of residential property, rent may only be increased by 4/5 of the increase of the consumer price index, and any decrease of the index must also be taken into account[30]. Clauses providing for automatic periodical increase in the rent are valid only if the agreement is concluded for at least three years, the increase is made only once a year, and is for a pre-determined amount in Swiss Francs[31].

i) Default and Remedies

Default in the payment of rent entitles the landlord to set a time-limit of at least 30 days for such payment combined with a threat of termination. If the tenant still does not make payment, the landlord may terminate the rental agreement with a 30-day notice (Article 257 (d) CO). Other violations of the rental agreement by the tenant entitle the landlord to terminate the lease by giving 30 days notice only if the violations are such that the landlord cannot reasonably be expected to accept a continuation of the agreement[32]. A termination based on default in payment and severe violation of the tenant's duties result in a forfeiture of the tenant's rights to request the court for an extension of the rental agreement[33].

Defaults of the landlord, especially with respect of his duty to carry out necessary repair work, will give the tenant the right to terminate the agreement.

[29] Article 257 (e) CO.
[30] Article 269 (b) CO.
[31] Article 269 (c) CO.
[32] Article 257 (f) CO.
[33] Article 272 (a) CO.

3. Rent Increase and Rent Reduction

The rent may be increased by the landlord under narrowly defined formal and quantitative requirements; with regard to the formal requirements, reference can be made to Article 269 (d) CO. The quantitative requirements laid down in Article 270 (b) CO in connection with Article 269 (a) CO state that an increase in the rent is only possible if the landlord can demonstrate that the increase is not excessive. An increase is not considered excessive if one or several of the following conditions are fulfilled:

(i) a rise in the mortgage interest rates,

(ii) a rise in the general costs for the landlord,

(iii) the rent is not comparable to other locally paid rent and requires adjustment,

(iv) the increase is intended to balance an earlier reduction, or

(v) the increase does not exceed the scope recommended by organizations representing the interests of landlords and tenants.

The tenant may dispute a rent increase before special semi-judicial authorities (*Schlichtungsbehörde/autorité de conciliation*), whose decisions may be challenged by an appeal to a competent cantonal court[34]. In the same proceeding, a tenant may also request a reduction of an excessive initial rent, if he can prove that he was either forced to enter into the underlying agreement by a personal emergency situation or that the landlord has made a substantial increased in rent compared to the preceding rental agreement for the same premises[35]. During the term of the rental agreement, the tenant may ask for a reduction in the rent if it can be shown that cost reductions result in an excessive profit for the landlord[36].

[34] Article 274 (f) CO.
[35] Article 270 CO.
[36] Article 270 (a) CO.

4. Privity of Contract and Estate

A rental agreement is an existing encumbrance for any purchaser of the property. The acquirer remains bound by the provisions of the rental agreement after the transfer of ownership, but he may, if he can show that he has a compelling need to use the property for his own purposes, terminate the contract in accordance with statutory notice requirements instead of the notice period as provided in the rental agreement. The acquirer may be held liable for any damages the tenant suffers as a consequence of the termination[37].

5. Rent Control

There is no *ex officio* rent control by public authorities. This function is exercised by the authorities and courts acting on motion of tenants, as described hereinbefore.

[37] See Article 261 CO.

F. Liabilities

1. Liability of Owner

The owner of land is liable (i) to neighbours for any damages suffered as a result of his exceeding any of his property rights[38] as well as (ii) towards third parties for damages and injuries caused by defects of the buildings on the property which are the result of faulty construction or lack of maintenance[39].

2. Occupier's Liability

There are no private law liabilities attached to the occupier of land. If, however, the occupier is the legal owner of buildings on the land, he may become liable under Article 58 CO for damages and injuries caused by defects of those buildings. Detailed discussion of this issue would extend beyond the scope of this publication. As far as tax liabilities and fees are concerned, those may attach to the occupier; one has to keep in mind, however, that the public authorities have the power to attach a statutory mortgage on the land so as to secure any such liabilities (see *supra* B. 9), which means that the land as such and thus the owner will ultimately be liable for such claims.

[38] Article 679 CC.
[39] Article 58 CO.

G. Finance

1. Sources

Banks are the most common source for financing the erection of buildings or acquisition of property. Due to the relatively stable increase rates in property prices in Switzerland since World War II, the investment of funds into real property is considered by banks to be the least risky form of investment. This almost non-existent risk exposure has resulted in a loosening of the applicable regulations governing banks so as to permit banks to extend loans, secured by real property with a very modest equity ratio. This enables banks to offer attractive interest rates for such loans, because they would only need to use a small part of their equity to cover those loans.

In addition to banks, changes in the legislation governing social security required employers to establish a pension fund scheme in which funds were deposited with insurance companies. This had the effect of such insurance companies ending up with large funds which had to be invested in a conservative manner. While they primarily chose to acquire property directly (which contributed to the booming market in the 1980's), the crash in real property prices resulted in a change in this policy, and thereafter, there has been an increasing tendency towards extending loans to individuals for the acquisition of real property. Another factor which certainly contributed to this change in policy were two enactments of the Federal Parliament designed to eliminate the harmful effects of the investment policy of insurance companies and pension funds on the real property market[40].

In order to better secure mortgage bonds, especially during the

[40] *Bundesbeschluss über Anlagevorschriften für Einrichtungen der beruflichen Vorsorge und für Versicherungseinrichtungen/Arrêté federale concernant des dispositions en matière de placements pour les institutions de prévoyance professionelle et pour les institutions d'assurance;*

Verordnung über die Bewertung der Grundstücke von Einrichtungen der beruflichen Vorsorge und von Versicherungseinrichtungen/Ordonnance concernant l'évaluation des immeubles des institutions de prévoyance professionelle et des institutions d'assurances.

phase of high mortgage interest rates in the early 1990's, it had once considered the establishment of so-called investment companies, which were to be, in essence, a pooling of a certain specified number of mortgages – for instance, a pool of about 300 to 400. This plan was, however, not realized, for the simple reason that such a structure would have amounted to a finance company, and therefore subjected to the provisions of the Swiss Banking Act. Such a company would have been required, other than comparable institutions in other countries, to have a certain amount of equity and to be able to prove a certain degree of liquidity, which would have led to prohibitive costs. Other solutions, such as the establishment of mortgage funds, were found to be impossible as it breached the regulations on investment funds. In any case, the decrease of the mortgage interest rates in 1993 and 1994 led to an abandonment of any efforts in that direction.

2. Loans

a) Residential Property Financing

The vast majority of Swiss residents acquiring real property obtain the necessary financing through a loan from a bank or an insurance company; the latter is a relatively recent consequence of Swiss insurance companies search for new types of investment for their funds. As a general rule, loans of up to 80% of the purchase price of the property will be granted, if the bank considers that price to reflect the reasonable market value of the property. Of the total purchase price, 65% will be granted as a loan secured by a first mortgage, and 15% as a loan secured by a second mortgage (for the difference between first and second mortgages, see chapter I.). The difference between the interest rates for these two loans is usually approximately 1%. In early 1994, loans secured by a first mortgage could be obtained at an interest rate of less than 5%. In the meantime, the interest rates have increased to about 5.5% (end of 1995). The purchaser of the property will, according to the above-mentioned figures, be required to contribute 20% of the purchase price from his own funds or other sources.

b) Commercial Property Financing

The financing for commercially used property is not fundamentally different from residential property. One major difference, however, is that, in addition to the market value of the property, the expected profit from the business for which the property is acquired is an important factor for the lender to take into account.

c) Variable Interest Rate Loans

Loans with variable interest rates are the most common form of loans secured by mortgages. The mortgage interest rate is determined by the leading Swiss banks, and, in recent years has ranged between 4.5% and 8%. The mortgage interest rate is influenced by factors such as the general interest rates, the situation on the real estate market, the inflation rate and the general economical parameters.

d) Fixed Interest Rate Loans

Influenced by some bad experiences of house owners in times of rising mortgage interest rates, more and more owners now prefer to take out fixed interest rate loans. Such fixed interest rate loans are usually available for a term of 3 to 6 years and start with a slightly higher interest rate as compared to variable interest rate loans. However, the advantage is that the owner is in a position to anticipate the payments to be make for the next few years.

e) Mezzanine or Mixed Funding

An attractive alternative solution for residential and commercial property owners is to combine variable and fixed interest loans in order to profit from the advantages of both types of loans.

3. Sale and Lease Back/Leasing

Leasing contracts as such are not regulated in the Code of Obligations, but are governed by the principles developed in practice and

case law. Although leasing has become a very common instrument for financing business activities, especially in the acquisition of expensive machinery with a limited life span, it is of lesser significance in the context of real property. Banks and specialized leasing companies have shown limited interest in the sale and lease-back transactions underlying leasing agreements. If real property is subject to leasing contracts, the provisions of such agreements usually provide that the lessee makes amortisation payments and is granted a purchase right after the expiry of the term of the agreement.

4. Other Types of Property Finance

As has already been mentioned, interest rates for loans secured by mortgages are in Switzerland usually more attractive than any other way of obtaining capital for the acquisition or development of real property. Business or tax considerations, however, may lead an owner or acquirer of land to the conclusion that it is more advisable to undertake a project not on his risk alone, but together with partners contributing equity and/or know-how. The possible structures of such collaborations are described in chapter H.

H. Property Investment and Investment Market

1. Type of Investor

A distinction must be drawn between private investors, i.e. persons or corporations investing their own personal fortune or equity, respectively, and institutional investors, i.e. corporations and similar entities that invest monies of third parties.

2. Investment Vehicles

Investment into real property is made either by natural persons, i.e. private persons acquiring the property for their own account, or corporations. The latter might acquire property either as an investment for its own business or account or, as in case of banks or insurance companies, as investment of the monies they have received from their clients. Due to the legal situation as described in chapter J, trusts and partnerships do not exist or are not well suited as vehicles for permanent investment into real property.

3. Types of Investment

As a consequence of the increasingly strict laws regulating rental agreements, investment in residential property today is less attractive than it used to be a few years ago. Nevertheless, luxury apartments in attractive neighbourhoods might still be interesting investments, if acquired at a reasonable price. The continuing boom of investment into industrial and office buildings throughout the 1980's led to a considerable over supply of such space and unoccupied buildings of that type on the market. Any further investment in new developments of such buildings is therefore not recommended at present. The same can be said about retail space, as long as it is not situated in very

attractive locations. As a consequence of the numerous regulations governing land used in the heavily subsidized Swiss agricultural at sector, investment in such land is not a viable investment for typical investors. The tourist sector is an area that still looks promising, i.e. hotels and other facilities which support tourism; the eventual liberalization of the statutory limits on acquisition of real property by non-residents (see chapter M.) will be a factor that plays an important role.

I. Security

1. Mortgages

The Civil Code provides for two slightly different types of mortgages, namely the actual mortgage (*Grundpfandverschreibung/ hypothèque*)[41] and the mortgage note (*Schuldbrief/cédule hypothecaire*)[42]. The main difference between these two types is that mortgage notes are negotiable instruments issued to name or bearer and may be transferred upon delivery, whereas mortgages can only be transferred upon written assignment. Under both types, the debtor remains personally liable for the secured debt, which becomes important in cases where the sale of the property does not result in full coverage for the debt.

2. Secured Liabilities

Mortgages may be used to secure any existing, future or contingent debt to the extent of the value of the property; mortgage notes may not be used to secure future debts. Included in the coverage are not only the principal amount but also any accrued interest and expenses for liquidation of the debt. The debtor need not be the owner of the property.

3. Debentures

Debentures (*Fahrnisverschreibung/hypothèque mobilière enrégistré*) are possible under Swiss law only for pledged chattel where the possession of that good is not transferred, but an entry is made into an official register. They are valid only where such registers are kept, i.e. for cattle, ships and aircraft, but cannot be applied to real property.

[41] Articles 824 et seq. CC.
[42] Articles 842 et seq. CC.

More specifically, the so-called "floating charges" over a general body of assets specifically charged, as commonly practised in the UK, are not possible under Swiss law.

4. Bonds and Guarantees/Other Security Transactions and Other Types of Security

In the context of real estate, any loan that is given in an amount beyond the market value of the property is considered to be a common commercial loan, subject to the rules and customs applicable to such loans. In addition to a mortgage on the property itself or, for that matter, on any other real property, loans may be secured by offering any other existing type of security. In that regard, the following might be briefly mentioned:

If the borrower owns any movable assets, he may pledge those in order to provide security for the loan agreement. The statutory regulations of Swiss law on pledges (*Faustpfand/nantissement*)[43] require the transfer of possession of the pledged assets to the creditor. This renders pledges of movables very unattractive for both creditor and borrower. Therefore, in practice, pledges are used only where the possession of the assets is easily transferred, for example where the assets are embodied in a negotiable title, but not where the actual possession of the assets is crucial for the running of for the owner's business, such as in the case of machinery. A very common form of pledges is the deposit of securities, share certificates or insurance policies with a bank. As an alternative, especially in the commercial sector, the debtor may assign receivables from his business to the bank. The willingness of a bank to accept such an assignment as security depends of course entirely on the quality of the borrower's creditors and the assigned claims.

If the entity who receives the loan does not have any assets which might be pledged in order to secure payment of the obligations arising from the loan agreement, the creditor may accept either a surety (*Bürgschaft/cautionnement*)[44] or a guarantee (*Garantie/porte-fort*)

[43] Articles 848 et seq. CO.
[44] Articles 492 et seq. CO.

instead as sufficient security[45]. Both of these are declarations of third parties who guarantee the performance of the debtor's duties under the loan agreement. The difference between these two forms of third party securities is that the guarantee is an unconditional undertaking of the guarantor, which is completely independent of the underlying transaction between creditor and debtor, and in fact creates an obligation of the guarantor to pay parallel to the obligation of the main debtor. A suretyship is an obligation to pay in case of default of the main debtor, which depends on the validity of the contract between creditor and main debtor. The surety is entitled to raise the same defenses as the main debtor against the creditor's claims. Whereas a suretyship is valid only if established in writing and, if provided by an individual, in a notarised agreement, a guarantee requires no special formalities. Due to the strict legal consequences of a guarantee, however, such a promise must be clearly ascertainable in order to be upheld by a court.

5. Protection of Security and Registration

As has already been mentioned (see *supra*, chapters I. 3 and 4) the registration of a mortgage in the land register is a prerequisite for its validity. This registration also determines the rank and priority of the mortgage in relation to any other existing mortgages on the same property (see *infra*).

6. Priority of Security

The priority of mortgages is determined by their fixed rank as determined in the land register. Usually, there is a mortgage in the first and a mortgage in the second rank (so-called first and second mortgages), the maximum amounts of which must also be recorded/mentioned in the register. A feature of the fixed rank system for mortgages is that even if a loan secured by a first mortgage is paid off, the second mortgage will not move up, but remains in the same second rank. This

[45] Article 111 CO.

being the case, the owner has the possibility of obtaining a new loan up to the maximum amount secured by the first mortgage.

7. Enforcement Procedures

In case of default of the debtor, the creditor whose claim is secured by a mortgage is entitled to execution against the property, including any accessories thereto. For that purpose, he has to start proceedings in accordance with the Federal Statute on Debt Collection and Bankruptcy (*Schuldbetreibungs- und Konkursgesetz/Loi fédérale sur la poursuite pour dettes et la faillite*) by obtaining payment order issued by the competent enforcement office, making specific reference to the mortgage. The debtor is granted a time-limit of six months to pay up, with the explicit warning that in case of non-payment there will be an execution sale of the mortgaged property by public auction. After the expiry of these six months, the creditor may request the execution within two years after the issuance of the payment order. The resulting amount from the ensuing public auction sale is, primarily used to cover the costs of the enforcement proceedings, and, thereafter distributed among the secured creditors in accordance with the amount of their claims (including interest and costs) and the rank of their rights. The remaining surplus (if any) will be given to the former owner. In order to avoid heavy losses which were a result of the modest proceeds (received) from an auction sale, banks used to take over the property from the owner, if they thought that they could obtain a better price by selling if they sold the property themselves; since this was often not the case and the banks were then left with real property they actually did not want, banks have departed from that practice in recent times.

J. Companies and Business Entities

In connection with the acquisition, development or ownership of real property, Swiss law offers various possibilities for the structuring of the legal relations between the parties to such a project. The most important vehicles are described in this chapter.

1. Corporations

a) Stock Corporation

The Swiss joint stock corporation (*Aktiengesellschaft/société anonyme*)[46] is the predominant legal vehicle for any type of business activity in Switzerland. It is the legal entity used by large public companies, by subsidiaries of multinational corporations, by joint ventures and also by small business units. It suits the requirements of foreign business interests the best. No special license is required to do business, except in such areas as banking, insurance, railways, etc. Among the main features of the stock corporation are that it is a legal entity distinct from its shareholders, carrying its own company name. Its shareholders are not personally liable for any of the liabilities of the company. The shareholders' only obligation is to pay in the capital to which they subscribed. Only exceptionally will courts pierce the corporate veil and allow creditors to satisfy their claims from the assets of shareholders. A stock corporation has a stated capital, which is divided into shares with a nominal value of at least CHF 10 each. The formation of the stock corporation is relatively easy. As a minimum, 20% of the share capital or at least CHF 50'000 must be paid in. In addition to the articles of incorporation, which can be drafted using standard forms, an incorporators' meeting in the presence of a notary public must be held where the incorporating shareholders declare their intent to form a corporation based on the articles they have agreed upon. The corporation comes into existence upon its registration in the commercial register, which is also published in the

[46] Articles 620 et seq. CO.

Commercial Gazette. In practice, the incorporation proceeding including registration will require anywhere between 15 and 25 days. The formation of a corporation triggers a 3% stamp tax on the consideration received by the company for the issued shares (which is often equal to the stated capital).

b) Co-operative Company

A co-operative company (*Genossenschaft/société coopérative*)[47] is an association which is similar to a stock corporation in some respects; the main differences are that its legal structure focusses more on the members' individuality and not on their capital contribution, and that its primary purpose is not to make a monetary profit, but to further or secure special economic interests of its members. A co-operative company does not have a pre-determined capital, because it is statutorily required to be accessible to new members. In practice, co-operative companies in Switzerland have an important role to play as vehicles used by individuals with similar interests with the goal of reducing prices for certain services or goods; they exist, e.g. in the agricultural field as sale or purchase organisations for farmers, or as (usually rather small) saving and loan banks. In the context of real property, residential building co-operative companies are formed to provide housing at reasonable prices for its members. The incorporation procedure for a co-operative company is *mutatis mutandis* identical to the formation of a stock corporation.

2. Partnerships

a) Ordinary Partnership

An ordinary partnership (*einfache Gesellschaft/société simple*)[48] is the association of two or more individuals based on a contractual agreement. It is formed without any special formal requirement. Its purpose is usually of temporary character, due to the fact that the ordinary partnership is not an independent legal entity, cannot be

[47] Articles 828 et seq. CO.
[48] Articles 530 et seq. CO.

entered in the commercial register and carries no firm name of its own. All partners remain jointly and severally liable for the liabilities of the ordinary partnership. As far as property is concerned, ordinary partnerships are formed only for construction projects, the time frame of which is limited.

b) General Partnership

A general partnership (*Kollektivgesellschaft/société en nom collectif*)[49] is an association of two or more individuals under a firm name, forming an independent legal entity based on a partnership agreement between the partners. Although general partnerships are not corporations, they can acquire rights and assume liabilities. Nevertheless, the partners' liability towards third parties is not limited.

c) Limited Partnership

A limited partnership (*Kommanditgesellschaft/société en commandite*)[50] is a general partnership in which (at least) one partner, the so-called general partner, is fully liable for the obligations of the partnership, whereas the other partners' liability may be limited. A limited partnership may also include corporations, but only as limited, and not as general partners.

3. Other Types of Business Associations

There is no Swiss equivalent to the United States concept of trust. Similar purposes are fulfilled by foundations (*Stiftung/fondation*)[51], fiduciary contracts and the like. The fact that the purpose of a foundation has to be laid down in a public deed and cannot, be altered or modified by the founder by any means, and that the foundation is under close supervision by a public authority, renders it unsuitable for investment in real property.

[49] Articles 552 et seq. CO.
[50] Articles 594 et seq. CO.
[51] Articles 80 et seq. CC.

4. Joint Ventures

There is no distinct body of Swiss law that specifically covers the formation or operation of joint ventures; accordingly, there is no statutory definition of the term "joint venture". Swiss law allows basically two forms for a joint venture: the contractual joint venture and the joint venture company. The formation of a partnership or a limited partnership for the purpose of a joint venture is usually excluded, because Swiss law requires that the general partners (not, however, the limited partners) be natural persons, whereas the partners of a joint venture are normally corporations.

a) Contractual Joint Ventures

Contractual joint ventures are subject to Art. 539 et seq. CO (*einfache Gesellschaft/société simple*), but the parties may contract out of most of those rules. Contractual joint ventures are chosen primarily in cases where no permanent structure is required or where flexibility is a key element for the success of a joint venture. Tax considerations may influence the decision as to the legal form as well. The advantages of a contractual joint venture are the informality of the formation procedure, the flexibility of its operation, the ease of termination, its lack of tax implications, its confidentiality and the low costs. The major disadvantage is that there is no limitation of liability for the parties involved, the lack of a permanent structure, and the limited ability to transfer the contractual interest. In addition, third parties usually prefer to deal with an independent legal entity rather than with several parties. A contractual joint venture is therefore recommended for short-term projects or projects which do not require a permanent structure only.

b) Corporate Joint Ventures

Joint venture companies under Swiss law are generally organized as stock corporations (see *supra* 1.a). They form an independent legal entity; the relationship between the incorporating parties is generally governed by a shareholders' agreement. The major advantages of a joint venture company are that it is an independent legal entity, which

enables it to enter into agreements and to acquire property, that the liability of the incorporating parties is limited to the amount subscribed as their share of the corporation's capital, and the transferability of the interest in the joint venture by sale of the shares. The major disadvantages are the higher costs, the formal procedure required to terminate the joint venture, the fact that the joint venture will be subject to taxes, as well as the lack of flexibility and secrecy due to the statutory disclosure requirements. Nevertheless, a corporate joint venture is usually selected for a joint venture in Switzerland whenever the activity intended is not of short-term nature the incurring of contractual relations to third parties.

K. Taxes

We would like to thank Peter Reinarz, tax lawyer of Bär & Karrer, for his valuable input for this chapter.

1. The Swiss Tax System in General

Switzerland has a strongly federalistic structure, which becomes evident also in its taxation system. While the levy of certain, primarily indirect taxes (VAT, stamp taxes, withholding tax on dividends and certain interest payments) is reserved to the federal government, other taxes – primarily the direct taxes on income and net worth – are levied not only by the federal government, but also at the levels of the cantons and the communes. In particular, special taxes on real property, transfers of real property and real property gains are levied by the cantons and communes only. The legislative power with regard to the cantonal and communal taxes generally lies with the legislative bodies of the 26 Swiss cantons. Although there exists a federal law aiming at harmonizing the cantonal tax laws in certain respects, in fact there is still a considerable variety of different cantonal tax systems and rules. The intercantonal harmonization law does not apply to real property taxes and real property transfer taxes and it does not include the rates of taxation. As a result, the income and capital/net worth tax burden as well as the special taxes on real property and transfers of real property vary considerably from canton to canton and even between the communes of one given canton.

Furthermore, the codified tax laws at the different levels (Confederation, cantons, communes) are not very detailed, as compared to the tax legislations of many other industrialized countries, which leaves a considerable amount of discretion to the tax administrations for the interpretation and application of the tax laws. These laws are open enough to allow the cantonal authorities, within certain limits, to negotiate and enter into special agreements and private rulings with individual and corporate taxpayers who are subject to their tax jurisdiction.

2. Taxation of Corporate Entities

a) In General

Swiss resident corporations are liable to federal, cantonal and communal taxes on their worldwide income and on their equity capital. The federal taxes of an ordinarily taxed corporation account for approximately one third and the combined cantonal and communal taxes for approximately two thirds of the total direct tax burden, depending on the canton and commune of residence. Income and capital attributable to a foreign permanent establishment or foreign real estate is exempt from Swiss taxes; it is, however, taken into consideration for determining the applicable tax rate (the corporate income tax rates are generally graduated, see below). A corporation is considered resident in Switzerland, if it is incorporated in Switzerland or, in the case of a corporation incorporated abroad, if it is effectively managed from Switzerland. Legal entities incorporated abroad are subject to Swiss income and capital taxes for their permanent establishments and real property maintained in Switzerland. Foreign partnerships and similar non-incorporated foreign business entities are, at least for federal tax purposes, taxed according to the rules pertaining to corporations. The concept of group consolidation is unknown in Swiss direct taxation.

The classical system of economic double taxation of the corporation and its shareholders still applies at the federal level and in most of the cantons. Accordingly, corporate profits are first taxed at the level of the corporation and, subsequent to their distribution, also subject to income tax in the hands of the shareholders. Corporate shareholders holding a substantial participation are, however, relieved from such double taxation and certain cantons (e.g. Nidwalden, Appenzell-Innerrhoden) do also provide for a similar relief to individual shareholders having their tax domicile in the same canton as the corporation.

Corporations are also subject to annual capital taxes on their net equity (paid-in share capital, surplus, retained earnings and those hidden reserves that have borne income tax). The federal capital tax is levied at a flat rate of .08%. The combined cantonal/communal capital tax burden may range from .05% up to 1%.

b) Corporate Income Taxes

(i) Federal Tax Level

Corporations are subject to federal income taxes on their worldwide net income, which includes, in particular, income from real property located in Switzerland and capital gains on such property. The federal corporate income tax rates are graduated, ranging from 3.63% to 9.8%, and apply to the net income *after* taxes (i.e., taxes are deductible expenses). The tax progression depend upon the profitability ratio between the net profit and the net equity. The maximum 9.8% tax rate applies if the ratio between the net income and the net equity exceeds 23.15%.

Any unrealized income, including unrealized gains on real property, generally must not be accounted for and is not included in the taxable income. On the other hand, financing costs and capital losses as well as depreciation on real property can be deducted as expenses. According to guidelines published by the Federal Tax Administration, no depreciation is generally allowed on the value of land. The standard depreciation rates for buildings range from 2% to 8% p.a., if the taxpayer uses the declining balance depreciation method, and to 1% to 4% if the straight line depreciation method is used. Losses of a fiscal year which could not be compensated with profits of the same year may be carried forward for federal tax purposes for seven years; no tax loss carry-back is provided for.

Dividends paid to the shareholders are not deductible. However, a special tax relief ("participation exemption") applies to dividends received by a corporation from qualifying Swiss or foreign corporate participations (participations representing a control of at least 20% of the shares of another corporation *or* a fair market value of at least CHF 2 million).

(ii) Cantonal/Communal Tax Level

As indicated above, each of the 26 Swiss cantons has its own tax law; communal taxes are generally levied as a multiple of the cantonal tax. In order to assimilate the cantonal tax laws to the federal law on direct taxes ("FDTL") and among each other, the federal law concerning the harmonization of the direct taxes of the cantons and communes dated

14 December 1990 ("FLH") was enacted on 1 January 1993. All cantons will have to adapt their respective cantonal laws to the FLH within a period of eight years, i.e., by the year 2001. After 2001, the FLH will directly apply to cantonal taxation, whenever the respective provisions of the cantonal tax laws are not in conformity with it. According to the FLH, the cantonal liberties regarding the contents of their tax laws have been restricted to the determination of the tax rates, tax tariffs and tax exemptions. On the other hand, the principles on taxation, taxable objects, tax periods as well as the procedural provisions of the cantonal tax laws have to be brought in line with the FLH by 1 January 2001.

At present, ordinary cantonal income tax rates vary between approximately 12% and 35%, whereby federal and cantonal/communal income and capital taxes may or may not be deductible depending upon the tax legislation of the relevant canton. The taxable income is basically determined in the same manner as for federal income tax purposes; certain differences may, however, apply with regard to capital gains realized on immovable property (see below). Cantonal income taxes are usually calculated on a similar basis as the federal income tax, i.e., the tax rate is determined, within upper and lower limits, by the proportion between the taxable income and the net equity.

Substantially all cantonal tax laws provide for similar mechanisms to relieve dividend income derived from (domestic or foreign) substantial participations from income taxation as is provided under federal tax law. In addition, most of the cantons provide for special tax privileges for holding companies and other special purpose companies, such as companies performing the bulk of their business activities abroad, companies providing various kinds of services to related parties, etc..

As a rule, income derived from real property located within the territory of a canton is subject to corporate income taxation by such canton (and/or commune). Special rules may, however, apply to capital gains realized on immovable business property. While in the majority of the cantons such gains are included in the income subject to the normal corporate income tax, some cantons (including, e.g., Zurich and Berne) apply a split-system with regard to gains realized on business real estate. In these cantons, only the recaptured tax-

effective depreciations of prior years (if any) are subject to the normal income tax, while the realized increase in value is subject to the special *real property gains tax*, which applies also to real property gains realized by private individuals (see below). Capital gains realized by professional real estate brokers on their immovable business assets are in most cantons (except Zurich and Berne) subject to the normal income tax as income from a gainful activity. Capital losses on real property can be deducted if the capital gains are subject to the normal income tax. If the real property gains are subject to the special tax, losses on other immovable assets located within the same jurisdiction cannot be set off.

3. Taxation of Individuals

a) In General

Swiss resident individuals are, on principle, subject to income and net worth taxes for their worldwide income and net worth. Foreign real estate and permanent business establishments maintained abroad are, however, exempt from Swiss taxation; the respective income and assets are, however, taken into account for the determination of the applicable tax rates. Foreign resident individuals are subject to federal, cantonal and communal taxes on income and net worth with regard to certain types of income with a sufficient connex in the Swiss territories concerned, such as income derived from dependent professional services performed in the canton, business income derived from a permanent establishment maintained in the canton, income and gains from immovable property located within the canton, and interest income from loans secured by real estate located in the canton.

At the federal tax level, any capital gains realized on private (movable or immovable) assets are exempt from income taxation. At the cantonal/communal tax level, capital gains on private movable assets are tax-free, while capital gains on private immovable property are usually subject to a special immovable property gains tax (see below).

Depending upon the size of the taxable income and the canton and commune in question, the combined burden of federal, cantonal and

communal income taxes may reach some 45% (the maximum federal income tax rate being 11.5%).

The annual charge of net worth taxes similarly depends largely upon the canton and the commune of residence. In the city of Zurich, the maximum net worth tax burden amounts to approx. 0.7%.

b) Taxation of Current Income from Immovable Property

The taxable income of an individual does not only include rental or lease fees as well as fees for a right to build or other servitudes received from third parties, but also the rental or lease value of immovable property used personally by the taxpayer or his/her family. Such rental or lease values are generally determined periodically by the local tax authorities on the basis of fair market values. Generally, all maintenance as well as financing costs (debt interest) for immovable property (whether private or business) can be deducted for income tax purposes. Exceptions to this general rule may apply to debt interest incurred during the phase of construction of a building (which must be capitalized), as well as certain "delayed maintenance" and renovation costs for used buildings within five years of the acquisition of such property ("Dumont practice"). Typically, taxpayers may choose between claiming a lump-sum maintenance deduction (e.g., 20% of the current rental or lease income or lease value of property personally used by the taxpayer) or a deduction of actual maintenance costs.

c) Special Immovable Property Gains Taxes

The Swiss tax treatment of gains realized upon dispositions of immovable property located in Switzerland is quite complicated.

At the federal tax level, such gains are only taxed if they are realized on business property of the taxpayer or in connection with a professional activity as a real estate broker. It should be noted that even private persons may, under certain conditions developed by the tax practice, come within the definition of "professional real estate brokers" for tax purposes. Otherwise, gains realized on private immovable property are not subject to tax at the federal level.

In most of the cantons, capital gains realized upon the disposition of immovable property are exempt from the normal personal income

taxes, but are subject to a special immovable property gains tax. Gains realized on immovable *business* property are, however, in the majority of the cantons (excluding Zurich and Berne) subject to the normal income tax rather than the special immovable property gains tax.

The details (and the scope of application, see above) of the immovable property gains taxes still vary from canton to canton. Generally, only those gains on immovable property which have been *realized* are taxable. There are basically two categories of taxable real property transactions: (a) sales, exchanges and similar transactions by which the transferor transfers the legal power of disposition of the property to the transferee, and (b) other transactions by which the effective or economic capacity to dispose of the property, or the "beneficial ownership" of the property, is transferred to the transferee without a transfer of the legal title to the property. Such second category of transactions may include, for example, transfers of all or a controlling majority of the shares of a "real estate company", grants of pre-emption rights or rights of first refusal, and the establishment of encumbrances (such as private or public servitudes or easements, e.g., a right to build on the owner's land) which permanently and substantially limit ownership rights.

Certain types of transactions are usually exempt from the real property gains tax. Exempt transactions may include transfers in connection with setting-up or dissolution of a marital community of property or with a divorce, transfers by virtue of inheritance or gift and at the partition of an estate, transfers as a consequence of zoning, rectifications of boundaries or consolidation of agricultural plots, and transfers in connection with reorganizations of enterprises (transformations, mergers, split-offs etc.), if certain conditions are met. Reinvestment of the proceeds of a real property sale in other real property located in the canton (or even in another canton) within a certain period of time may also qualify the transaction for a gains tax exemption.

The taxable gain generally corresponds to the excess of the realized net proceeds over the investment value of the real property. The investment value is the aggregate of the acquisition price including expenses connected therewith and all subsequent expenditures for the property which increased its value. If the acquisition of the property

qualified for a gains tax exemption, either the value at the last taxable transfer or the fair market value at the time of the tax-exempt transfer is taken into account as acquisition price. In the case of very long holding periods, the taxpayer may, e.g., in the canton of Zurich elect the market value 20 years before the actual transfer to be the relevant acquisition price.

The immovable property gains tax rates vary considerably from canton to canton. There is usually a double progression scheme taking into account the amount of the taxable gain as well as the holding period. Speculation surcharges may apply in the case of holding periods of less than two years.

For example, the canton of Zurich levies a surcharge on the "simple" gains tax of 50% in the case of a holding period of less than one year, or 25% if the holding period is more than one but less than two years. If the holding period amounts to at least five years, the "simple" gains tax is reduced by 3% for each additional year, up to a maximum tax reduction of 50% for holding periods of 20 years or more. The "simple" gains tax rate is progressive and reaches a maximum of 40% for those gain portions exceeding CHF 50'000.

4. Other Taxes Affecting Swiss Real Property

a) Real Property Object Taxes

Some cantons (or the communes) levy special object taxes on the value of real property located in the territory. These taxes are usually imposed in addition to the normal income and net worth or capital taxes. They are structured as a tax on an object, not as a tax on the person who owns the property (and as such owes the tax). The rates of such object taxes usually range from .05% to .2%.

b) Real Property Transfer Taxes

In most of the cantons, transfers *inter vivos* of immovable property are subject to either cantonal or communal transfer taxes (a few cantons do instead levy special land register fees). The transfer tax hits all legal and economic transfers of immovable property. Economic transfers are basically defined in the same manner as for the purposes

of the immovable property gains tax. Therefore, a transfer of a controlling interest in a real estate company is generally deemed to be a taxable transfer of the real property owned by the company. The tax is computed on the purchase price or, if such price is deemed to be arbitrary in related-party transactions, on the estimated market value of the transferred property. Basically the same exemptions as for the purposes of the immovable property gains tax apply to the transfer tax. Many cantons provide for a joint and several liability for the tax of both the transferor and the transferee of the property. The transfer tax rates range widely between .1 and 4%. Surcharges and tax reductions may apply in the case of short or long holding periods, as the case may be.

c) Value Added Taxes

Effective 1 January 1995, the previous Swiss federal sales tax (*Warenumsatzsteuer, WUSt/Impôt sur le chiffre d'affaires, IchA)* was replaced by a modern, substantially EU-compatible VAT system (*Mehrwertsteuer, MWSt/Taxe sur la valeur ajoutée, TVA)*. The VAT is levied on the turnover from domestic supplies and imports of goods and services. The standard Swiss VAT rate is presently 6.5%; certain products covering basic needs, such as food, medicaments, newspapers etc. are taxed at a reduced rate of 2%.

The turnover from immovable property leases is generally exempt from the VAT. However, the landlord may opt for VAT liability of rental income from immovable property leases, if the tenant is a VAT subject. To the extent that the landlord pays VAT on the rental income, the input VAT charges (e.g., on the construction costs) can be deducted from his own VAT liability.

L. Restrictions on Use and Other Restrictions

1. Restrictions on Ownership of Land

The most important restrictions on ownership of land presently in force concern foreign persons or entities dominated by foreigners (see chapter XIII). Otherwise, there are few legal restrictions on land ownership. Minors and mentally incapacitated persons may be owners of land, but their rights must be exercised by their legal representatives according to the applicable provisions of the Civil Code.

2. Restrictions on Disposal of Land

There are specific statutory restrictions on the disposal of land by entities under public law. Those relevant to private legal entities and individuals were the regulations contained in a federal enactment of 1989, which was designed to limit the negative effects of rising property prices and speculation in the real property market[52]. It provided for a five-year waiting period for the sale of real property calculated from the date of its acquisition. Exceptions were made for narrowly defined categories of transactions, such as inheritance, sale to close family members, and cases of foreclosure. Permission for a sale before the expiration of the five-year period were granted only in special cases, especially if the seller did not make a profit, or if he had used the property as his residence for two years, or erected buildings on the property. The life-span that enactment was limited to a five-years period, i.e. until 31 December 1994. To date, no extension of this law or any similar enactment is in sight. Otherwise, land is freely disposable, subject only to the general rules described herein.

[52] *Bundesbeschluss über eine Sperrfrist für die Veräusserung nichtlandwirtschaftlicher Grundstücke und die Veröffentlichung von Eigentumsübertragungen von Grundstücken/Arrêté fédéral concernant un délai d'interdiction de revente des immeubles non agricoles et la publication des transferts de propriété immobilière.*

M. Acquisition of Real Estate By Foreigners

1. General Remarks

The Federal Law on the Acquisition of Real Estate by Non-Residents of December 16, 1983, in force since January 1, 1985, the so-called "*Lex Friedrich*"[53] regulates and restricts the acquisition of real estate by foreigners. In March 1994, the Swiss government proposed to the Swiss parliament a revision of the *Lex Friedrich*, providing for a strong liberalization of the law. In summer 1995, however, the Swiss voters rejected such revision of the *Lex Friedrich*. It is, therefore, very likely that the present statute containing substantial restriction for the acquisition of real property by foreigners will remain in force for the next years. In order to reach at least some of the years pursued by the proposal of the government, the latter decided in the summer of 1996 that the quota of the cantons (see *infra*, 5.) could be transferred among the cantons.

This statute is a consequence of the fact that the land available in Switzerland for urbanization and development is scarce, and that therefore the growing number of foreigners acquiring real property in Switzerland was a cause for concern in large parts of the population. In addition to the *Lex Friedrich*, an Ordinance on Acquisition of Real Estate by Persons in Foreign Countries[54], hereinafter referred to as Ordinance to *Lex Friedrich*, was enacted, which defines the federal statute in detail.

All transactions that convey control over an interest in real property to a non-resident are subject to restrictions. Such transactions require a permit from the competent cantonal authorities before the transaction can be completed (see section 3 hereinafter). Unlawful acquisitions made in violation of the provisions of the applicable statute are void and may lead to confiscation of the property.

[53] *Bundesgesetz über den Erwerb von Grundstücken durch Personen im Ausland/ Loi fédérale sur l'acquisition d'immeubles par des personnes à l'étranger*, named after the then federal Justice Minister Friedrich.

[54] *Verordnung über den Erwerb von Grundstücken durch Personen im Ausland/ Ordonnance sur l'acquisition d'immeubles par des personnes à l'étranger.*

The goal of this chapter is only to give a rough overview, touching on, in a little more detail, the core questions which come up in the context of non-residents' involvement in real estate transactions. Since the issues regarding *Lex Friedrich* problems are, however, quite complex, the following overview can only serve as a guideline and does not discuss all aspects of the Statute, the Ordinance, and the practice of the judiciary developed thereunder.

2. Definition of the Term "Acquisition of Real Estate" under the Lex Friedrich

The term "acquisition of real estate" is very broad and applies to every kind of control over or interest in real estate. In detail, the term includes the following legal or economical interests in real estate[55]:

a) acquisition of ownership, of a right to build[56], of a right of residence[57] or of usufruct[58];

b) participation in a partnership without legal personality but capable of holding funds[59], the assets of which include real estate in Switzerland or the real purpose of which is the acquisition of real estate;

c) acquisition of ownership, usufruct rights on a share of a real estate investment fund[60], if the certificates of participation are not marketed on a regular basis;

[55] Article 4 *Lex Friedrich*.
[56] See Articles 779 et seq. CC and B.6.c *supra*.
[57] See Article 776 CC and B.6.b *supra*.
[58] See Article 745 et seq. CC and B.6.a *supra*.
[59] Such as a general partnership (*Kollektivgesellschaft/société en nom collectif*) according to Articles 552 et seq. CO, or a limited partnership (*Kommanditgesellschaft/société en commandite*) according to Articles 594 et seq. CO. A simple partnership (*Einfache Gesellschaft/société simple*) according to Articles 530 et seq. CO, which is not registered in the Commercial Register, is not considered a partnership without legal personality but capable of having funds under the *Lex Friedrich*. Therefore, the rules of Article 4 (a) are applicable to the simple partnership.
[60] See Federal Statute on Investment funds (*Anlagefondsgesetz/Loi fédérale sur les fonds de placement*).

d) acquisition of an ownership or usufruct right on a share of a legal entity[61] the assets of which, appraised at their real value[62], include for more than one third real estate situated in Switzerland[63] if, thereby, non-residents obtain or reinforce a dominating position[64];

e) acquisition of a right of ownership or usufruct on a share of a legal entity, where the real purpose is the purchase of real estate[65];

f) creation or exercise of a right of emption, right of pre-emption or right of redemption or repurchase of a property or share according to b) through e) above;

g) acquisition of other rights, which grant their holder a similar position to that of the owner of a property.

Subsection g) of this Article has to be read in connection with

[61] Such as a stock corporation (*Aktiengesellschaft/société anonyme*) according to Articles 620 et seq. CO, a corporation with unlimited partners (*Kommanditgesellschaft/société en commandite*) according to Articles 764 et seq. CO, a limited liability company (*Gesellschaft mit beschränkter Haftung [GmbH]/société à responsabilité limitée*) according to Articles 772 et seq. CO, or a co-operative company (*Genossenschaft/société coopérative*) according to Articles 828 et seq. CO.

Also to be included in this list is the association (*Verein/association*) according to Articles 60 et seq. CC, which is a legal entity but does not have shares; a membership in an association could also include a claim of using real estate.

Although generally considered a legal entity, a foundation (*Stiftung/fondation*) according to Articles 80 et seq. CC is not covered by Article 4 (b) *Lex Friedrich*, because one cannot acquire shares in a foundation. If, however, the beneficiary is a non-resident, Article 4 (g) *Lex Friedrich* may apply.

[62] I.e., not book value. As a consequence of the considerable freedom in depreciation of assets under Swiss company law, real estate has most of the time a considerably lower book value than real value. Although it will be necessary to get an appraisal in order to have a reliable valuation, the value of the fire insurance gives a more reliable indication of real value than the book value.

[63] So-called real estate company in the broader sense; to be distinct from the real estate company in the narrower sense, see Article 4 (e) *Lex Friedrich.*

[64] "Dominating position" is a relative term and, therefore, no strict guidelines can be applied to assess whether a non-resident obtains or reinforces a dominating position. In any event, however, a foreign dominance is presumed if more than one third of the shares in the entity are held by non-residents.

[65] So-called real estate company in the narrower sense to be distinguished from the real estate company in the broader sense, see Article 4 (d) *Lex Friedrich*.

Article 1 (2) of the Ordinance to the *Lex Friedrich*, which lists additional examples (the list is not considered to be exhaustive) of fact-patterns falling under the restrictions created by the Statute:

a) long-term lease or tenancy of real estate[66], where the agreements exceed the routine of ordinary or commercial business activity and put the lessor or the landlord in a state of special dependency on the lessee or the tenant[67];

b) the financing of a purchase of, or the construction on, real estate[68], where the agreements, the size of the loans or the financial circumstances of the debtor put the purchaser or the contractor in a state of special dependency on the creditor[69];

c) the constitution of prohibitions to build or similar restrictions of the right of property with real or contractual effect concerning an adjoining property.

3. Terminology

a) Definition of the Term "Non-Resident" under the Lex Friedrich (Article 5)

Article 5 *Lex Friedrich* defines the term "non-resident" as follows:

(i) individuals without Swiss residence rights[70];

[66] The Swiss Federal Supreme Court ruled in a 1979 decision that a lease agreement of 15 years is to be considered a long-term lease within the meaning of this Article. In practice, a 10 year lease-agreement is to be considered "long-term".

[67] Whether there exists a special dependency among the parties of a lease agreement has to be decided on a case by case basis. The Federal Supreme Court ruled that such dependency is imminent if the tenant can act as he would be the owner of the property, e.g., if the tenant is also financing the property he rents or if he pays the rent in advance for several years.

[68] In general, the limit where a permit is required can be set when more than 2/3 of the purchase price of the real estate is financed by a non-resident. However, this rate is only valid as a guideline and not as a strict rule.

[69] As in Article 1 (2)(a) of the Ordinance to the *Lex Friedrich*, the prime example of dependency is again a combined credit and lease agreement.

[70] Foreigners have residence rights if they were granted a so-called Permit C (*Niederlassungsbewilligung/autorisation d'établissement*).

(ii) legal entities or unincorporated entities capable of acquiring property, which have their registered seat or factual domicile in a foreign country;

(iii) legal entities or unincorporated entities capable of acquiring property, which have their registered seat or factual domicile in Switzerland, but are controlled by non-residents; the rules to be applied in order to assess whether a company is controlled by a non-resident are described in Article 6 *Lex Friedrich* (see section 3. b *infra*).

(iv) individuals having Swiss residence rights and legal or unincorporated entities capable of acquiring property, which have their seat in Switzerland, if they acquire real estate on behalf of non-residents. This subsection deals with cases where a trustee who does not need a permit buys real estate on behalf of a non-resident. It is obvious that non-residents try to evade the rather strict rules of the statute by using a strawman as a front. The statute does not generally prohibit the fiduciary acquisition of real estate for a non-resident *per se*, but requires full disclosure of the fiduciary agreement and, specifically, the disclosure of the fiduciary. There are, however, cases where a fiduciary acquisition on behalf of a non-resident is not allowed at all, e.g., vacation condominiums in apartment hotels, etc., see Articles 8 (3), 9 (1)(b) and (c), 9 (2) *Lex Friedrich* as well as Article 8 Ordinance to *Lex Friedrich.*

b) Definition of the Term "Control by Non-Residents" under Lex Friedrich (Article 6)

A non-resident is considered to exercise control when, by reason of the importance of his financial interest/voting rights or any other reason he can exercise, alone or together with other non-residents, a controlling influence on the direction or management.

Foreign control of a legal entity is presumed in a situation where non-residents:

(i) own more than one third of the share capital, registered capital or certificate of interest; if there exist participating receipts and/

or bonus shares, such capital has to be added to the "ordinary" capital in order to compute the fraction of non-resident holding[71];

(ii) have more than one third of the voting rights in the general meeting or in the partners' meeting; one of the main reasons why not only the capital, but also the voting rights are relevant for the control of an entity is the fact that a shareholder holding only a minority of the capital (e.g., 10%) can control an entity if he has shares with privileged voting rights[72]. A minority shareholder can also control an entity by concluding a shareholders' agreement. This subsection, however, does not mention this case and, therefore, such a case is not within the scope of this subsection; it is rather within the scope of the general clause of subsection 1 of Article 6;

(iii) form the majority of the members of the board or of the beneficiaries of a private foundation;

(iv) have made reimbursable advances, i.e., secured and unsecured loans, liabilities on current account, accounts payable, etc. to the legal entity the total of which exceeds half of the difference between its total assets and its total debts towards persons not subject to a permit[73].

Foreign control of a general[74] or limited partnership[75] is presumed in situations where non-residents:

(i) are partners with unlimited liability; i.e. all partners of a general partnership but only the unlimited partners of a limited partner-

[71] This subsection is applicable to the stock corporation (*Aktiengesellschaft/société anonyme*) according to Articles 620 et seq. CO, the limited liability company (*Gesellschaft mit beschränkter Haftung [GmbH]/société a responsabilité limitée*) according to Articles 772 et seq. CO, and the co-operative company (*Genossenschaft/société coopérative*) according to Articles 828 et seq. CO.

[72] This subsection is applicable to the stock corporation (*Aktiengesellschaft/société anonyme*) according to Articles 620 et seq. CO, the limited liability company (*Gesellschaft mit beschränkter Haftung [GmbH]/société de responsabilité limitée*) according to Articles 772 et seq. CO, the cooperative (*Genossenschaft/ société coopérative*) according to Articles 828 et seq. CO, and the association (*Verein/ association*), because these entities have a general assembly or a partners meeting.

ship;

(ii) have, as limited partners, contributed more than one third of the equity of the partnership; the one third has to be computed of the total equity of the partnership and not of the sum of all partners' contributions. With regard to the valuation, the same standards apply as mentioned in footnote 64 *supra*;

(iii) have made reimbursable advances to the partnership or to partners with unlimited liability, if the total of those exceeds half of the difference between the total assets of the partnership and its total debts towards persons not subject to a permit[76].

4. Right to a Permit

If a permit is required, the statute lists in Article 8 the "General Grounds for Granting a Permit" and in Art. 9 the "Additional Grounds for a Grant by the Cantons".

a) Permanent Business Establishments (Article 8 (1)(a) Lex Friedrich)

Most of the permits are granted for the creation of permanent business establishments[77]. A permit is only granted if the acquirer actually controls the business. He must be a leading person in the

[73] The following formula can be applied in order to assess whether the reimbursable advances lead to foreign control:

X = foreign reimbursable advances
Y = total assets
Z = Swiss reimbursable advances

if X < (Y - Z)/2, no foreign control is presumed.

Not the book values, but the real values have to be applied, see Footnote 64 *supra*.

[74] General partnership (*Kollektivgesellschaft/société en nom collective*) according to Articles 552 et seq. CO.

[75] Limited partnership (*Kommanditgesellschaft/société en commandite*) according to Articles 594 et seq. CO.

[76] The same principles apply as outlined in 3 b)(iv) *supra*.

[77] Article 8 (l)(a) *Lex Friedrich*.

management or on the board[78].

Furthermore, with respect to the acquisition of property, the owner must conduct a business on the acquired premises which is in line with his main business, e.g., a production company may not own a hotel in Switzerland, because this would constitute a capital investment.

A permit is, as a matter of principle, not granted if the acquisition of real estate which serves an agricultural purpose and is made by an acquiror which is merely a subsidiary of another enterprise organized on a commercial basis, for the construction of buildings which do not in reality serve the constructor as a permanent business establishment/structure required to run the business, and for the commercial letting out of lodgings which are not part of a hotel or aparthotel[79].

Finally, the real property must cover permissible surface area, so that land reserves for an enlargement of the place of operation are within permissible, specified limits[80].

b) Insurance Companies (Article 8 (1)(b) Lex Friedrich)

Insurance companies dominated by non-residents are granted permits if they are allowed to operate their business in Switzerland and if they invest their technically necessary reserves regarding their Swiss portfolios in Swiss real estate.

c) Welfare funds (Article 8 (1)(c) Lex Friedrich)

The acquisition of real property may also be permitted if a welfare fund acquires real property in favour of employees of a foreign enterprise which has a permanent business establishment in Switzerland or if the purpose thereof is exclusively charitable. In both cases, however, in order to qualify, the acquisition must be exempt from the

[78] Article 3 (1) Ordinance to the *Lex Friedrich*.

[79] Article 3 (3) Ordinance to the *Lex Friedrich*.

[80] Article 10 (1) Ordinance to the *Lex Friedrich*. It mentions that the net surface for primary apartments shall not exceed 200 square meters. For secondary apartments, the net surface shall not exceed 100 square meters. In case of a single family home, the size of the total surface area of the property shall not exceed 1000 square meters.

direct federal tax.

d) Mortgage Liquidation (Article 8 (1)(4) Lex Friedrich)

Furthermore, a foreign bank or insurance company allowed to run a business establishment in Switzerland may acquire real estate as a result of the enforcement of a mortgage, such as in the case of an overdue mortgage-secured loan. In those cases, however, the bank or insurance company must resell the property within a period of two years.

e) Testamentary Beneficiaries (Article 8 (2) Lex Friedrich)

Testamentary heirs may also hold real estate for a limited period of two years, unless they qualify for a permit on some other ground. It must be noted that statutory heirs do not need a permit[81].

f) Cases of Hardship (Article 8 (3) Lex Friedrich)

A foreign buyer, who does not qualify for a permit, may acquire real estate[82] from a (Swiss or foreign) seller, if that seller can show that he is suffering some hardship. In other words, the seller must be in a situation of some unforeseen difficulty, which can only be remedied by the transfer of the property to a non-resident.

g) Cantonal Grounds (Article 9 Lex Friedrich)

Additional grounds for the granting of permits can be established by the individual cantons as cantonal law so long as they are based upon the principles defined in Article 9 *Lex Friedrich*. For instance, if a canton is experiencing a housing shortage, it may grant a permit to a foreign acquirer subject to the condition that he construct additional subsidized housing. Furthermore, permits may be granted by the can-

[81] Article 7 (a) *Lex Friedrich*.

[82] This exception cannot be called in cantons where there are so-called "cantonal grounds" to acquire real estate (see Article 9 *Lex Friedrich*, subsection g *infra*) and where there is not a freeze on authorization according to Article 13(1) (a) *Lex Friedrich*.

tons if the real estate serves as the first home or the legal and factual domicile of an individual or as a second apartment, if it is situated at a place in which that individual has exceptionally close ties, which are worth protecting so long as they last.

Furthermore, cantons have the power to enact by law that a natural person may be granted a permit to acquire a holiday apartment or a residential unit in an aparthotel as long as this is within the limits of the cantonal quota. The Federal Council determines every two years the annual cantonal quota for each canton which has such a quota[83].

5. Quotas

Every two years, the Federal Council *(Bundesrat/Conseil Fédéral)* – after consultation with the cantonal governments – determines the number of units of holiday homes and apartments in apartment hotels which may be sold to foreigners in every canton[84]. In 1985, the quotas for all cantons collectively totalled 2000 units. In application of Article 1 (2) *Lex Friedrich*, this number has been gradually reduced, so that in 1996, the total quota is 1420 units. The same figure applies for 1997 and 1998. The cantons with the largest quotas are Berne (125 units), Grisons (270), Ticino (180), Vaud (160) and Valais (310). The cantons of the largest cities, i.e. Zurich, Basel and Geneva, have no quotas at all.

The determination of the quotas for each canton takes into account such items as the dependency of a canton on tourism, the tourist development program and the proportion of real estate owned by non-residents in a canton[85]. In the course of the revision of the Ordinance to *Lex Friedrich* (which was refused in the popular vote, however), the Federal Council had proposed that cantons be able to assign their surplus quotas among each other, so as to use up the whole quotas. In the last few years, the total quota for Switzerland were not used up, with only four cantons (Ticino, Valais, Grisons and Vaud) usually exhausting their quotas[86].

[83] Article 11 *Lex Friedrich*.
[84] Article 11 (1) *Lex Friedrich*.
[85] Article 11 (3) *Lex Friedrich*.

After the proposed revision of the Statute was rejected, other ways were sought to improve the unsatisfactory situation. Finally, the government decided to amend the Ordinance (which as such is not subject to a popular vote). It now provides for a possibility for the federal government to assign unused quotas towards the end of a calendar year to cantons who have already exhausted their quotas in the course of the year. The additional number of units cannot exceed 50 % of the annual regular quota of a specific canton. This new provision enters into force on 1 August 1996, which means that already in autumn of this year additional quotas might be available for certain cantons.

6. Refusal of Permit

Article 12 *Lex Friedrich* lists some grounds for the mandatory refusal for the granting of a permit. A permit will not be granted if:

- the property represents an investment of funds, which is not authorized under the statute[87];
- the buyer has tried to evade the statute[88];
- the buyer of a second or holiday home or an apartment, his spouse or one of his children under twenty years of age already owns a similar property in Switzerland[89];
- the property is located near an important military installation and an acquisition could therefore jeopardize the national security[90]; or
- an acquisition would be in conflict with higher national interests[91].

[86] The canton of Ticino had already exhausted its quota for 1996 at the end of February 1996, for example.
[87] Article 12 (a) *Lex Friedrich*; e.g., a non-resident wants to buy an apartment to rent it out.
[88] Article 12 (a) *Lex Friedrich.*
[89] Article 12 (c) *Lex Friedrich.*
[90] Article 12 (e) *Lex Friedrich.*
[91] Article 12 (f) *Lex Friedrich.*

7. Procedures in Order to Obtain a Permit

Applications for permits have to be filed with the cantonal authorities in charge of the territory within which the real estate is situated[92]. Acquirers who are not sure whether their investment triggers a permit requirement must seek a declaration that a permit is not required[93], and that negative declaration must be filed together with the execution of the contract of acquisition[94]. The decisions of the competent cantonal authorities are subject to an appeal to the cantonal appeals authorities. The decisions of the cantonal appeals authorities are again subject to appeal to the Federal appeals authorities[95], which are the Federal Supreme Court, the Federal Council, or the Federal Department of Justice, as the case may be[96].

In practice, the registrars of the land register[97] have the important task of enforcing the statute. Where they cannot immediately determine that a real estate transaction is exempt from a permit requirement, they will hold up the registration process and grant the acquirer a thirty day period in order to get a ruling from the competent cantonal authorities stating that a permit is not required[98].

If a permit is obtained, the conditions and charges, intended to ensure that the property is used in conformity with the purpose stated by the acquirer, are registered in the land register[99]. If there are pressing reasons, such conditions and charges can be revoked by the authorities, e.g., in case of a change of circumstances for the acquirer so that the fulfilment of a charge is impossible or cannot be expected of him.

[92] Article 15 (2) *Lex Friedrich*, Article 16 Ordinance to *Lex Friedrich*.
[93] Article 17 Lex Friedrich.
[94] In practice, such filing has to be made within one month after the execution of the contract.
[95] Article 20 *Lex Friedrich*.
[96] Article 21 *Lex Friedrich*.
[97] The same applies to the registrars of the Commercial Registers.
[98] Article 18 *Lex Friedrich*.
[99] Article 14 *Lex Friedrich*, Article 11 Ordinance to *Lex Friedrich*.

8. Sanctions

a) Administrative Measures

In case the acquirer has obtained the permit fraudulently by supplying inaccurate information or where he – despite formal notice – does not comply with an obligation, the authorization is automatically withdrawn. Furthermore, sanctions provided for by the laws on foreigners are reserved.

b) Measures under Civil Law

Legal transactions regarding an acquisition have no legal effect in the absence of authorization, if such is required prior to the transaction[100].

Legal transactions are nullified in situations where (i) the buyer executes a legal transaction without requesting a permit or before the latter becomes effective; (ii) the authority has refused the grant of a permit or has withdrawn it by a ruling becoming effective; (iii) the land or commercial registrar sets aside the request without the authorizing authority having previously refused to give authorization; or (iv) the authorities in charge of auctions cancels the adjudication, without the authorizing authority having previously refused to give authorization[101].

The consequences of ineffectiveness and nullity are that the contractual commitments become unenforceable, and any performance on the contract can be recouped within one year from the time the claimant becomes aware of his claim. In cases where criminal proceedings are initiated, the time period of one year starts to run upon the completion of the proceedings, not later, however, than 10 years after claimant knows about his claim. Furthermore, the cantonal or federal authorities will reinstate the original status[102].

[100] Article 26 (1) *Lex Friedrich.*
[101] Article 26 (2) *Lex Friedrich.*
[102] Article 26 and 27 *Lex Friedrich.*

c) Criminal Measures

The consequences in case of any criminally executed illegal transactions are rather harsh: imprisonment or fines of up to CHF 100'000 are required by law[103]. In cases where the perpetrator has acted in a professional capacity, the imprisonment is not less than six months[104]. If the illegal transaction is based on negligence, the fine is up to CHF 50'000[105].

If a person provides inaccurate information in the course of a permit application or if obligations of *Lex Friedrich* are non complied with, Articles 29 and 30 *Lex Friedrich* also provide for heavy fines of up to CHF 100'000.

[103] Article 28 (1) *Lex Friedrich*.
[104] Article 28 (2) *Lex Friedrich*.
[105] Article 28 (3) *Lex Friedrich*.

N. Environmental Protection

1. Protection against Pollution

The Swiss Constitution empowers the Swiss parliament to legislate in the field of environmental protection. A Federal Environmental Protection Statute[106] was enacted in 1983 and deals in a very broad sense with pollution, especially air pollution, excessive noise, soil contamination, dangerous substances etc. The implementation of the Statute is a duty of the cantons, who have had to fulfilled that duty in recent years in very different ways; not all cantons were very quick to respond to the new legislation. As far as real estate and construction is concerned, a major role is played by the detailed zoning laws, that are intended to preserve the undeveloped areas of Switzerland in order to maintain room for agriculture and recreational areas for the population (see *infra* chapter O.). The construction of new properties is subject to detailed regulations which control the possible impact such buildings may to have on the environment. For larger projects, a detailed study of such impact and effects[107] is required as a prerequisite for a building permit. As a general rule, the law in that field is based on the principle that polluters have to pay for the damages they cause[108], thus creating a direct liability for any entity guilty of pollution.

2. Waste Storage and Disposal

Federal law regulates waste storage and disposal only insofar as the most dangerous waste is concerned, otherwise leaving the regulation of the matter within the competence of the cantons. In addition, federal law states the general principle that waste must be recycled, stabilized or destroyed. Municipal waste is usually incinerated in

[106] *Umweltschutzgesetz/Loi fédérale sur la protection de l'environnement.*
[107] *Umweltverträglichkeitsprüfung/étude d'impact sur l'environnement.*
[108] *Verursacherprinzip/principe du pollueur-payeur.*

government-owned plants, some of which are used for energy generation (so-called waste-to-energy plants). For the disposal of industrial waste, large fees, depending on the nature and harmful quality of waste, must be paid. Similarly, private households are charged flat fees on a *per capita* basis for waste disposal, or, as in an increasing number of cantons and municipalities, the disposal of domestic waste is made in special standardized waste bags, which have a disposal fee included in their purchase price. By doing so, legislators hope to encourage the use of recyclable goods and the minimalization of the refuse through a change in attitude and habit.

3. Air Pollution

According to a federal air pollution ordinance, newly built and old structures must fulfil certain conditions in order to obtain a building permit or a further permit for their operation. This ordinance covers not only buildings, but all structures that might have an air polluting effect, especially heating systems, vehicles and fuels. The ordinance sets emission limits that may not be exceeded and provides for periodic inspection. If a heating system does not meet the emission standards set by the applicable provisions, the owner will be granted a time-limit to modify or replace the system. In case of non-compliance, the owner may face criminal and civil sanctions.

O. Planning and Building Regulations

1. Zoning Law

Swiss law provides for detailed regulations on the procedures and circumstances under which land can be developed. One of the two important sources for the legislation that must be consulted is the zoning law which, as usual in Switzerland, is governed partly by federal and partly by cantonal and municipal statutes.

a) Federal Law

The federal parliament, based on an authorization which has been embodied in Art. 22 of the Federal Constitution since 1969, enacted the Zoning Act in 1979 (*Raumplanungsgesetz/Loi fédérale sur l'aménagement du territoire*), which aims at providing for a resourceful use of the land and a well-structured settlement policy. The Act provides for three general types of zones, namely the building zone, which is to serve the development of settlements, the agricultural zone, which is reserved for the production of agricultural goods, and the protection zone, where any use that might endanger territories worthy of protection is prohibited. The detailed definition of place and size of these zones is reserved to the cantons and municipalities; the power of the federal legislator is limited to the enactment of the general guidelines, to define the implementing authorities of the cantons and to set a uniform standard categories; the execution of the principles laid down in the Zoning Act is reserved to the executing legislation of cantons and municipalities. The latter are also empowered to introduce additional types of zones, something the cantons have done in ample fashion. In addition, the federal government's role is to encourage and to coordinate the collaboration between the cantons in this field. As far as direct effect of federal law on individuals is concerned, Art. 22(3) of the Swiss Constitution must be mentioned, which provides for fair compensation to be paid to anybody who suffers a limitation in his property rights amounting to an expropriation, as a consequence of zoning measures.

b) Cantonal Law

The cantonal zoning laws set down the allocation plans, which describe the several zones that exist and the manner the land in these zones may be used. The most important zone is the building zone, which is divided into several sub-zones that determine the permissible building purposes and density and height of such buildings. Usually, there are zones for residential buildings, again sub-divided into houses of different sizes, industrial zones, a zone for public buildings, and core zones for old parts and the center of towns, where more dense building construction is permitted. In addition, cantons usually provide for reserve zones, i.e. land that must not be assigned to one of the above-mentioned zones for the time being; land in that zone might provide local legislators with a certain flexibility in responding to future developments and requirements.

c) Municipal Law

The powers that are reserved for the municipalities depend on the cantonal legislation. Generally, it can be observed that the cantons have enacted a framework providing for a very detailed regulation but grant the municipalities wide discretion in the partitioning of their territory into the several zones prescribed by the cantonal laws. Very often, the decisions made at that level are the most important and far reaching for individual land owners, because they are decisive for the potential building activities on the land and thus ultimately for its value.

d) Judicial Review

The proceedings in which zoning decisions of the competent public authorities may be challenged vary from canton to canton. Suffice it to say that those decisions can be challenged in courts and that ultimately an appeal can be brought against any zoning measure to the Swiss Federal Supreme Court, based either on a violation of Federal law or erroneous application of cantonal law, including arbitrariness of factual assumptions.

2. Building Regulations

As in the case of detailed zoning regulations, the actual building regulations are enacted by the cantons and applied by local building authorities. In addition to the regulations flowing directly from the requirements of the zone, in which a plot of land is situated, i.e. number of floors and permissible use of a building, the building regulations set down requirements with respect to technical issues (static, health and safety conditions, fire safety and the like) they contain provisions which set standards for the design and the aesthetic impression of a building. Usually a building is required to harmonize with its neighbourhood buildings and the environment. It need not be emphasized that such provisions grant the local building authorities wide discretion and often lead to fierce debates between the authorities on one side and owners and their architects on the other side, who have different ideas about what is tasteful.

3. Planning Procedures

In order to obtain a building permit, the petitioner has to submit to the competent authority of the municipality plans and documents that demonstrate that the project fulfils the following three requirements: (i) the intended building and its use is in conformity with the zone in which the land is situated, (ii) the property is connected or can be connected to the necessary utilities, such as electricity, sewer system etc., and (iii) fulfils the requirements of the applicable building regulations. After publication of the project in the local official gazette and after an opportunity has been given to all affected third parties to raise objections to the project, a building permit will be issued, if the competent building commission finds that the project is in accordance with all applicable legal provisions. Both the petitioner and third parties whose rights have been affected might appeal against the decisions of the municipal authority to higher administrative bodies and/or courts, depending on the procedural laws of the canton in question. Ultimately, an appeal can be brought before the Swiss Federal Supreme Court, which, however, conducts a very narrow review of the merits of the cantonal decision, limited to arbitrariness of factual

assumptions and blatant violations of the applicable legal provisions. In order to obtain answers on the permissibility of a project before going through the whole permit proceeding, the relevant plans and documents can first be submitted to the competent building commission. It will then issue a preliminary opinion, to which it is bound if subsequently a permit is requested based thereon. The cost and fees for obtaining the permit are negligeable, compared to the actual cost of the building itself. The most substantial cost in that phase of a project is the work that must be carried out by the architect, who is in charge of the necessary plans, and by lawyers, who are consulted to clarify building and zoning law issues which may arise.

4. Duration and Conditions of Building Permits; Enforcement and Penalties

Once a permit is issued, the owner has to start execution of the project within a certain period of time, which is determined by cantonal law; usually, this time-limit is two years. After that time-period, the permit expires. The permit might be granted with conditions attached, if the building commission finds that the requirements for a permit are not entirely fulfilled, but that nevertheless the legality of the project can be ensured if certain additional measures of minor importance are taken by the owner. A revocation of a building permit by the authorities is possible only if the project has not been executed and important public interest require the revocation thereof.

In order to ensure that the project is executed in accordance with the plans submitted in the planning proceedings, and that eventual conditions linked to the permit are fulfilled, the local building authority must be notified of all relevant steps of the execution. The authority will supervise the works and their conformity with the permit. Violations of the permit will – as, of course, any building activity without the necessary permit – lead to criminal as well as financial liability for the owner, and, if the subsequent granting of a permit is not possible, will result in an order to remove the illegal structures. If the owner refuses to follow such order, the authority has the power to cause the removal with the appropriate means at the owner's cost.

5. Building Standards Control and Supervision

The supervision of the safety of a building is exercised by a local authority commonly referred to as the “building police”. Its duty is the periodic supervision and control of larger, publicly accessible structures periodically and of regular buildings if there is any indication that there may exist unsafe conditions. If violations of the applicable safety standards are found, the owner will be granted a time-limit to remedy the situation. If no action follows, the building police might order the closing of the building and fine the owner; in order to restore safe conditions, the building police might cause the necessary works to be done at the owner’s cost.

P. Development of Real Estate

1. Structure of Development Projects

The most common organizational structure of a project is one in which the owner of a property hires a general contractor and finances the project from his own funds or obtains financing from banks as straight commercial loans secured by a mortgage on the property under development. If the owner is not in a position to undertake a project alone, he might take in a partner who can provide the financing and with whom he may enter a joint venture. That partner might be interested in the project for his own business purposes or can regard it as a pure investment opportunity. The formation of a separate corporation might facilitate the subsequent sale of the finished project to third parties. Another possibility is the additional involvement of future buyers or tenants, who might be interested in participating in the construction process in order to be able to influence the plans and construction works for the building so as to make it more suitable for their specific needs. In such a case, long-term leases would be concluded between the owner and future tenants, in order to give the tenant an opportunity to recover his investments. The owner of the property will, in addition to his intention of obtaining financing at attractive rates and associating himself with knowledgable and reliable business partners, closely scrutinize tax aspects of the organizational structure of the development closely. If a direct or indirect sale of the property is not possible because it would trigger undesirable tax consequences, a structure as described above might be an alternative.

2. Development Vehicles and Agreements

The agreements concluded by the partners of a development project may either be of a purely contractual nature or involve the establishment of a corporation for that purpose[109]. The considerations to be

[109] See chapter J.

made (by the parties) are essentially the same as those made in connection with any joint venture[110].

A common structure for the development of residential property aimed at individuals with modest resources are co-operative companies[111]. Prospective tenants of such housing schemes have to become a member of such a co-operative company in order to be eligible for an apartment. One of the reasons co-operative companies are used for such projects is that municipalities tend to be more willing to convey public land to entities which undertake that they will offer housing to the public at reasonable prices. Since co-operative companies are statutorily required not to aim at maximising profits but to primarily further the interests of their members, they are considered to fulfil that condition.

3. Building Contracts

a) Work Contract

A work contract (*Werkvertrag/contrat d'entreprise*)[112] is a contract whereby the contractor promises to produce a [work project] and the principal promises to pay a certain price for this. The essential feature of that contract is that the amount to be paid by the principal is due only if the work is carried out and completed as agreed. This is the typical framework of a construction work contract in the construction industry. The amount of compensation may consist either in a fixed price, which is stipulated in advance and generally excludes an increase except where extraordinary circumstances, which could not have been foreseen or which were excluded from the assumptions made by both parties, impede the completion, or the price may be determined pursuant to the value of the labour. The contractor usually bears the risk of success of his endeavours, especially where a fixed price is agreed on.

[110] See in that context *supra* J/4.
[111] See *supra* J/1/b.
[112] Articles 363 et seq. CO.

b) Mandate

By accepting a mandate (*Auftrag/mandat*)[113], the agent is obligated to carry out the contractually agreed business transactions or services with which he has been entrusted. Any contract which does not qualify as a special type of contract under provisions of the Code of Obligations is subject to the provisions of the mandate. The essential difference between a work contract and mandate is that the contractor under a mandate does not guarantee a success, must make every effort to achieve a success. He may therefore also be entitled to remuneration in cases where he is not able to reach his goal. Whereas most contracts in the construction context qualify as work contracts, the law of mandate has to be applied to some contracts where this is considered appropriate. This is the case, e.g. in the relationship between owner and architect, if the architect is not project manager at the same time.

c) Terms of Construction Contracts

Although the provisions regulating the work contract in the Code of Obligations are applicable to construction contracts, the parties are totally free to determine the terms of their agreement, such terms superseding the non-mandatory provisions of the Code. They will include into their agreements provisions governing the date of completion, consequences of prior termination, damages to be paid in case of default, and the conditions of payment. As far as the latter item is concerned, in larger projects, usually stage payments are provided, which entitle the contractor to draw a percentage of the total price whenever certain defined steps of the construction process have been completed.

d) Statutory Mortgage of Contractor

The contractor has right to place a statutory mortgage over the property in instance of non-payment for work done, which must be registered within three months after completion of the contractually agreed works (*Bauhandwerkerpfandrecht/hypothèque des entrepreneurs*)[114].

[113] Articles 394 et seq. CO.
[114] Articles 837 et seq. CC.

4. Parties Involved and Their Roles

In addition to the actual partners of a development project, i.e. owner and any additional partners, who together bear the financial risk of the project, additional persons or entities are involved who are entrusted with the execution and completion of the project as such. In this respect, an important role is played by the architect, who, usually supported by civil, mechanical or electrical engineers responsible for technical issues, must furnish the plans, which have to be drawn out in great detail in order to obtain a building permit. At that stage, the architect might work together with construction law experts, who make sure that the project will be in accordance with all applicable provisions of zoning, building and environmental laws and other regulations. The quality of the project at that early phase might also be one argument to attract investors and/or future buyers in order to secure the financing for the project. In addition to the architect by a special project manager, the actual execution of the project is then supervised.

5. Defects Insurance

Defects insurance must be provided by the parties that are contractually required to do so. Every architect or contractor in Switzerland has professional liability insurance covering events that may cause damages in connection with this person's professional activity. Especially in large projects for business developments, it is important to make sure that eventual delays are covered by insurance; in cases of *force majeure* none of the parties involved is liable.

6. Copyright

The copyright in the design of the building, insofar as protection under the applicable provisions of Swiss law is provided, remains with the architect. Recent disputes between renowned architects and owners have shown that it is not entirely clear under what circumstances and to what extent the owner of a building requires the per-

mission of the architect to alter the look or design of the building. This question might only become an issue, however, in cases of buildings that have an artistic value, and certainly not for standard buildings. In order to avoid such problems, the inclusion of a specific clause in the contract with the architect might therefore be advisable.

7. Fees

The fees of all parties involved in a project are subject to negotiation between the parties and should be agreed up on in advance. In the absence of an agreement on the fees, the consideration will usually be based on the existing tariffs of the respective professional organizations, although those tariffs are not mandatory. In cases of disputes as to the remuneration, a judge will certainly use such tariffs as one indicator for an appropriate remuneration, but will also take into account the local price level as well as the character of the work done in a special case.

Q. Literature

The following is a list of publications dealing with the issues discussed in this publication. In addition to few English books on Swiss law, we have included some of the most important books in German containing information that might be interesting.

I. English

AUF DER MAUR, ROLF — *Introduction to Swiss Intellectual Property Law*, Basel 1995.

HOCHSTRASSER, DANIEL/ VOGT, NEDIM PETER — *Commercial Litigation and Enforcement of Foreign Judgments in Switzerland*, Zurich 1995.

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II. German

AMONN, KURT — *Grundriss des Schuldbetreibungs- und Konkursrechts*, 5th ed. Bern 1993.

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