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Switzerland: Grappling with the financial assistance rules

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Recent case law addresses the granting of an upstream or cross-stream: (1) security (*eg,* granting of a guarantee) by a Swiss subsidiary to secure obligations of its parent company or any of its affiliates, other than 100 per cent direct or indirect subsidiaries; or (2) loan (also in the form of cash pools) by a Swiss subsidiary to its direct or indirect parent company or to any of its affiliates, other than 100 percent direct or indirect subsidiaries.

Such financial assistance must:

- be allowed by the Swiss subsidiary's articles of association, which shall include the purpose of group support and financial assistance
- be in the interest of the Swiss subsidiary (*ie*, dealing at arm's length, provision against consideration, review of importance of the security or loan compared to the other assets of the companies involved and financial capacity of the recipient) and
- not constitute a repayment of the equity capital of the Swiss subsidiary or an unjustifiable contribution.

Otherwise, in case any doubt arises (in particular regarding whether the relevant case constitutes an arm's-length transaction), the amount of the security or loan shall be limited to the freely distributable funds of the Swiss subsidiary that needs to be blocked in the amount of the security or loan. Furthermore, the subsidiary's shareholders' meeting shall resolve on and approve the granting of such security or loan.

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Non-compliance

"If an up-stream or cross-stream transaction does not meet the financial assistance rules as outlined above, the transaction may be null and void."

If an up-stream or cross-stream transaction does not meet the financial assistance rules as outlined above, the transaction may be null and void (*eg,* because it violates the company's purpose clause or it infringes the protected equity capital of the company); can be challenged by the company or its shareholders; and may lead to directors' liability.

Tax

Should a financial assistance issue arise from a corporate law perspective (*eg,* if an upstream loan exceeds the distributable reserves of the respective Swiss company), no Swiss tax consequences should be triggered. However, if a subsidiary has granted an upstream or cross-stream loan and the granting of the loan was not in the interest of the subsidiary, or did not meet the dealing at an arm's-length standard in another way (*eg,* in cases in which the repayment of the loan has been unlikely from the beginning), the Swiss tax authorities may, depending on the individual case, requalify this loan as a constructive dividend distribution.In this circumstance, the loan is subject to Swiss withholding tax of 35 percent (or 53.8 percent grossed-up if the Swiss withholding tax has not been transferred to and is not borne by the recipient).

Further, to avoid any deemed dividend distribution subject to Swiss withholding tax, the thin cap rules and the safe-haven interest rates as annually published by the Swiss Federal Tax Administration need to be observed. Alternatively, evidence needs to be provided that the applied interest rate complies with the arm's-length principle.

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