Dear clients and business friends,

On 3 March 2013, a majority of the Swiss electorate voted in favour of the so-called Minder Initiative. In addition to transitional arrangements, the Minder Initiative comprises 24 demands formulated as “principles” at the constitutional level (Art. 95 (3) of the Federal Constitution), that primarily address the issue of board and executive compensation at listed Swiss companies.

In view of the (necessary) clarifications and implementation of the new constitutional provisions, a number of complex questions raised by the Initiative will have to be answered by the Federal Council and legislators. In particular a number of questions will need answering in connection with the competencies of the general meeting of shareholders regarding salaries, inadmissible payments, the voting behaviour of pension funds, the level of detail of new provisions of the articles of association and the criminal law provisions.

Below, we discuss (but without any promises to be comprehensive) a few open questions as well as possible answers. In addition, you will find a summary overview of the new articles of the Constitution.

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1. Do the provisions of the Minder Initiative apply with immediate effect?

The Minder Initiative will bring about a partial revision of the Federal Constitution (Cst), inserting a new Art. 95 (3) Cst. The provisions of Art. 95 (3) Cst are to be understood as a mandate to legislators and are thus not directly applicable.

As a first step, the Federal Council is now required to enact, in accordance with the transitional provisions adopted as part of the Minder Initiative, the required (preliminary) implementation provisions by way of an ordinance, and has one year since adoption of the Initiative to do so, i.e. by 3 March 2014 at the latest. In the event that the Federal Council enacts the implementation ordinance in the course of the current year, it is conceivable that these provisions could apply as early as the 2014 financial year.

In substantive terms, the Federal Council is bound, when enacting implementation provisions, by the framework set forth in the text of the Initiative. To the extent doing so would be compatible with Art. 95 (3) Cst, the Federal Council is certainly free to consider the content of the so-called indirect counter-proposal to the Minder Initiative elaborated by Parliament and which, as such, will no longer come into play.

As a second step, the Swiss Federal Parliament, in its capacity as legislator, will need to enact the necessary statutory provisions in order to implement Art. 95 (3) Cst. There is no time limit that dictates when these statutory provisions must be enacted. The entry into force of the final bill is thus not to be expected before 1 January 2015. It is may be assumed that the statutory implementation of the Minder Initiative will be incorporated into the ongoing revision of the law on companies limited by shares. Accordingly, the legislative objectives of this yet to be enacted revision of the law on companies limited by shares will extend beyond the scope of the Minder Initiative and encompass a range of other issues besides compensation (e.g. organisation of the equity capital, claw-back actions; liability of the auditors, etc.).

2. What companies are subject to the Minder Initiative?

Article 95 (3) Cst shall be exclusively applicable to Swiss companies limited by shares that are publicly listed in Switzerland or abroad. Swiss companies limited by shares are companies that have been incorporated under Swiss law and that are entered into the commercial register. Where a company happens to be publicly listed in Switzerland, but was not incorporated as a Swiss company limited by shares, it will, as a consequence, not fall within the scope of application of the Minder Initiative.
3. How must the General Meeting of Shareholders vote in future with regard to executive compensation?

Pursuant to Art. 95 (3) Cst, the General Meeting of Shareholders (GMS) will vote annually with regards to the aggregate amount of all compensation for the Board of Directors (BoD), the Executive Management (EM) and where applicable, the Board of Advisors. It is to be assumed that the resolution of the GMS will be binding (and not be a mere recommendation).

The wording as set forth in the provision does not require that a separate vote be held for each individual compensation package of the executive board members. But it is to be assumed that in future, a separate vote will take place in the GMS on the aggregate amounts to be paid to each of the different bodies, i.e. mainly BoD and EM, in their entirety.

In the context of the provisions governing compensation, many questions still remain unanswered. How, in particular, should bonus payments be dealt with, given that typically they can only be determined following the end of the financial year? Can these be approved retroactively, or must an overall budget allocation be approved in advance covering the next financial year as a whole? What elements will comprise the entirety of the compensation package? What happens if the applicable budget allocation is exceeded during the course of a given year (e.g. in the case of personnel changes in the EM); is it permissible that at the next GMS, a supplementary budget be submitted for approval, or is the originally approved budget irrevocable? Or – as an alternative to voting on an aggregate budget allocation – will the solution already set forth as part of the indirect counter-proposal be adopted. That is, an advance vote takes place with regard to base salary, with a subsequent vote taking place at the next annual GMS with regard to prior year additional (variable) compensation? It will be a matter for the implementation provisions and the implementing legislation, to provide unambiguous and practicable (as much as possible) solutions to these issues.

What is clear despite the many current uncertainties is: Article 95 (3) Cst does not seek to introduce an effective upper compensation threshold. Nevertheless, the rights of shareholders have been strengthened in the area in question.

The adoption of the Minder Initiative will, as a rule, not have any impact on the transparency provisions set forth in Art. 663bis OR governing compensation at publicly listed companies, in that these provisions will remain in force. Accordingly, in the notes to the balance sheet, companies will still need to disclose, inter alia, the aggregate sum paid as compensation to the BoD as well as the amount paid to each of the members of the BoD, including his or her name and function. For the EM, the corresponding information must include, in addition to the aggregate amount paid out, the name of and function of the most highly paid member of the EM and the amount he or she was paid.

**An overview of the new Art. 95 (3) Cst**

<table>
<thead>
<tr>
<th>Approval of compensation packages by the General Meeting of Shareholders (GMS)</th>
<th>The GMS must vote annually on the aggregate amount of all compensation for the Board of Directors and the Executive Management (and where applicable the Board of Advisors). The GMS vote is mandatory and binding.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extraordinary forms of compensation</td>
<td>Severance payments or other payments, payments in advance and fees and premiums for company acquisitions to members of governing bodies are prohibited. Also prohibited are (additional) consulting or employment contracts at another group company.</td>
</tr>
<tr>
<td>Election of Board of Directors, members of the Executive Management and the Compensation Committee</td>
<td>The GMS elects annually and individually the members of the Board of Directors, the Chairman of the Board of Directors, and the members of the Compensation Committee.</td>
</tr>
<tr>
<td>Rules in the articles of association</td>
<td>The articles of association must by law contain the following provisions: rules on the amount of credit extended, loans and pensions of board members of governing bodies; bonus and incentive schemes of governing bodies; the number of mandates entrusted to members of governing bodies outside the group, and the term of employment contracts of members of the Executive Management.</td>
</tr>
<tr>
<td>Voting at the GMS</td>
<td>Voting by proxy at the GMS will continue to be admissible. An independent proxy must be elected by the GMS on an annual basis. Proxies to governing bodies and portfolio representation are illegal. Pension funds that are shareholders must vote in the interest of the insured members and disclose their voting behaviour. Shareholders must be provided with the possibility to cast their votes electronically.</td>
</tr>
<tr>
<td>Delegation of management of the company</td>
<td>Management of a Swiss publicly listed company cannot be delegated to a juridical person.</td>
</tr>
<tr>
<td>Criminal law provisions</td>
<td>Violations of the provisions of Art. 95 (3) Cst are punishable with imprisonment (up to three years) and a fine (up to six times annual remuneration).</td>
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4. What is to be understood as constituting illegal “severance or other payments” and “payments in advance”?

4.1 Severance or other payments

The term “severance or other payments” is not further defined in the text of the Initiative. We are hopeful that the Federal Council or legislators will find a practicable definition.

In general, severance payments are payments that are triggered by the termination of an employment relationship. Prohibited severance payments should only be constituted by contractually agreed payments and not payments owed by virtue of (labour) law provisions. We are of the opinion that it will be necessary to clearly distinguish between remuneration for services performed or compensation for a specific disadvantage caused by the termination of the employment relationship (e.g. compensation for unused annual leave) on the one hand, and compensation that is intended to facilitate the departure of an employee that does not constitute remuneration for work or a specific disadvantage on the other (so-called “golden parachutes”). It is our view that only the latter should fall within the scope of prohibited severance payments.

The term “other payments” should be understood as “payments similar to severance payments”. This might include for example disguised severance payments, with which the same outcome is achieved as is sought with a severance payment (e.g. unusually generous compensation for a post-employment non-competition clause). These “other payments” will not necessarily constitute payment of a sum of money, but could conceivably encompass other forms of compensation (e.g. an additional pension fund contribution or a lavishly well-paid consultant contract). An unusually long notice period for termination could also fall within the scope of the term “other (severance) payments”. At the end of the day, much is likely to depend on the circumstances of a given case.

4.2 Advance payments

The precise meaning of the term “payments in advance” is also unclear. What is likely to be clear is that this term encompasses salary payments made in advance of work that has yet to be performed. How does this relate, however, to starting or transfer bonuses that are intended to compensate a new BoD or EM member for the loss of any entitlements vis-à-vis his previous employer (e.g. the forfeiture of stock options or the loss of pension fund benefits)? Such cases do not, when viewed objectively, constitute cases of “advance” salary payments. Rather, these constitute direct compensation for disadvantages occasioned by the change of employer. Such payments might in fact be allowed based on the mere wording of Art. 95 (3) Cst, however clarity on this point will be required.

It is conceivable that companies will be tempted to pay a higher basic salary as an alternative to offering payments in advance. The extent to which such (potentially circumventing) practices will even be identifiable and whether it will be possible to capture them within the scope of a statutory provision is a question that, for the moment, remains unanswered.

5. Does the Minder Initiative have an impact on how GMS will be conducted in future?

5.1 Voting by proxy

The adoption of the Minder Initiative will affect, in various ways, how future GMS will be conducted. In the future, independent proxy voting will be the only admissible form of institutional voting by proxy. Proxies to governing bodies and portfolio representation, on the other hand, will in future be illegal. The independent proxy is to be elected each year by the GMS and can no longer be directly appointed by the company. It seems clear that a legal entity can also be considered for the role of independent proxy. It is also clear that the independence of the proxy holder will be more heavily weighted in the future than has been the case in the past.

The wording of Art. 95 (3) Cst does not provide any guidance on the modalities of proxy representation by independent proxy and in particular how the shareholder’s instructions are to be issued, as well as how to proceed when such instructions are incomplete. Here there is need for further regulation.

5.2 Electronic casting of votes

Art. 95 (3) Cst requires that shareholders be allowed to cast their vote at the GMS “by electronic voting from a remote location”. The central question is whether the intention here is to allow direct participation at the GMS by electronic means and thus the conduct of a virtual GMS, which might include the possibility of voting, asking questions and tabling proposals in real time. Statements made in the context of the Initiative Committee would indicate that those behind the Initiative only wished to make the electronic casting of votes possible.

Whether electronic votes can or even must be cast in advance is currently an open question. It is also an open question as to whether it is sufficient that shareholders are merely provided the possibility to cast their votes by instructing the independent proxy by electronic means.

Clearly not prescribed by the Minder Initiative is the possibility of an exclusively virtual GMS without a specific meeting place, as was set forth in the indirect counter-proposal.

Even if all outstanding issues have not yet been clarified, electronic voting from a remote location is likely to require most affected companies to take appropriate technical measures or at least to have recourse to a corresponding service provider, specialising in the electronic casting of votes.

6. How detailed do the rules covering incentive and bonus schemes need to be articulated in the articles of association?

Art. 95 (3) Cst provides that bonus and incentive schemes, the amount of credit extended, loans and pensions paid out, and the number of mandates entrusted to members of company boards must be governed by the articles of association.

Based on the text of the Initiative, one could be of the view that the entirety of any bonus and incentive schemes must be included in the articles of association. However, because the rules governing such schemes are often extensive and complex, and because even minor modifications to these rules would involve amendments to the articles of association, this is likely to prove impracticable in our view. A more meaningful and practice-oriented approach would be to include the essential guidelines and cornerstones of such schemes (circle of beneficiaries, basis for calculations etc.) in the articles of association and to regulate the details in a separate set of compensation regulations to be approved by the GMS. Changes to the regulations would still require the approval of the GMS, but would – contrary to the articles of association – not need to be publicly notified and entered in the commercial register. It is clear that such a
solution would need to be clarified in the implementing legislation.

With regard to those points that must by law now be included in the articles of association (amount of credit extended, loans and pensions paid out, and the number of mandates entrusted to members of company boards), it is likely that including rules on these directly in the articles of association would be practicable. Here too however, it is conceivable that this might be achieved by means of a generally worded clause in the articles of association including a reference to regulations subject to approval by the GMS.

7. What impact is the Minder Initiative likely to have on pension funds?

Art. 95 (3) Cst requires that pension funds vote “in the interest of their insured members”. The term “pension fund” has not been clarified in more detail. This term certainly comprises those pension funds and investment trusts subject to the Federal Act on Occupational Old Age, Survivors’ and Invalidity Insurance (BVG). Contrary to the view (also) expressed in the context of the struggle for the public vote, it is our opinion that the new requirement does not include an obligation on the part of the pension funds to vote. Nevertheless, pension funds will no longer have complete free discretion not to participate in the GMS. The implementing provisions will need to provide clarity on this point.

Where pension funds do vote, however, it is clear that they must do so “in the interest of their insured members”. Holding an annual survey to determine what these interests might be is likely to be barely practicable. In addition, this is certainly not directed at the individual interests of the insured members but rather their interests as a whole. It has been well argued that exercising the right to vote and thus determining the interests of the insured members is part and parcel of the management and administrative functions of the pension fund management. Accordingly, it would seem appropriate to let the supreme management bodies of a given pension fund decide what is in “the interests of its insured members”. Because these bodies (at least in the case of pension funds) are by law required to have an equal number of employee and employer representatives, it is our opinion that this provides sufficient certainty that the pension fund’s voting behaviour in the GMS will be determined in an objective manner in the interest of the insured members. Additionally, one could also require that when determining the pension fund’s voting behaviour, in any event the consent of all employee representatives would be needed.

A certain degree of oversight particular for the insured members will already be provided by the fact that pension funds will be required to disclose their voting behaviour.

8. Who are the criminal provisions directed against?

One of the greatest challenges, if not the greatest challenge in implementing Art. 95 (3) Cst arises from the criminal law provisions. The text of the constitution only mentions that violations of the provisions of Art. 95 (3) Cst are to be punishable by imprisonment up to three years and fines of up to six times the perpetrator’s annual compensation. Which actions and factual elements will ultimately lead to criminal sanctions and whether in any event, intent will be a statutory prerequisite, will necessarily have to be governed by formal legislation (at the level of a decree or legislative decree).

With regard to the potential group of perpetrators, this includes those persons, who, as a result of their position or function in the company, would even be capable of committing a violation of the provisions of the Initiative. This would in particular include members of the BoD, the EM and other persons entrusted with the management of the company’s affairs, as well as members of management bodies at pension funds. However, even recipients of proscribed forms of compensation could be potential perpetrators and thus criminally liable.

9. Summary/Recommendations

Even if many open questions remain in the context of implementing Art. 95 (3) Cst as well as with regard to the entry into force of the implementation provisions and the final statutory norms, companies affected by the Minder Initiative are recommended to begin planning for implementing Art 95 (3) Cst in a timely manner. In addition, developments as they unfold over the next 12 months should be carefully observed. Concrete implementation measures (e.g. amending articles of association, introducing virtual GMS) would appear somewhat premature given that the contents of the implementing ordinance from the Federal Council are still unknown.