OUTSIDE PERSPECTIVES

Financial Institutions M&A in Switzerland

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1. Introduction

The consolidation process in the financial services industry is still rather slow, in particular when it comes to cross-border retail banking mergers, due to a number of political, legal and regulatory barriers even within the European Union. More activity is seen both in domestic and also cross-border M&A transactions in the private banking segment of the industry, where Switzerland's wealth management institutions rank among the top players. This article will highlight some of the main transactional and regulatory issues to be considered in financial institutions M&A transactions involving Swiss targets, with a particular focus on private banking services providers.

2. Transaction Structures

Generally, Swiss law provides for the following transaction structures for mergers and acquisitions:

- merger in accordance with the Swiss Merger Law (Fusionsgesetz), i.e. absorption or combination of two or more companies;
- demerger in accordance with the Swiss Merger Law, i.e. spin-off of a business in exchange for shares in acquiring entity to shareholders of transferring company;
- acquisition by way of purchase of shares (share deal);
- acquisition of assets (regular asset deal); and
- transfer of assets and liabilities (Vermögensübertragung) in accordance with the Swiss Merger Law; this newly introduced structure tool allows for a transfer of assets and liabilities by way of a transfer by law of an entirety of specific, hand-choosen assets and liabilities.

In financial institutions M&A, the preferred transaction structure is a share deal since it does not give rise to complex banking secrecy and operational issues in connection with the transfer of client relationships from one legal entity to the other as is the case in an asset deal. Asset deals are normally seen in cases of the purchase of the business of a branch office, only (in relation to which no share deal is possible) or where the acquiror is only interested in a specific group of clients (and not the entire clientele and business operations of the target bank).

In case of asset deals, the main question to be taken into consideration is about publicity and confidentiality, in particular regarding data protection and banking secrecy law. De-mergers and transfers of assets and liabilities (Vermögensübertragungen) by law require an inventory that has to be filed with the commercial registrar and thus is publicly available to any interested party. It is furthermore noteworthy that transfers of assets and liabilities (Vermögensübertragungen) require the filing of the purchase price, while in mergers and demergers some financial information, in particular the balance sheet of the transferring entity, has to be filed, but not necessarily the fair value of the transaction.

3. Particularities regarding Due Diligence

When inquiring whether or not a potential acquisition of a target entity may be of specific interest for the acquiror, the latter, based on the principle of caveat emptor, would in all likelihood be eager to know as much detail of the target financial institution as it possibly can prior to entering into negotiations and contract drafting sessions with the seller.

A legal due diligence, in general, would focus on the following key topics: Regulatory compliance, corporate matters, material contracts, litigation, real estate and leases/tenancy, tangible assets, IP/IT and data protection, employees, competition, environment, social security and insurance. When inquiring into the risks relating to the acquisition of a financial institution, the target's client relationships and the quality of the assets under control are of key relevance and must be thoroughly addressed. The due diligence process itself has to be handled in a way that Swiss banking secrecy and data protection provisions are complied with. As a general rule, bank clients' names may not be disclosed and have to be eliminated in the data room documents.

In due diligences regarding financial

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institutions a first provisional identification of regulatory "show-stoppers/deal-breakers" may be achieved by a review of the annual long form reports of the target's auditors to the supervisory authority and the internal audit reports.

4. Regulatory Requirements; New Rules on Consolidated Supervision

A new bank and broker/dealer license will have to be obtained from the Swiss financial services authority, i.e., the Federal Banking Commission ("FBC"), if the transaction leads to a new legal entity being the holder of the relevant licenses, e.g., in case of a combination, but not upon a share deal or an absorption (unless the absorbing entity does not yet have a bank license).

In the case of a share deal (being the most often used transaction structure), notification requirements and the obligation to obtain a so-called additional license from the FBC may apply; in addition, the requirement of consolidated supervision may have to be observed:

a) The acquisition or disposal of a qualified participation (10% or more of capital or voting rights) in a Swiss bank is subject to a notification obligation vis-a-vis the FBC; the notification has to be made prior to closing; the FBC will intervene if the acquiror may have a negative impact on a prudent and solid business activity of the target bank (e.g., reputational risk). This notification duty also exists whenever a qualified participation reaches, exceeds or falls below the thresholds of 20, 33 and 50 % of the voting rights or the capital.

b) A so-called additional license is required if a non-Swiss person or entity purchases a qualified shareholding in a target bank that is or will be (as a consequence of the transaction) under foreign, i.e. non-Swiss control. The requirements for the granting of such additional licence are: (i) the country of residence of the purchaser must guarantee reciprocity, or be a WTO/GATS-member, (ii) the company name of the bank shall in no way indicate that the target bank is Swiss controlled and (iii) in case of the target bank being or becoming part of a financial group, consent to the transaction must be granted by the foreign supervisory authority.

c) If a bank, as a consequence of a transaction, becomes part of a financial group or conglomerate: the new articles 3b – 3h of the Swiss Federal Banking Act require that such group or conglomerate be subject to adequate consolidated supervision by the lead/home supervisory authority of such group.

Under the new Federal Act on Insurance Supervision (Versicherungsaufsichtsgesetz, "VAG"), entering into force as of January 1, 2006, several notification and approval obligations apply with regards to insurance companies subject to Swiss supervision by Swiss Federal Office of Private Insurance ("FOPI"). Such obligations towards FOPI apply not only to the insurance company regarding its participations and its shareholders, but also to buyers and sellers of participations in insurance companies as well as, in certain cases, to any substantial (insurance or non-insurance) acquisitions and divestitures by insurance business-dominated financial conglomerates. ■