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Popular Initiative on Responsible Enterprises: Switzerland's Long Arm on Subject Enterprises

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Although its fate and timing are very unclear, the popular initiative "for responsible enterprises – for the protection of human rights and environment" (initiative on responsible enterprises; *Konzernverantwortungsinitiative*; *Initiative Multinationales Responsables*; "Initiative") is not only hotly debated among the many Swiss based international companies that would be affected by it, but also among lawmakers in Berne. In short, the Initiative, which is expected to be voted upon by the Swiss people, proposes that enterprises shall be held liable before a Swiss court if one of its controlled enterprises violates human rights or environmental standards abroad. These enterprises will have additional duties and will have to monitor and report on the compliance with these duties.

The Initiative raises a bundle of legal questions of which we focused on one: Its scope of applicability. As we will see, a far reaching concept is proposed to ensure that a large number of enterprises is subject to the Initiative.

By Thomas U. Reutter / Annette Weber

1) "Enterprises"

The Initiative is applicable to enterprises (*Unternehmen*) having their registered office, central administration (*Hauptverwaltung*) or principal place of business (*Hauptniederlassung*) in Switzerland ("subject enterprises"). The term "enterprise" shall ensure that all kinds of undertakings are captured, irrespectively of their legal form.

Although not stated in the proposal, the explanatory notes of the sponsors (the "Explanation") add that only private enterprises (*privat tätige Unternehmen*) fall under the scope of applicability. Hence, it seems that the intention is to exempt any enterprises which fulfil sovereign tasks. Enterprises controlled by a government are therefore not exempted if they act as private players.

2) Registered Office/Central Administration/Principal Place of Business in Switzerland

The Initiative provides an interesting mix of economic and legal concepts to ensure that not only businesses incorporated in Switzerland but also those managed out of Switzerland are captured: An enterprise must have either (i) its registered office, (ii) central administration (*Hauptverwaltung*) or (iii) principal place of business (*Hauptniederlassung*) in Switzerland. The registered office of an enterprise is the seat set out in the articles of incorporation. "Central administration" refers to the place at which the decision making or the management of an enterprise is made. The main activities (for example the main production of an enterprise's goods) define the principal place of an enterprise. The three places are meant to apply alternatively, *i.e.*, it is sufficient if one of them

is met. The concept was taken from the Lugano Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters. The sponsors thus follow the concept of an international treaty applicable to European countries rather than Swiss international private law in order to provide a maximum of fora legally possible.

3) Business Abroad

The Initiative limits its application indirectly by imposing duties which subject enterprises and their controlled enterprises (see below for a definition of "controlled enterprises") shall fulfil *abroad*. Enterprises (or their controlled enterprises) which do not have a business outside of Switzerland obviously do not have to adhere to the duties and are not subject to the liability regime set out in the Initiative.

The Initiative does not limit the application to specific foreign jurisdictions, for example, to jurisdictions which do not have similar human rights or environmental standards as Switzerland. As a result, enterprises with businesses, for example, in Germany, will be subject to the duties and the liability regime in principle, although in practice, the focus will be on enterprises with businesses in countries lacking a fully developed judicial system and rule of law.

4) Controlled Enterprises

Subject enterprises do not only have to ensure that they themselves comply with the duties set out in the Initiative but also the enterprises they control. The Initiative does not provide a definition of "control". Instead it states that the actual circumstances are decisive and that control may also be exercised by using economic power.

The term "control" as proposed by the Initiative appears to go beyond the usual concepts used in financial reporting and to again combine the relevant legal and economic concepts – to extend its reach or to avoid abuses – depending on the point of view. "Controlled enterprises" include therefore subsidiaries but may also extend to companies that are not consolidated into the relevant group of companies in case there is factual control over such outside enterprises. For example, a supplier which delivers exclusively to and is accordingly fully dependent on a subject enterprise (or one of its controlled subsidiaries) may be regarded as a "controlled enterprise".

However, a different reading of "factual control" may also lead to a narrower interpretation: The mere majority ownership of shares in a company, even though trigging financial consolidation requirements under most accounting standards, does not mean factual control. Accounting standards typically require the *ability* to exercise control by holding a majority stake in a company whereas the *actual* exercise of control is required for factual control which is a higher standard. For example, a passive majority shareholder – in the extreme a financial investor who is not represented on the board

of its subsidiary which runs local operations by local management independently – will hardly have factual control. "Factual control", *i.e.* some form of subordination expressed by the power to give binding instructions, is also required for the concept of liability of a principal vis-à-vis its agent (*Geschäftsherrenhaftung*) which provides the model for liability under the Initiative. Although hardly intended by the sponsors, one may not exclude that the concept of "factual control" may in certain cases lead to a scope of companies narrower than under most relevant financial reporting standards. In practice, the exercise of (factual) control (vs. the mere ability to exercise control) will be difficult to assess without further guidance in the transposing statute.

In the context of a group of companies, the Initiative does not require that the subject enterprise is the ultimate holding company of a group of companies. It therefore targets subsidiaries as well. International operating groups of companies will therefore have to carefully analyze whether one of its group companies fall under the scope of the Initiative.

5) SME

The Initiative does not provide for an exemption for international operating small and medium sized companies (SME). SME are only addressed in the sub-provision dealing with duties of diligence: "The lawmaker shall consider the needs of SME with low risks" implying that such SME shall have less extensive duties. The Explanation is somewhat misleading in the absence of a specific exemption for SME as such in stating that "SME are basically exempt from the Initiative unless they are active in a business of a high-risk sector". In substance, however, it seems rather obvious that SME shall not be subject to the same standard as multinational corporations. In case the Initiative is adopted, the legislator will have the discretion (but no duty) to include such an exemption in the statute transposing the Initiative because the duties and the liability set out in the Initiative are principle based.

6) Conclusion

The Initiative chooses a novel approach for its scope of application. Broad in concept, it limits its applicability in certain instances. The Initiative will impose also duties on foreign enterprises with a central administration or principal place in Switzerland and allow liability claims against such enterprises in Swiss courts although the relation to Switzerland will be remote in such cases. Multinational groups of companies may become subject to the Initiative by surprise as a result of the Initiative's extensive scope.

If the Initiative will be adopted, subject enterprises may try to either (i) minimize their business in Switzerland in a way that they will not be subject to the Initiative, (ii) exercise less control on subsidiaries or enterprises more generally, e.g. by outsourcing certain businesses to third parties, in order to avoid "factual control", or (iii) take more con-

trol over their subsidiaries and independent contractors in order to ensure compliance with the duties and to minimize liability exposure under the Initiative. The outcomes described in (i) and (ii) are hardly in the interest of corporate social responsibility while the outcome described in (iii) may not be in the interest of the foreign local enterprise and the local market at large. In any event, the Initiative, if adopted, will likely change the way business is done by international groups with substantial Swiss presence – potentially also in ways which were not intended by its sponsors.

Thomas Reutter (thomas.reutter@baerkarrer.ch)
Annette Weber (annette.weber@baerkarrer.ch)

Digital Assets – Proposed Amendments to the Legal and Regulatory Framework of Distributed Ledger Technology in Switzerland

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Switzerland targets adjustments of the existing legal and regulatory framework of distributed ledger technology (DLT). The Federal Council initiated consultation on proposed amendments to, *inter alia*, civil law (including securities law), insolvency law, financial market law, and anti-money laundering regulation on 22 March 2019. This article summarizes the key points of the suggested adjustments and analyses their potential impact on market participants. The content of the rules may still be subject to changes in the ongoing legislative process.

By Luca Bianchi / Fabio Andreotti

1) Introduction

In recent years, the blockchain and initial coin offering (ICO) industry has been subject to a very strong growth in Switzerland as well as globally (CapLaw-2016-47, 25 et seq.). As a consequence, regulators and legislators worldwide are in the process of solving two fundamental problems, namely: the ***regulatory mismatch*** between historically grown and, thus, outdated laws and innovative business models (***Problem 1***); and the ***lack of legal certainty*** for market participants caused thereby (***Problem 2***) (CapLaw-2017-02, 14; CapLaw-2016-31, 4). Solving these two problems increases the attractiveness of a country for the digital assets industry in a competitive international environment.

In this context, Switzerland has developed a pragmatic solution which suggests selective amendments to its existing laws. In particular, the Federal Council published a *Report on the Legal Framework for Distributed Ledger Technology and Blockchain in Switzerland* on 14 December 2018 (the ***Report***). Subsequently, the Federal Council