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Disclosure of Beneficial Owners and the Slow Death of Bearer Shares: The Implementation of the Recommendation of the Global Forum on Transparency

On 21 June 2019, the Federal Assembly passed the Federal Act on the implementation of the recommendations of the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Act). The Act is a further step towards increasing transparency in relation to the legal and beneficial ownership of shares of Swiss legal entities and marks the continuation of the Financial Action Task Force (FATF/GAFI) amendments of 2015 following the peer reviews led by the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) and the FATF. The Act prohibits the issuance of bearer shares for non-listed companies, unless they are issued as intermediated securities held with a Swiss custodian. It also introduces criminal law sanctions for breaches of the obligation to disclose the beneficial ownership of shares as well as for breaches of several corporate housekeeping duties generally, including the duty to properly keep a share register and a register of beneficial owners. In addition, it contains potentially draconian sanctions, including for holders of bearer shares who could eventually be expropriated without compensation if they do not comply with the disclosure requirements, and for companies which could eventually be dissolved if they do not comply with their duties to maintain corporate registers or if they unlawfully issue bearer shares. At the same time, the Act leads to welcome clarification around the disclosure of beneficial owners and addresses a number of issues that were subject to controversy until now.

Abolition of Bearer Shares

A central aspect of the Act will be the abolition of bearer shares for joint stock companies (article 622 (1bis) CO as amended), with **two exceptions**:

– First, companies with **equity securities listed** on a stock exchange will continue to be able to issue bearer shares (article 622 (1bis) CO as amended). This exception will, however, only be available to a limited number of companies.

– Second, other companies will be able to issue bearer shares only if the shares are **issued as intermediated securities** held by a Swiss custodian designated by the company (article 622 (1bis) CO as amended). Such intermediated securities are held on custody accounts through the banking system.

In both cases, **this fact will need to be registered with the commercial register** (article 622 (2bis) CO as amended). These measures go one step further than the reform introduced in 2015, which required share-

holders to disclose their identity to the company within a month of the acquisition of the shares, but was deemed to be ineffective in the peer review of the Global Forum.

Transitional regime

Notwithstanding several motions to allow companies which had complied with the previous regime to be grandfathered, parliament decided to vote in favour of the proposition of the Federal Council and also apply the abolition to existing companies; as a result, **existing bearer shares will need to be converted** into registered shares, subject to the two limited exceptions (for listed companies and certain intermediated securities) mentioned above.

To soften the blow, the Act provides for a transitional regime: the abolition will not be effective immediately when the Act comes in force. Instead, companies will have a period of **18 months to amend their articles of association** and convert their existing bearer shares into registered shares unless the shares are already issued as intermediated securities or the company has listed equity securities on a stock exchange or issued as intermediated securities held by a Swiss custodian. Even if one of the **exemptions** applies, the company will need to **record this fact with the commercial register** (article 2 of the Transitional Rules of the Amendment of 21 June 2019).

If bearer shares are still outstanding by the end of the transitional period of 18 months, they will be **converted by law into registered shares** (article 4 (1) Transitional Rules). The commercial registrar will be responsible for recording this change in the commercial register (article 4 (2) Transitional Rules). The change will also be effective against third parties (article 4 (1) Transitional Rules). Therefore, the shares will need to be endorsed to be transferred and the new acquirer will have to request the registration of their details in the share register. However, transfer restrictions will not apply to the transfer of such shares, which will retain their existing nominal value, voting rights and financial rights (article 4 (3) Transitional Rules).

To enforce a swift adjustment of the articles of incorporation after the 18 months interim period, the commercial register will not be allowed to complete any change to the articles of association until the company has implemented the changes to its articles of incorporation (article 5 (1) Transitional Rules).

Following the conversion, the Company will need to **register the holders of bearer shares who complied** with their disclosure duties in its share register (article 6 (1) Transitional Rules). If shareholders fail to comply with their disclosure duties, not only will they continue to see their voting rights suspended and lose their financial rights (article 6 (2) Transitional Rules), but they will need to **file a claim in court with the prior consent of the company within five years** of the entry into force of the Act, if they want **to have their rights reinstated**.

If **they miss this deadline**, their **shares will become null and void** by law and the shareholders will lose any rights they have to the shares. Instead, their shares will be replaced by treasury shares held by the company (article 8 (1) Transitional Rules). If the shareholders prove that they were not a fault, they will still have the right to apply to the court to be paid out the fair value of their shares, provided, however, the company has sufficient freely disposable equity to make this payment (article 8 (2) Transitional Rules). In all other cases, the law does not provide for a compensation of expropriated shareholders. However, it needs to be seen whether courts will leave shareholders disenfranchised, e.g., if the company does not consent to the reinstatement of rights without any valid grounds.

Changes to the Obligation to Disclose the Beneficial Owner

In addition to the abolition of bearer shares, the Act also amends the regime for the disclosure of the beneficial owner of shareholders acquiring, alone or in concert with third parties, **more than 25%** of the shares in a company. This regime continues to apply to all joint stock companies, regardless of whether they have issued bearer or registered shares and also to limited liability companies.

Control as the Determinant of Beneficial Ownership

The amendments clarify several controversial point:

– In particular, they define the beneficial owner of a legal entity as the **physical person exercising control by analogy with the consolidation rules** under Swiss accounting law (article 697*j* (2) CO as amended). Therefore, a physical person controls a legal person if it holds, directly or indirectly, a majority of votes in the highest management body, if it directly or indirectly has the right to appoint or remove a majority of the members of the supreme management or administrative body or if it is able to exercise a controlling influence based on the articles of association, the foundation deed, a contract or comparable instrument (article 963 (2) CO). This clarification solves numerous controversies concerning the definition of the beneficial owner in corporate structures and should therefore contribute to greater legal certainty.

– Furthermore, if no physical person controls a legal entity holding, alone or in concert with third parties, more than 25%, the latter is required to **make a negative declaration** (article 697*j* (2) CO as amended): so, where the shareholder is a state-owned entity, has dispersed ownership, or is set up structurally so that it cannot be controlled by natural persons, e.g. with certain charitable foundations, the shareholder must nevertheless make a declaration.

Regime for Listed Companies and their Affiliates

A further clarification concerns listed companies and their affiliates: when the shareholder is a listed company, is controlled by a listed company or controls a listed company, it is **not necessary to make a full declaration** regarding the beneficial owner. It is sufficient to declare this fact as well as the name and seat of the listed company (article 697*j* (3) CO as amended). This substantially simplifies the ongoing compliance burden, without decreasing the level of transparency, since the rules on the disclosure of substantial shareholding under the Financial Market Infrastructure Act (or similar foreign laws) ensure an appropriate level of disclosure for listed companies.

Deadline to Give Notice of Changes

One important amendment concerns alterations made due to changes of name, surname or address of the beneficial owner: currently, article 697*j* (3) CO does not specify the deadline to give notice of such changes to the company, which led certain commentators to take the stance that the notice is not subject to any timing constraints. To solve the controversy, the Act specifies that **shareholders have three months** to disclose the change to the company (article 697*j* (4) CO as amended).

Sanctions for non-compliance

To ensure effective compliance with the transparency obligations and the record keeping duties, the Act introduces new **criminal offences** in the Swiss criminal code:

– Pursuant to article 327 of the Swiss Criminal Code, the **failure to comply with the obligations to disclose the beneficial owners** of large shareholdings (including any changes) will be subject to a fine.

– Similarly, intentional breaches of the corporate law obligations relating to the **maintenance of the share register and the register of beneficial owners** and other similar registers will also be subject to a fine (article 327*a* of the Swiss Criminal Code).

These sanctions apply in addition to the corporate law effects of failing to comply with disclosure duties: namely the suspension of voting rights (article 697*m* (2) CO) and the loss of property rights until a proper notice is given to the company (article 697*m* (3) CO).

Furthermore, the **failure to duly maintain the required registers** or **unlawfully issuing bearer**

shares will constitute a violation of organizational duties which can, at the request of a shareholder, a creditor or the commercial register, lead the court to summon the company to comply with its duties or take steps to dissolve the company and liquidate it in accordance with bankruptcy law (article 731*a* CO as amended).

Outlook

The Act has now been approved by the Swiss parliament and will become law if no referendum is petitioned for. We expect that it enters into force shortly thereafter, **possibly as soon as October 2019** to remedy all outstanding issues prior to the next peer review.

Both companies and shareholders should carefully assess whether there is a need to act:

– All **companies which have issued bearer shares should act** and assess whether they are allowed to continue to have bearer shares, i.e. whether they have listed equity securities or have issued their shares as intermediated securities held by a Swiss custodian. If they are or ensure that they meet the requirements within the 18 months interim period, it is essential that they register in the commercial register the fact of their exemption to avoid a mandatory conversion. For the other companies with bearer shares, it may be advisable to prospectively convert bearer shares into registered shares, or at least to ensure that the conversion of bearer shares by law is properly reflected in the articles of association and the commercial register after the interim period of 18 months.

– Furthermore, **all companies, including those who have issued registered shares**, should assess whether they have an effective and compliant corporate housekeeping in view of the new criminal sanctions in case of non-compliance.

– Similarly, **shareholders** of non-listed joint stock companies and partners of limited liability companies should analyze whether they **hold bearer shares or more than 25% of the share capital** in any company, whether through bearer or registered shares. If so, they should carefully **review their existing filings** (and whether they made filings so far). Any deficiencies should be cured promptly and, if possible, before the new law enters into force to avoid the new criminal sanctions. In addition, holders of non-listed bearer shares must be particularly cautious, since they may, if they do not comply with the transparency requirements, need to go through a cumbersome court procedure to have their rights re-instated, and in some cases entirely lose their rights without compensation.

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