

**THE LAW GOVERNING COMPANIES IN  
SWISS PRIVATE INTERNATIONAL LAW**

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- I. Introductory Remarks
- II. Notion of Company
  - A. Organized Associations of Persons and Organized Units of Assets (Article 150 Swiss PIL Act)
  - B. Evaluation of the Organization Factor
- III. The Incorporation Theory
  - A. The *Lex Societatis*
    - 1. Law of the Place of Organization (Primary Rule) and Law of the Place of Central Administration (Subsidiary Rule) (Article 154 Swiss PIL Act)
    - 2. Scope of Application of the *Lex Societatis* (Article 155 Swiss PIL Act)
  - B. Recognition *Ipsa Jure* of the Existence of a Foreign Company
  - C. Branches of Foreign Companies in Switzerland
    - 1. Application of the *Lex Societatis* of the Mother Company
    - 2. Application of Swiss Law to Certain Matters (Article 160 Swiss PIL Act)
  - D. The Incorporation Theory in European Community Law
- IV. Correctives to the Incorporation Theory in Favour of Third Parties
  - A. Necessary Correctives to the Incorporation Theory
    - 1. Restriction of the Freedom of Incorporation in Cases of Abuse or Fraudulent Conduct
    - 2. Development of Community Case Law
  - B. Restriction of Representation Power (Article 158 Swiss PIL Act)

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\* This section contains summaries of books recently published by young authors in languages other than English.

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- C. Liability for a Foreign Company (Article 159 Swiss PIL Act)
    - 1. Application of Swiss Law instead of the *Lex Societatis*
    - 2. Conditions of Application of Article 159 Swiss PIL Act
    - 3. Consequences of Application of Article 159 Swiss PIL Act
    - 4. Jurisdiction of Swiss Courts (Article 152 Swiss PIL Act)
  - D. Public Policy Exceptions
    - 1. Public Policy Clause (Article 17 Swiss PIL Act)
    - 2. Application of Mandatory Provisions of Swiss Law (Article 18 Swiss PIL Act)
    - 3. Observance of Mandatory Provisions of Foreign Law (Article 19 Swiss PIL Act)
  - E. Exception Clause (Article 15 Swiss PIL Act)
  - F. The *Fraus Legis* Principle
    - 1. Application of the *Fraus Legis* Principle in Company Law
    - 2. Consequences of Application of the *Fraus Legis* Principle as a Corrective to the Incorporation Theory
- V. Changing the *Lex Societatis*
- A. The Law Applicable to the International Transfer of a Company
    - 1. Transfer of a Foreign Company to Switzerland (Articles 161 and 162 Swiss PIL Act)
    - 2. Transfer of a Swiss Company Abroad (Article 163 Swiss PIL Act)
  - B. The Law Applicable to International Merger, Demerger and Transfer of Assets and Liabilities
    - 1. The Law Applicable to International Merger
      - a) Merger from abroad to Switzerland (Article 163a Swiss PIL Act)
      - b) Merger from Switzerland abroad (Article 163b Swiss PIL Act)
    - 2. The Law Applicable to International Demerger
      - a) Demerger from abroad to Switzerland (Article 163d cum Article 163a Swiss PIL Act)
      - b) Demerger from Switzerland abroad (Article 163d cum Article 163b Swiss PIL Act)
    - 3. The Law Applicable to International Transfer of Assets and Liabilities
      - a) Transfer of Assets and Liabilities from abroad to Switzerland (Article 163d cum Article 163a Swiss PIL Act)
      - b) Transfer of Assets and Liabilities from Switzerland abroad (Article 163d cum Article 163b Swiss PIL Act)
    - 4. The Law Applicable to Merger, Demerger and Transfer Contracts (Article 163c Swiss PIL Act)
  - C. Common Provisions Applicable in Cases of Emigration of a Swiss Company
    - 1. Protection of Rights of Creditors and Partners prior to Deletion from the Register of Commerce (Article 164 Swiss PIL Act)
    - 2. Jurisdiction for Actions for Examination of Participation and over Membership Rights (Article 164a(1) Swiss PIL Act)

- 3. Retention of the Place of Debt Enforcement and Jurisdiction in Switzerland (Article 164a(2) Swiss PIL Act)
- D. Recognition of International Transfers of a Company, Mergers, Demergers or Transfers of Assets and Liabilities among Foreign Companies (Article 164b Swiss PIL Act)

## VI. Conclusion

## I. Introductory Remarks

In the Swiss Federal Private International Law Act of 18 December 1987 (hereinafter: Swiss PIL Act), the Swiss legislator has, with respect to companies, opted for a system of conflict of law rules referring primarily to the incorporation theory. This system is gradually being completed by the case law of the Swiss Federal Court,<sup>1</sup> which clarifies the exact scope of application of the law governing companies – i.e., the *lex societatis* – determined by the Swiss PIL Act.

The purpose of this article is to give a short overview of the system of connecting factors applied to companies under the Swiss conflict of law rules and to discuss the two main issues which distinguish the Swiss system from the traditional incorporation theory: the existence of correctives to the incorporation theory in favour of third parties and the possibility to change the *lex societatis* without any prior liquidation or new formation.

A survey of the case law of the European Court of Justice (hereinafter: ECJ) concerning the freedom of establishment will draw a parallel between Swiss law and European Community law.

## II. Notion of Company

### A. Organized Associations of Persons and Organized Units of Assets (Article 150 Swiss PIL Act)

In terms of Swiss private international law, a company means 'any organized association of persons and any organized unit of assets' (Article 150(1) Swiss PIL Act). The purpose of such a wide notion of company is to assign every entity to the legal

<sup>1</sup> The Swiss Federal Court is the highest Swiss Court; its decisions are cited as follows when published: ATF (= Arrêt du Tribunal Fédéral) 124 (= volume) II (= indicating the area of law) 15 (= page).

category of 'companies', provided it has a solid organization or is at least organized as a whole.<sup>2</sup>

An entity without sufficient organization is governed by the provisions on contracts (Article 150(2) Swiss PIL Act).<sup>3</sup> Hence, if an entity is not sufficiently organized in the sense of Article 150 Swiss PIL Act, regardless of its legal status or form of association, it will be classified in the legal category of 'contracts' under Swiss private international law (Articles 112 *et seq.* Swiss PIL Act). Otherwise, it will be governed by the provisions on companies (Articles 150-165 Swiss PIL Act).

The notion of company in Swiss private international law differs from the one in Swiss substantive law<sup>4</sup> and is thus autonomous. The composition of a company (i.e., either an association of persons or an association of companies or a unit of assets), its legal status (with or without legal personality), the nature of its purpose (profit or non-profit) and its form of association (partnership, corporation, limited liability company, cooperative, etc.) are of no significance for its classification in the legal category of 'companies' in Swiss private international law. Thus not only the forms of companies existing in Swiss substantive law but also other forms of associations of persons or units of assets existing in foreign substantive laws but unknown to Swiss substantive law,<sup>5</sup> i.e., any analogous legal relationships of foreign type, will fall into the legal category of 'companies' if they are organized in the sense of Article 150(1) of the Swiss PIL Act.

It follows from this autonomous notion of company under Swiss conflict of laws that there is no *numerus clausus* of companies in Swiss private international law, contrary to the basic principle of Swiss substantive law.<sup>6</sup>

<sup>2</sup> See *Projet de loi de la commission d'experts et Rapport explicatif – Loi fédérale sur le droit international privé*, Zurich 1978, p. 346.

<sup>3</sup> Article 150(2) Swiss PIL Act reads: 'Simple partnerships without any organisation shall be governed by the provisions on contracts (Art. 116 *et seq.*)'. This wording is misleading and should read as follows: 'Entities without sufficient organization shall be governed by the provisions on contracts.' See GUILLAUME F., *Lex societatis – Principes de rattachement des sociétés et correctifs institués au bénéfice des tiers en droit international privé suisse*, Zurich 2001, pp. 14 *et seq.*

<sup>4</sup> See Article 530(1) of the Swiss Code of Obligations and *infra* II. B.

<sup>5</sup> See *Projet de loi* (note 2), p. 346; DUTOIT B., *Commentaire de la loi fédérale du 18 décembre 1987*, 3<sup>rd</sup> ed., Basel/Geneva/Munich 2001, ad Art. 150, No 3, p. 483; VON PLANTA A., in: HONSELL/VOGT/SCHNYDER (eds.), *Kommentar zum schweizerischen Privatrecht – Internationales Privatrecht*, Basel/Frankfurt am Main 1996, ad Art. 150, No 1, p. 1121; VISCHER F., in: GIRSBERGER ET AL. (eds.), *Zürcher Kommentar zum IPRG*, 2<sup>nd</sup> ed., Zurich 2004, ad Art. 150, No 1, p. 1724.

<sup>6</sup> See Article 530(2) of the Swiss Code of Obligations, which provides that any entity that does not fulfil the prerequisites of one of the Swiss legal forms of company is deemed to be a simple partnership.

## B. Evaluation of the Organization Factor

By generally referring to the organization of an entity, an element that must be evaluated in each individual case, Article 150 Swiss PIL Act leaves the decision to the discretion of the judge.<sup>7</sup> When applying this rule, the Swiss judge must classify<sup>8</sup> the entity concerned, i.e., evaluate several factors connected with the structure of the entity concerned<sup>9</sup>, in order to determine whether its internal organization is sufficient so as to be recognized by third parties.<sup>10</sup> If the judge decides in the affirmative, the entity concerned falls into the legal category of 'companies'.

Since the classification must be made on a case-by-case basis, it is not possible to discuss every element that can be taken into account when classifying an entity as a company. Nevertheless, some basic elements can be presented to shed light on the mechanism of classification in the field of company law.

As regards an association of persons, reference can be made to the notion of 'company' in Swiss substantive law. According to Article 530(1) of the Swiss Code of Obligations (hereinafter: Swiss CO), a company is 'a contractual relationship between two or more persons to attain a common purpose by joint efforts or means'. If the form of organization of the entity to be classified is similar to one of the Swiss companies (general partnership, limited partnership, corporation, corporation with unlimited partners, limited liability company, cooperative, association or foundation), its degree of organization will most probably be sufficient in the sense of Article 150(1) of the Swiss PIL Act to fall into the legal category of 'companies'. On the other hand, if the entity concerned does not have the characteristics of one of the Swiss forms of company, it will be considered as a Swiss Simple Partnership in the sense of Article 530(2) of the Swiss CO and its classification in the category of 'companies' will be more problematic. In such a case, the following elements can be taken into consideration when classifying an entity in the legal category of 'companies': (1) the common purpose of the members of the entity; (2) a certain degree of independence of the entity from its members; and (3) the designation of at least one member as representative of the entity towards third parties. We are of the opinion that if these three factors are present, the entity concerned will be considered as a company under the Swiss conflict of laws.

<sup>7</sup> *Projet de loi* (note 2), p. 346.

<sup>8</sup> The classification is made on the basis of the law of the forum; this principle has been accepted for a long time in Swiss law. See, e.g., ATF 96 II 78; ATF 108 II 442.

<sup>9</sup> DUTOIT B. (note 5), ad Art. 150, No 4, p. 484; VON PLANTA A. (note 5), ad Art. 150, No 18, p. 1126.

<sup>10</sup> DUTOIT B. (note 5), ad Art. 150, No 4, p. 484; EBENROTH C.T./MESSER U., 'Das Gesellschaftsrecht im neuen schweizerischen IPRG', in: *Revue de droit suisse* 1989 I, pp. 49-106, at p. 67; VON PLANTA A. (note 5), ad Art. 150, No 18, p. 1126; SCHWANDER I., *Einführung in das internationale Privatrecht – Zweiter Band: Besonderer Teil*, St. Gallen 1997, No 721, p. 319.

The notion of 'unit of assets' does not exist in Swiss substantive law and is not defined in the Swiss PIL Act either. To be considered as a company, the unit of assets must be at least organized as a whole. This notion can be compared with the notion of association of persons: the factor of organization is the same for both types. In our opinion, at least three requirements must be fulfilled in order for a specific unit of assets to be included in the notion of 'company' as defined under Article 150(1) of the Swiss PIL Act: (1) one or several persons – natural person or legal person – must own and manage the unit of assets for the benefit of one or several beneficiaries; (2) the assets must be organized as a separate patrimony, which implies that these assets are independent of the owner's or manager's assets; and (3) the assets must have been combined to pursue a special purpose.

The notion of 'unit of assets' of Article 150(1) of the Swiss PIL Act seems to be 'tailor made' for a trust. We are of the opinion that a trust fulfills in principle the requirements of the organization factor set forth in Article 150(1) Swiss PIL Act.<sup>11</sup> However, as the classification must be made on a case-by-case basis, a specific trust may nevertheless be classified in the legal category of 'contracts'.<sup>12</sup> As a result, a trust can be classified either as a company or as a contract under Swiss private international law.<sup>13</sup> The Swiss Federal Court has ruled that a specific trust may be classified as a company although not all trusts have a sufficient degree of organization to be included in the scope of application of Articles 150 *et seq.* of the Swiss PIL Act.<sup>14</sup>

<sup>11</sup> Same opinion: GHANDCHI J., *Der Geltungsbereich des Art. 159 IPRG (Haftung für ausländische Gesellschaften)*, Zurich 1991, p. 53; SUPINO P., *Rechtsgestaltung mit Trust aus Schweizer Sicht*, Zurich 1994, p. 162; MAYER T.M., *Die organisierte Vermögenseinheit gemäss Art. 150 des Bundesgesetzes über das Internationale Privatrecht – Unter besonderer Berücksichtigung des Trust*, Basel/Frankfurt am Main 1998, p. 118.

<sup>12</sup> VISCHER F. (note 5), ad Art. 150, No 13, p. 1726.

<sup>13</sup> This legal insecurity could be avoided only by ratification of the Hague Convention on the Law Applicable to Trusts and on their Recognition of 1 July 1985. Such ratification is currently being considered by Switzerland; see <http://www.ofj.admin.ch/f/index.html> and the pre-draft of 'Arrêté fédéral portant approbation de la Convention de La Haye relative à la loi applicable au trust et à sa reconnaissance' at <http://www.ofj.admin.ch/f/index.html>. See GUILLAUME F., 'Incompatibilité du trust avec le droit suisse? Un mythe s'effrite', in: *Revue suisse de droit international et de droit européen* 2000, pp. 1-36.

<sup>14</sup> Decision of 3 September 1999 published in *Semaine Judiciaire* 2000 I, pp. 269 *et seq.*, at p. 271. This decision modifies the former case law in which the Swiss Federal Court took the stand that all trusts had to be classified in the legal category of 'contracts'; see ATF 96 II 79.

### III. The Incorporation Theory

#### A. The *Lex Societatis*

When an entity is classified as a company under Article 150 of the Swiss PIL Act, its governing law (i.e., its *lex societatis*) is determined according to Article 154 of the Swiss PIL Act.

#### 1. Law of the Place of Organization (Primary Rule) and Law of the Place of Central Administration (Subsidiary Rule) (Article 154 Swiss PIL Act)

Swiss private international law refers to the so-called incorporation theory, which means that companies are governed by the law of their place of incorporation.<sup>15</sup> Traditionally, this connecting system is opposed to the so-called real seat theory,<sup>16</sup> which refers to the law of the State where the central administration of the company or, more precisely, the center of gravity of the company is located. The main difference between these two main connecting theories is that the founders' freedom of choice prevails in the incorporation theory, as a result of which a formal connection between the company and the State of incorporation suffices. On the contrary, the real seat theory believes that the formation of companies must be preventively controlled by the authorities and consequently refers to a material connection between the company and the State of incorporation.

More precisely, Article 154(1) of the Swiss PIL Act provides that 'companies shall be governed by the law of the State under whose law they are organized'. This primary rule is supplemented by a subsidiary rule referring to the actual administration of the company: if the governing law cannot be determined under Article 154(1) of the Swiss PIL Act, Article 154(2) of the Swiss PIL Act applies and the company shall be subject to the 'law of the State in which it is actually managed'.

The *lex societatis* is determined by a system of rules operating 'in cascade', which applies differently depending on the requirements of formation of the law of the organization State. If this law prescribes certain publicity or registration requirements for the formation of a company, the law of the place of organization applies only if such requirements are fulfilled under Article 154(1) of the Swiss PIL Act (first level of the cascade). Otherwise, the subsidiary rule of Article 154(2) of the Swiss PIL Act applies (second level of the cascade), and the law of the actual administration is the *lex societatis*. In cases where there are no special re-

<sup>15</sup> For a general survey of the incorporation theory and its application in English, Dutch, Swiss and Italian laws, see GUILLAUME F. (note 3), pp. 115 *et seq.*

<sup>16</sup> For a general survey of the real seat theory and its application in French, German and Belgian laws, see GUILLAUME F. (note 3), pp. 133 *et seq.*

quirements of formation, the primary rule applies and the governing law is the organization law, provided the company is organized in accordance with that law (first level of the cascade). If the organization State cannot be identified with certainty because of the lack of requirements of formation, the subsidiary rule applies, and the law of the State in which the company has its actual administration is applicable (second level of the cascade).

If a company has more than one place of management, it is not quite clear if the State in which the company is 'actually managed', as specified in Article 154(2) of the Swiss PIL Act, should be interpreted as referring to any of the places of administration of the company or only to its central administration. In our opinion, where a company does not meet the formation or organization requirements laid down by the law of the State where it is organized, it is to be governed by the law of the place of its central administration.<sup>17</sup> For reasons of legal security and predictability, in such a case the *lex societatis* cannot be determined by the law of any place of administration of the company. This would lead to an extremely large range of possible governing laws, which cannot be the intention of a system of conflict of law rules operating in cascade. Such a system aims indeed to determine one governing law with certainty. Hence, the subsidiary rule of Article 154(2) of the Swiss PIL Act must be read as referring to the central administration of the company.

In this respect, one can say that Swiss private international law refers to the incorporation theory as a primary rule and to the real seat theory as a subsidiary rule.<sup>18</sup> The law of the real seat is subsidiarily applicable when the connection with the place of incorporation does not work. Hence, it appears that the two classical conflict of law rules determining the *lex societatis* complement each other and are not mutually exclusive.<sup>19</sup>

<sup>17</sup> Same opinion: VON PLANTA A. (note 5), ad Art. 154, No 14, p. 1143.

<sup>18</sup> See DUTOIT B. (note 5), ad Art. 154, No 5, p. 494; KLEY-STRULLER A., 'Die Staatszugehörigkeit juristischer Personen', in: *Revue suisse de droit international et de droit européen* 1991, pp. 163-202, at p. 16; REYMOND PH., 'Les personnes morales et les sociétés dans le nouveau droit international privé suisse', in: DESSEMONTET F. (ed.), *Le nouveau droit international privé suisse*, 2<sup>nd</sup> ed., Lausanne 1989, pp. 143-207, at p. 179.

<sup>19</sup> Article 154 of the Swiss PIL Act has been inspired by the Hague Convention Concerning the Recognition of the Legal Personality of Foreign Companies, Associations and Institutions of 1 June 1956, which has not yet entered into force. This Convention refers primarily to the place of incorporation for the recognition of foreign companies (see Article 1), but reserves the possibility to refuse the recognition if the statutory seat is not situated in the State of the real seat (see Article 2). The connection with the State of the real seat of the company is considered here as a corrective to the primary conflict of law rule which refers to the State of incorporation.

## 2. Scope of Application of the *Lex Societatis* (Article 155 Swiss PIL Act)

The law governing a company determined in accordance with Article 154 of the Swiss PIL Act applies to all aspects of its legal status; hence, it is applicable to both its internal and external relationships.

In particular, the *lex societatis* determines the legal nature of the company, its formation and dissolution, its legal capacity to hold and exercise rights and obligations, its name or trade name, its organization, its internal relationships (in particular the relationships between the company and its members), the liability for the violation of company law provisions, the liability for its debts and the power of representation of persons acting on behalf of the company in accordance with its organization.<sup>20</sup>

### B. Recognition *Ipsa Jure* of the Existence of a Foreign Company

The existence of a foreign company duly created under its governing law is automatically recognized in Switzerland. This rule seemed so obvious to the Swiss legislator that he did not consider it useful to formulate an express rule: the recognition *ipso jure* of foreign companies in Switzerland is implicit in the Swiss PIL Act.<sup>21</sup>

Thus, any foreign company which is duly created under the law of its place of organization (see Article 154(1) Swiss PIL Act) or under the law of its place of central administration (see Article 154(2) Swiss PIL Act) is recognized as a company *ipso jure* in Switzerland. Accordingly, foreign companies are legally capable of having rights and incurring obligations and can both sue and be sued in their corporate capacity in Swiss courts. But if neither the formation requirements of the place of organization nor those of the place of central administration are satisfied, the company has not been formed validly and its existence cannot be recognized in Switzerland.<sup>22</sup> The Swiss legislator anticipated the number of cases in which such a situation would happen to be very small, as it is expected that foreign companies will be formed validly either under the law of their place of organization or under that of their place of central administration.

Thus, the system of recognition under Swiss private international law is very flexible, as even the existence of foreign companies which have not been validly formed according to the law of their place of incorporation is recognized

<sup>20</sup> See Article 155 of the Swiss PIL Act.

<sup>21</sup> See GUILLAUME F. (note 3), pp. 68 *et seq.*

<sup>22</sup> If such a foreign company has a branch in Switzerland, the branch will also be regarded as non-existent in Switzerland due to the lack of an existing central administration. See a former decision of the Swiss Federal Court at ATF 50 II 507 (512).

*ipso jure* in Switzerland based on the subsidiary rule.<sup>23</sup> This is a consequence of the system of connecting rules operating in cascade under Article 154 of the Swiss PIL Act.

## C. Branches of Foreign Companies in Switzerland

### 1. Application of the *Lex Societatis* of the Mother Company

A foreign company may have a branch in Switzerland. Under Swiss substantive law, a branch does not have its own legal status, as a result of which its existence is dependent on that of its main office.<sup>24</sup> It therefore follows that a branch is governed by the law applicable to the company that has created the branch, which is determined by Article 154 of the Swiss PIL Act.<sup>25</sup> Therefore, there is no need for a special conflict rule determining the law governing a branch of a foreign company.

### 2. Application of Swiss Law to Certain Matters (Article 160 Swiss PIL Act)

Applying the law of the place of their organization to companies runs the risk that a company will be organized under a foreign law although it acts merely, if not only, through a Swiss branch in Switzerland. In such cases, the foreign company may be an empty shell and the Swiss branch its only place of business. In order to avoid such risk and to protect persons entering into relationships with the Swiss branch of a foreign company, the Swiss legislator decided that certain matters must be governed by Swiss law.<sup>26</sup> The application of Swiss law here is clearly the manifestation of Swiss public policy.

Swiss law applies in particular with regard to the representation power of the branch (Article 160(2) Swiss PIL Act *cum* Article 935(2) Swiss CO), the rules applying to the duty to register the branch in the Register of Commerce (Arti-

<sup>23</sup> See SCHWANDER I., 'Das Statut der internationalen Gesellschaft', in: *Revue suisse de droit international et de droit européen* 2002, pp. 57-77, at pp. 65-66.

<sup>24</sup> There is no legal definition of the branch of a company in Swiss law. However, the Swiss Federal Court has provided a definition that is not disputed, see ATF 108 II 122 (124); ATF 117 II 85 (88).

<sup>25</sup> See, nevertheless, Article 160(1) of the Swiss PIL Act, the wording of which is misleading and disputable as it refers to the registered office of a company, designating Swiss law as applicable to the branch. In reality this provision only states the principle that foreign companies may have a branch in Switzerland. For further comments, see GUILLAUME F. (note 3), pp. 41 *et seq.*

<sup>26</sup> See Article 160(1), second sentence, of the Swiss PIL Act. The application of the provisions of Swiss law on branches to specific matters in order to protect local business is the only meaning of this provision.

cle 160(3) Swiss PIL Act *cum* Article 935(2) Swiss CO and Articles 75 and 75a of the Swiss Register of Commerce Ordinance), the company name of the branch (Article 952(2) Swiss CO and Article 70(2) of the Swiss Register of Commerce Ordinance) and commercial accounting (Article 957 Swiss CO).<sup>27</sup> As a result, even if the internal relationships of a Swiss branch are governed by the foreign *lex societatis* of the mother company, some of the external relationships are governed by Swiss substantive law if the protection of local business so requires.

However, the scope of application of Swiss substantive law to a Swiss branch of a foreign company is limited to the aim pursued, i.e., to protect local business. Hence, Swiss law does not apply to the representation power when the Swiss branch is active abroad. From the point of view of Swiss private international law, in such a case the *lex societatis* of the mother company applies when determining an organ's or a legal representative's power of representation.<sup>28</sup>

## D. The Incorporation Theory in European Community Law

It is of interest to mention here that the principle of connection with the place of incorporation is also admitted as a primary rule in European Community law.

Although European Community law does not provide any connecting factor for companies, one can refer to Article 48 of the Treaty establishing the European Community of 10 November 1997 (hereinafter: EC), which concerns the freedom of establishment. Article 48 EC reads:

'Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the European Union shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States.'

Literally, this provision seems to stipulate two requirements: (1) the company must be formed in accordance with the law of a Member State; and (2) the registered office or central administration or principal place of business of the company must be situated within the European Union. However, the national law of all the Member States at that time required companies to have their registered office in the State whose law governed their legal status. Thus it follows that in reality only one requirement must be fulfilled under Article 48 of the EC Treaty: the incorporation

<sup>27</sup> MARTZ J.-D., *Die inländische Zweigniederlassung einer ausländischen Unternehmung nach schweizerischem IPRG*, Bern 1995, pp. 48 *et seq.*

<sup>28</sup> EBENROTH C.T./MESSER U. (note 10), p. 95; GIRSBERGER D., in: HONSELL/VOGT/SCHNYDER (eds.), *Kommentar zum schweizerischen Privatrecht - Internationales Privatrecht*, Basel/Frankfurt am Main 1996, ad Art. 160, No 14, p. 1195.

of the company in a Member State.<sup>29</sup> This interpretation of Article 48 EC has been confirmed by the European Court of Justice, which held that Member States must apply the incorporation theory towards companies formed in another Member State.<sup>30</sup> Furthermore, the principle of the recognition *ipso jure* of the existence of a company incorporated in another Member State has now been established in the case law of the ECJ.<sup>31</sup>

The ECJ stated also that, in accordance with the freedom of establishment, any company incorporated in a Member State may freely establish branches in another Member State.<sup>32</sup> It follows from this case law of the ECJ that the mother company need not be active in the Member State where it is incorporated: it may pursue all its activities in the Member State where its branch is established. The ECJ clearly stated that the reasons for a company's incorporation in another Member State other than the one where it is active through its branch are of no significance.

This case law of the ECJ has had important repercussions in practice as many companies are now formed in Member States whose company law is deemed to be more permissive (such as limited companies in England), although they are exclusively active in another Member State. By doing this, the managers of the company can reduce the scope of the company's liability and their own personal liability, thus resulting in a serious risk for third parties who enter into relationships with such companies.<sup>33</sup> Nevertheless, it seems that the Registers of Commerce of the Member States have no way of refusing the registration of such branches.

On the other hand, Member States may continue to apply their conflict of law rules – such as the connecting factor of the real seat – towards companies formed in a non-Member State, for instance, in Switzerland. With respect to its relations with Member States, Switzerland is indeed considered a third State. It follows from this that Member States whose conflict of law rules refer to the real seat may apply this connecting factor to companies whose seat is in Switzerland. Furthermore, the requirements for establishing a branch of a Swiss company in a

<sup>29</sup> See GOLDMAN B., 'La nationalité des sociétés dans la Communauté Economique Européenne', in: *TFC DIP* 1966-1969, pp. 215-246, at p. 222; LOUSSOUARN Y., 'Le rattachement des sociétés et la Communauté Economique Européenne', in: *Mélanges offerts à Pierre-Henri Teitgen*, Paris 1984, pp. 239-270, at p. 245. However, this issue is disputed; see EDWARDS V., *EC Company Law*, Oxford 1999, pp. 339 *et seq.*

<sup>30</sup> ECJ, 9 March 1999, *Centros case*, C-212/97; ECJ, 5 November 2002, *Überseering BV case*, C-208/00; ECJ, 30 September 2003, *Inspire Art Ltd case*, C-167/01.

<sup>31</sup> ECJ, 9 March 1999, *Centros case*, C-212/97.

<sup>32</sup> ECJ, 9 March 1999, *Centros case*, C-212/97; ECJ, 30 September 2003, *Inspire Art Ltd case*, C-167/01.

<sup>33</sup> Thus it appears that, in addition to tax law, company law is an important factor in the choice of the State of incorporation. To provide protection to the creditors of companies, it will probably be necessary to adopt European company law instruments which regulate the liability in respect of insolvency proceedings.

Member State are determined by the national law of each Member State as Swiss companies cannot take advantage of the above-mentioned case law of the ECJ. However, if a Swiss company creates a subsidiary in a Member State, such a company will benefit from the freedom of establishment within the European Union. As a result, this subsidiary will be allowed to freely establish a branch in another Member State, even if it has no activity in its State of incorporation.

#### IV. Correctives to the Incorporation Theory in Favour of Third Parties

Article 154 of the Swiss PIL Act is completed by special conflict of law rules which are correctives to the general principle that connects companies to their place of organization.

##### A. Necessary Correctives to the Incorporation Theory

###### 1. *Restriction of the Freedom of Incorporation in Cases of Abuse or Fraudulent Conduct*

The incorporation theory is characterized by the inherent risk that a company can be incorporated in a foreign State whose law prescribes only minimal requirements of formation and restricts the liability of the founders and directors of companies. This theory is derived from English private international law, according to which the legal nature of companies is first determined by the domicile of origin – by analogy with a natural person. The domicile of origin being situated in the State where the company has been formed, the place of incorporation replaces the domicile of origin. Due to its source, the connection with the State of incorporation cannot be changed under English law and companies are in principle governed by the same law from their formation until their dissolution.<sup>34</sup>

When the Swiss legislator adopted the incorporation theory (Article 154(1) Swiss PIL Act), he referred to the place of organization of the company and developed the connecting system by making it possible for companies to change their governing law. This reflects the acceptance of corporation law shopping among States. Nevertheless, although the basic rule leaves the founders a certain latitude

<sup>34</sup> NORTH P.M./FAWCETT J.J., *Private International Law*, 13<sup>th</sup> ed., London 2004, p. 175.

in their freedom of choice, the Swiss legislator has made it clear that this freedom must be restricted in cases of abuse or fraudulent conduct.<sup>35</sup>

To prevent companies from evading their obligations, especially those relating to representation power and liability, Swiss private international law contains rules safeguarding the rights of the creditors of a company whose business is carried out in Switzerland although it is incorporated abroad ('pseudo-foreign companies'). The idea is to avoid situations where the creditors of a pseudo-foreign company find themselves confronted with a debtor who is a financial lure.

## 2. Development of Community Case Law

Before identifying the correctives to the incorporation theory in Swiss private international law, it is of interest to mention the development of the case law of the ECJ relating to the connection of companies. This case law is closely connected to the freedom of establishment inside the European Union (Articles 43 and 48 EC).

In the *Daily Mail case*<sup>36</sup>, the ECJ first decided that Member States are free to choose the connecting factor for companies. In this case, the ECJ held that the possibility for a company to transfer its seat from one Member State to another without losing its legal capacity is not resolved by European Community law, in particular by the rules concerning the right of establishment, and thus must be dealt with by the legislation of the Member States.

Later the ECJ held in the *Centros case*<sup>37</sup> that, in accordance with the freedom of establishment, a company formed under the law of a Member State may set up a branch in another Member State. Furthermore, it made clear that

'the fact that a company does not conduct any business in the Member State in which it has its registered office and pursues its activities only in the Member State where its branch is established is not sufficient to prove the existence of abuse or fraudulent conduct which would entitle the latter Member State to deny that company the benefit of the provisions of Community law relating to the right of establishment'.

By these words, the ECJ implicitly admitted that the real seat theory is contrary to the principle of the freedom of establishment. Nevertheless, the ECJ stated that Member States may adopt appropriate measures for preventing or penalizing fraud 'either in relation to the company itself, if need be in cooperation with the Member State in which it was formed, or in relation to its members, where it has been es-

<sup>35</sup> See *Message du Conseil fédéral, du 10 novembre 1982, concernant une loi fédérale sur le droit international privé (loi de DIP)*, FF 1983 I 255 et seq., Nos 294,44.

<sup>36</sup> ECJ, 27 September 1988, *Daily Mail case*, C-81/87.

<sup>37</sup> ECJ, 9 March 1999, *Centros case*, C-212/97.

tablished that they are in fact attempting, by means of the formation of a company, to evade their obligations towards private or public creditors established in the territory of the Member State concerned'. Thus, the ECJ established in the *Centros case* the general principle of *fraus legis* in European Community company law.<sup>38</sup>

This case law was confirmed by the ECJ later in the *Überseering BV case*,<sup>39</sup> in which it held that Member States must apply the incorporation theory towards companies formed in another Member State. Nevertheless, the ECJ stated again that

'it is not inconceivable that overriding requirements relating to the general interest, such as the protection of the interests of creditors, minority shareholders, employees and even the taxation authorities, may, in certain circumstances and subject to certain conditions, justify restrictions on freedom of establishment. Such objectives cannot, however, justify denying the legal capacity and, consequently, the capacity to be a party to legal proceedings of a company properly incorporated in another Member State in which it has its registered office. Such a measure is tantamount to an outright negation of the freedom of establishment conferred on companies by Articles 43 EC and 48 EC.'

In the *Inspire Art Ltd case*,<sup>40</sup> the ECJ took a step forward by deciding that a Member State could not impose certain conditions prescribed in domestic company law in respect of company formation relating to minimum capital and directors' liability to a branch of a company formed in accordance with the law of another Member State. Hence, a Member State cannot invoke 'grounds of protecting creditors, nor combating improper recourse to freedom of establishment or safeguarding fairness in business dealings or the efficiency of tax inspections' in order to justify the application of mandatory provisions of its domestic legislation, even for the purpose of protecting the interests of other persons dealing with the company.

It follows from this case law that, although European Community law refers to the incorporation theory within the European Union, the necessity to provide correctives to the connecting factor in cases of abuse or fraudulent conduct is admitted by the ECJ. However, it is not quite clear what kind of correctives can still be invoked in this matter.

Swiss private international law is clearer than European Community law in this respect: it provides two main correctives with regard to representation power

<sup>38</sup> Same opinion: MENJUCQ M., *Liberté d'établissement et fraude à la loi communautaire*, Paris 1999, pp. 550 et seq.

<sup>39</sup> ECJ, 5 November 2002, *Überseering BV case*, C-208/00.

<sup>40</sup> ECJ, 30 September 2003, *Inspire Art Ltd case*, C-167/01.

and liability.<sup>41</sup> Where none of these two special correctives is applicable, one may invoke the general rules of public policy, the exception clause and the general principle of *fraus legis*<sup>42</sup> in order to apply a law other than the organization law determined by Article 154(1) of the Swiss PIL Act.

## B. Restriction of Representation Power (Article 158 Swiss PIL Act)

A company can only create legal relationships with third parties through organs or legal representatives. Since the laws of some States contain rules which limit representation power, the good faith of contracting parties must be protected by restricting the grounds on which obligations entered into in the name of the company are not valid. For this purpose, Article 158 of the Swiss PIL Act provides that a company may not invoke a restriction of an organ's or legal representative's representation power if such restriction is unknown to the law of the State in which the other party has its place of business or ordinary residence, unless the other party knew or should have known of the restriction.

The consequence of the said rule is that, although the *lex societatis* determines the powers of representation of persons acting for a company (see Article 155(i) Swiss PIL Act), the scope of the powers of representation is determined by Swiss law if the foreign company has contracted with a third party whose place of business or ordinary residence is in Switzerland. Therefore, a foreign company cannot invoke restrictions of its representation power under its own *lex societatis* when such restrictions do not exist for Swiss companies of the same legal form.

The purpose of this rule is to protect the third contracting party who thought that an organ or a legal representative of the foreign company<sup>43</sup> had a valid representation power.<sup>44</sup> In other words, the third party must have been acting in good faith when he contracted with the person who was representing the company.

<sup>41</sup> See *infra*, IV, B and C. The Swiss PIL Act contains two other correctives which are not discussed here; one relates to claims arising out of the public issue of equity and debt instruments (Article 156 Swiss PIL Act), the other to the protection of name and company name (Article 157 Swiss PIL Act).

<sup>42</sup> See *infra*, IV, D, E and F.

<sup>43</sup> Article 158 of the Swiss PIL Act is only applicable to the acts of the formal representatives of a company, i.e., an organ or a legal representative, and not to the acts of a contractual agent, which are governed by Article 126 of the Swiss PIL Act.

<sup>44</sup> See Article 9 of the First Council Directive 68/151/EEC of 9 March 1968 (68/151/EEC), OJ No L 65 of 14 March 1968, p. 8, which contains the same rule.

## C. Liability for a Foreign Company (Article 159 Swiss PIL Act)

### I. Application of Swiss Law Instead of the *Lex Societatis*

The liability for the debts of a foreign company plays a central role in the protection of third party interests. The main risk connected with the incorporation theory is that, when choosing the place of incorporation, the founders of a company are able to choose the legal framework that best suits them. Therein lies the fundamental weakness of the incorporation principle, which is the risk of formation of companies abroad only *pro forma*. The Swiss legislator tried to establish a special rule which would correct this risk by taking account of the interests of the Swiss creditors of pseudo-foreign companies.<sup>45</sup> The basic idea was that the application of Swiss law would be more profitable for Swiss creditors than the foreign *lex societatis*. Furthermore, the Swiss legislator thought that creating the institution of liability of the organs or legal representatives of the foreign company was the most realistic way of fighting abuse or fraudulent conduct of the founders as such liability would efficiently protect the interests of the foreign company's creditors. However, the elaboration of this special rule turned out to be very problematic and the scope of the final version is still highly debated.<sup>46</sup>

According to Article 159 of the Swiss PIL Act, the liability of persons acting in the name of a company created under a foreign law whose activities are carried out in or from Switzerland is subject to Swiss law. This provision is the Swiss legislator's reply to the pernicious effects of the incorporation theory on the liability for the debts of a foreign company and the violation of requirements of Swiss company law. Unfortunately, as we will see, the final wording of Article 159 of the Swiss PIL Act is unable to resolve the problems for which it was created.

The main characteristic of Article 159 of the Swiss PIL Act is that this provision adds an objective element to the application of the incorporation theory. In principle, in the said theory the *lex societatis* is determined on the basis of a subjective element: the will of the founders to incorporate the new company in a specific State. When there is no material element to support the formal element, the connection of the company with its State of incorporation is purely virtual, thus placing third parties at risk of being misled by the false appearance created by the founders of the company. In order to remedy this risk, the material element of the place where the activities of a company are carried out intervenes by way of Article 159 of the Swiss PIL Act. According to the said provision, Swiss courts may apply Swiss liability law instead of the *lex societatis* if the foreign company has a close connection with Switzerland. This rule reconciles the basic principle of the incorporation theory, which is the freedom of the founders to choose the place of incorporation of a new company. It also safeguards the interests of the company's

<sup>45</sup> *Projet de loi* (note 2), p. 352.

<sup>46</sup> See GUILLAUME F. (note 3), pp. 213 *et seq.*

creditors against the disadvantages arising from a purely subjective incorporation where the latter does not correspond with the place where the company is active in reality.

## 2. *Conditions of Application of Article 159 Swiss PIL Act*

The application of Article 159 of the Swiss PIL Act is subject to the following conditions.

The first condition is that a company – in the sense of Article 150 of the Swiss PIL Act – must have been formed validly under foreign law. Therefore, the *lex societatis* of a company must not be Swiss law. Furthermore, Article 159 of the Swiss PIL Act applies only if the *lex societatis* can be determined by applying Article 154(1) of the Swiss PIL Act, which means that a company must have fulfilled the requirements of the law of its organization State. Article 159 of the Swiss PIL Act cannot apply when the law governing a company must be determined according to Article 154(2) of the Swiss PIL Act, which refers to the law of the State in which the company is actually managed. In such case the said State can only be Switzerland and thus the application of Article 159 of the Swiss PIL Act is to no avail.

The second condition is that the activities of the foreign company must be managed in or from Switzerland. The place where the company carries out its business is not relevant here.<sup>47</sup> The company may carry out business in Switzerland or abroad; the fact that it is managed in Switzerland is sufficient for the application of Article 159 of the Swiss PIL Act. On the contrary, if the company is managed abroad, Article 159 of the Swiss PIL Act is not applicable even if the company carries out business in Switzerland. What is important in this context is that, although governed by a foreign law, the company gives the appearance of being a Swiss company because of its place of management. Furthermore, Article 159 of the Swiss PIL Act must be interpreted in the sense that the company must actually be managed in Switzerland; Switzerland must be the place with which the company is most closely connected from a management point of view.<sup>48</sup> As a result, the applicability of Article 159 of the Swiss PIL Act depends on the determination of the place of central administration of the company, which is a particularly difficult exercise. As seen above, it is left to the Swiss judge in each case to decide whether the level of management of the company in Switzerland is sufficient in the sense of Article 159 of the Swiss PIL Act.

<sup>47</sup> See GHANDCHI J. (note 11), p. 72; REYMOND PH. (note 18), p. 190.

<sup>48</sup> Thus the mere fact that a dummy representative of the company is domiciled in Switzerland is not sufficient for Article 159 of the Swiss PIL Act to be applicable.

The third condition is that the claimant must have believed in good faith that the company managed in Switzerland was Swiss.<sup>49</sup> In other words, the claimant must have been misled about the fact that foreign and not Swiss substantive law was applicable to the liability of the company. As a result, only third parties may file a claim based on this provision. If the action for liability concerns internal relationships (i.e., relationships between the company and its members), Article 159 of the Swiss PIL Act is not applicable, and the *lex societatis* is exclusively applicable to the liability of the company.<sup>50</sup>

The fourth condition is that the defendants in an action for liability must be the persons acting in the name of the company. The said wording must be interpreted as including every person who actually acts for the management or the administration of the company.<sup>51</sup> Thus, the defendants can be any organ of a company in the terms of Article 55 of the Swiss Civil Code (hereinafter: Swiss CC) or any *de facto* organ of a company.<sup>52</sup> According to this provision, any representative or agent of a company who is charged by law or the company statutes to fulfill company tasks or who in reality fulfills such tasks autonomously should be considered as a company organ.<sup>53</sup> The representatives, agents, directors, managers, administrators or liquidators of the company (natural persons or legal entities) are concerned in particular.

## 3. *Consequences of Application of Article 159 Swiss PIL Act*

When Article 159 of the Swiss PIL Act is applied, Swiss law governs the liability of persons acting in the name of a company for violation of any company law provision. Article 159 of the Swiss PIL Act is a corrective to the rule under which the *lex societatis* should, in principle, govern the liability for violation of company law provisions (Article 155(g) Swiss PIL Act) and the liability for the company's debts

<sup>49</sup> Decision of the Swiss Federal Court of 13 June 1994, published in *Semaine Judiciaire* 1994, pp. 687 *et seq.*, at p. 689. See VISCHER F. (note 5), ad Art. 159, No 8, p. 1785; VON PLANTA A. (note 9), ad Art. 159, No 8, p. 1182.

<sup>50</sup> See Article 155(f) and (h) of the Swiss PIL Act.

<sup>51</sup> DUTOIT B. (note 5), ad Art. 159, No 7, p. 508; GHANDCHI J. (note 11), pp. 111 *et seq.*; REYMOND PH. (note 18), p. 192.

<sup>52</sup> Swiss law is applicable when determining the persons liable under Article 159 of the Swiss PIL Act. This exception to Article 155(c) of the Swiss PIL Act is imposed by the *ratio legis* of Article 159 of the Swiss PIL Act, whose application could be hindered if none of the persons acting in the name of a company in Switzerland is regarded as an organ of the company under its *lex societatis*. Same opinion: GHANDCHI J. (note 11), p. 112; REYMOND PH. (note 18), p. 192.

<sup>53</sup> See ATF 117 II 570.

(Article 155(h) Swiss PIL Act).<sup>54</sup> On the other hand, Article 159 of the Swiss PIL Act does not apply to tortious or contractual liability.

The liability of the organs of a pseudo-foreign company is governed by the rules of the Swiss Code of Obligations or the Swiss Civil Code relating to the liability of organs of the type of company that is most similar to the foreign company concerned. The application of Article 159 of the Swiss PIL Act implies the transposition of the foreign company into the Swiss legal system, i.e., its classification in one of the legal categories of Swiss company law. When the foreign company does not correspond to any of the forms of companies existing in Swiss law, the application of Article 159 of the Swiss PIL Act appears to be very problematic. This can easily occur since the notion of 'company' under Swiss private international law is very broad (see Article 150 Swiss PIL Act). If the classification of the foreign company reveals that it does not correspond to any form of Swiss company, the Swiss general rules of liability apply by analogy (see Articles 41 *et seq.* and 55 Swiss CO). The same rule applies when the legal status of the corresponding form of Swiss company does not contain any special rule concerning the company's liability.

As a conflict of law rule, Article 159 of the Swiss PIL Act does not create a new form of liability in Swiss law: the said provision only allows the claimant for liability to invoke Swiss law instead of the *lex societatis*. In this context, we should point out that the conditions under which the corporate veil can be pierced are very restrictive under Swiss law.<sup>55</sup> Article 159 of the Swiss PIL Act does not provide for the possibility of such a piercing: this provision is only a conflict of law rule and has no substantive content.<sup>56</sup>

Invoking Swiss law is left to the claimant's discretion: he will invoke Article 159 of the Swiss PIL Act only if the application of Swiss law would lead to a result in his favour, which would not be the case should the *lex societatis* apply. In our opinion, Article 159 of the Swiss PIL Act is not a mandatory provision: it only applies when the protection of the so-called weaker party would be possible only by applying Swiss law to the liability of persons acting in the name of a foreign

<sup>54</sup> Therefore, Swiss substantive law applies not only to liability for violation of company law provisions but also to liability for the company's debts. As regards the liability for a company's debts, the scope of liability of the organs of the company will depend on the Swiss legal form to which the pseudo-foreign company is most similar. Same opinion: REYMOND PH. (note 18), p. 191. However, some legal authors are of the opinion that Swiss substantive law applies only to liability for violation of company law provisions: EBENROTH C.T./MESSER U. (note 10), p. 90; GHANDCHI J. (note 11), p. 95.

<sup>55</sup> According to the case law of the Swiss Federal Court, the piercing of the corporate veil is allowed only to regard a single shareholder of a company as constituting an economic entity with the company (see, e.g., ATF 85 II 111; ATF 102 III 165) or to hold the mother company liable for the debts of one of its subsidiaries (see, e.g., ATF 120 II 331) in certain circumstances.

<sup>56</sup> For further comments, see GUILLAUME F. (note 3), pp. 246 *et seq.*

company.<sup>57</sup> Otherwise, the general rule applies and the *lex societatis* governs the question of the company's liability.

#### 4. Jurisdiction of Swiss Courts (Article 152 Swiss PIL Act)

When Article 159 of the Swiss PIL Act applies, Swiss courts at the defendant's domicile or ordinary residence or at the place where the company is actually managed have jurisdiction (Article 152 Swiss PIL Act).

The latter is particularly important when the defendant is not domiciled in Switzerland because it is the only possible forum in Switzerland. In such case, if the claimant wishes to file his action for liability before a Swiss court, he must invoke Article 159 of the Swiss PIL Act and in this case Swiss law is necessarily the governing law.<sup>58</sup> The place where a company is actually managed pursuant to Article 152 of the Swiss PIL Act is the place of its central administration, as it is when Article 159 of the Swiss PIL Act applies.

However, if the defendant is domiciled abroad in a contracting State of the Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters adopted in Lugano on 16 September 1988 (hereinafter: Lugano Convention), the said Convention is exclusively applicable and the forum will in principle be the defendant's domicile (Article 2 Lugano Convention). In such case, Article 159 of the Swiss PIL Act cannot apply, unless the jurisdiction of Swiss courts can be based on a different provision of the Lugano Convention.

#### D. Public Policy Exceptions

If the conditions of application of neither of the two above-mentioned special correctives to the incorporation theory are fulfilled, it is possible to invoke the general rules of public policy and the exception clause in order to apply another law other than the one determined under Article 154(1) of the Swiss PIL Act in cases where it is necessary to protect the interests of creditors of the pseudo-foreign company.

<sup>57</sup> Same opinion: DESSEMONTET F., 'La responsabilité des organes en droit international privé', in: *Aspects du droit international des sociétés - Journée suisse de droit international du 25 novembre 1994 à Neuchâtel*, Zurich 1995, pp. 149-174, at p. 164; DUTOIT B. (note 5), ad Art. 159, No 9, pp. 508-509; VON OVERBECK A., 'Droit des sociétés: l'article 159 de la loi fédérale sur le droit international privé revu', in: MEIER/SIEHR (eds.), *Rechtskollisionen - Festschrift für Anton Heini zum 65. Geburtstag*, Zurich 1995, pp. 295-304, at p. 303; SCHWANDER I. (note 10), No 807, p. 353; VISCHER F. (note 5), ad Art. 159, No 3, p. 1784.

<sup>58</sup> See decision of the Swiss Federal Court of 13 June 1994, published in *Semaine Judiciaire* 1994, pp. 687 *et seq.*, at p. 688. Same opinion: VISCHER F. (note 5), ad Art. 152, No 5, p. 1739.

## 1. Public Policy Clause (Article 17 Swiss PIL Act)

According to Article 17 of the Swiss PIL Act, the application of provisions of foreign law is excluded if such application would lead to a result that is incompatible with Swiss public policy. The said provision addresses the 'defensive' or 'negative' facet of public policy by providing a mechanism that allows the judge to refuse the application of the foreign law designated as applicable under the Swiss conflict of law rules. Such refusal is justified when the facts of the case are such that the application of the relevant foreign rule would produce a result that departs so radically from the Swiss concepts of fundamental justice that its application would be intolerably outrageous to Swiss basic values.<sup>59</sup> Article 17 of the Swiss PIL Act aims at safeguarding the basic moral, social, economic and political values of Swiss society.<sup>60</sup> The public policy clause must be applied on a case-by-case basis. It may be invoked only if the application of the foreign applicable law would lead to a shocking result from the point of view of Swiss law.

The intervention of the public policy clause in the field of company law implies that the application of a provision of the *lex societatis* would violate Swiss public policy in a specific case. In the well-known *Chilon Valeurs* case,<sup>61</sup> the Swiss Federal Court held that, as a general limit to the incorporation theory, it is possible to apply Article 17 of the Swiss PIL Act to correct the connection of a foreign company to its State of organization (determined under Article 154(1) Swiss PIL Act). In the *Chilon Valeurs* case, the legal capacity of the foreign company was disputed. In particular, the defendant contested the claimant's legal capacity to sue in Swiss courts because of the allegedly fraudulent formation of the company abroad. According to the Swiss Federal Court, the mere fact that the laws of its State of organization allow a foreign company to proceed before the courts obviously does not contravene the basic values of Swiss legal order.<sup>62</sup> As a result, the debtors of a foreign company cannot invoke the public policy clause as a means of attempting to evade their obligations towards a pseudo-foreign company.<sup>63</sup>

<sup>59</sup> See ATF 102 Ia 574 (581).

<sup>60</sup> See BUCHER A., 'L'ordre public et le but social des lois en droit international privé', *Recueil des Cours* 1993 II (239), pp. 9-116; LAGARDE P., *Recherches sur l'ordre public en droit international privé*, Paris 1959; OTHENIN-GIRARD S., *La réserve d'ordre public en droit international privé suisse*, Zurich 1999.

<sup>61</sup> ATF 117 II 494 (501).

<sup>62</sup> ATF 117 II 494 (502).

<sup>63</sup> Such means of defence were allowed under the previous case law of the Swiss Federal Court with the so-called *réserve du siège fictif*. See ATF 108 II 398 (f): the Swiss Federal Court declared the incorporation of a company in Liechtenstein null and void; as a result, it held the company to be without legal capacity in Switzerland because its real seat was in Switzerland and its seat in Liechtenstein only fictitious. Due to the intervention of

The public policy clause could be applied for the purpose of protecting creditors, as this comes under the social role of a State and is included in its public policy.<sup>64</sup> Article 17 of the Swiss PIL Act allows, for instance, the application of Swiss law instead of the *lex societatis* to liability when the restricted conditions of application of Article 159 Swiss PIL Act prevent the intervention of the said provision. The Swiss Federal Court, for instance, has ruled that Article 17 of the Swiss PIL Act could apply as a means of imposing the application of the principle of piercing the corporate veil when the application of the *lex societatis* would lead to a result incompatible with Swiss public policy.<sup>65</sup> However, the Court found that such requirement was not fulfilled in the case at hand.

## 2. Application of Mandatory Provisions of Swiss Law (Article 18 Swiss PIL Act)

Article 18 of the Swiss PIL Act provides that, due to their particular purpose, the application of mandatory provisions of Swiss law shall remain reserved, regardless of the law designated as applicable by the Swiss PIL Act. This provision addresses the 'offensive' or 'positive' facet of public policy by providing a mechanism requiring a specific rule of Swiss law to be applied although the Swiss conflict of law rules designate another law as applicable. The so-called *lois d'application immédiate* are the provisions of Swiss law which apply without taking account of the law designated as applicable by the conflict of law rules.

Although every mandatory provision of Swiss law could be considered as a *loi d'application immédiate*, it is quite rare that the said classification is admitted in a concrete case. The application of a mandatory provision of Swiss law to the legal status of a foreign company instead of its *lex societatis* implies that the said provision belongs to the international public policy of Switzerland and that its application in the case at hand is necessary in light of all circumstances of the case.

Article 335 of the Swiss Civil Code provides, for instance, that a family foundation can be constituted for the purpose of paying the costs of the education, outfitting or maintenance of the members of the family or for similar purposes. However, as a general rule, it is prohibited to tie up property for generations (prohibition of *fideicommissa*). With respect to this provision, the Swiss Federal Court ruled that so-called 'support foundations' are illegal under Swiss law; by allowing a person or family to use the foundation for a purpose other than that specified in

public policy, the pseudo-foreign company was not allowed to institute proceedings in Switzerland against its debtors. For further comments on the *réserve du siège fictif*, see GUILLAUME F. (note 3), pp. 124 *et seq.*

<sup>64</sup> See *Message du Conseil fédéral, du 10 novembre 1982, concernant une loi fédérale sur le droit international privé (loi de DIP)*, FF 1983 I 255 *et seq.*, Nos 291 and 294.44.

<sup>65</sup> See ATF 128 III 346 (350).

Article 335 of the Swiss Civil Code, such foundations aim at circumventing the prohibition of *fideicommissa*.<sup>66</sup> However, the Federal Justices did not regard Article 335 of the Swiss Civil Code as a *loi d'application immédiate*: they merely referred to the *fraus legis* in order to declare the foundation at issue non-existent under Swiss law. Later in a similar case, the Swiss Federal Court ruled that Article 18 of the Swiss PIL Act does not apply to the formation of companies, thus invoking the incorporation theory.<sup>67</sup>

On the contrary, in our opinion, Article 335 of the Swiss Civil Code is one of the rare rules of Swiss law which could be regarded as a *loi d'application immédiate*. In particular, the said provision should be applicable when the beneficiary of a foreign foundation is domiciled in Switzerland because the formation of a pseudo-foreign foundation can undermine international public policy in Switzerland.<sup>68</sup> But this does not mean that the foreign foundation should be regarded as non-existent in Switzerland. There are other possible correctives, such as the reintegration of the property of the foundation into the founder's inheritance. The Swiss Federal Court should have nuanced its decision by making it clear that Article 18 of the Swiss PIL Act was not applicable in the case at hand because the beneficiary of the foundation was domiciled abroad. That being the case, the affair lacked a sufficient connection with international public policy in Switzerland to justify the application of Article 18 of the Swiss PIL Act. One should note, however, that Article 18 of the Swiss PIL Act may apply in other circumstances, in particular when a company has been formed abroad for the purpose of avoiding certain mandatory provisions of Swiss law.<sup>69</sup>

### 3. Observance of Mandatory Provisions of Foreign Law (Article 19 Swiss PIL Act)

According to Article 19(1) of the Swiss PIL Act, mandatory provisions of another law may be taken into consideration in lieu of the law designated by the Swiss PIL Act if interests which are legitimate and clearly preponderant under the Swiss conception of law so require and if the case has a close connection with such law. The purpose of such a provision and the consequences of its application shall be con-

<sup>66</sup> See ATF 108 II 398 (403).

<sup>67</sup> ATF 117 II 494 (501-502).

<sup>68</sup> Same opinion: VON PLANTA A. (note 5), ad Art. 154, No 18, pp. 1144 *et seq.*; VISCHER F. (note 5), ad Art. 154, No 34, p. 1755. For further comments on Article 18 Swiss PIL Act *cum* Article 335 Swiss CC, see GUILLAUME F. (note 3), pp. 282 *et seq.*

<sup>69</sup> See PERRIN J.-F., 'Théorie de l'incorporation et cohérence de l'ordre juridique', in: DOMINICÉ/PATRY/REYMOND (eds.), *Etudes de droit international en l'honneur de Pierre Lalive*, Basel/Frankfurt am Main 1993, pp. 141-150, at pp. 149 *et seq.*

sidered when deciding whether it is to be taken into account so as to reach a decision compatible with the Swiss conception of law (Article 19(2) Swiss PIL Act).

This provision, which is rarely applied, allows Swiss judges to take account of a mandatory provision of a third State in certain circumstances. Its application is subject to the following conditions: (1) the foreign provision must be mandatory in its legal system; (2) the application of the said provision must be justified by interests which are legitimate and clearly preponderant under the Swiss conception of law; and (3) the case must have a close connection to the law to which the mandatory provision belongs. Swiss judges will take account of a foreign mandatory provision if so required by a clearly preponderant interest, from the Swiss point of view, having regard for the consequences of the application of the *lex societatis* in the concrete case. The application of Article 19 of the Swiss PIL Act presupposes that the foreign mandatory provision concerned is the only provision that can uphold the public policy of Switzerland. This can occur only if no *loi d'application immédiate* of Swiss law is applicable.

Under Article 19 of the Swiss PIL Act a mandatory provision of a foreign law other than the *lex societatis* may be applied to the legal status of a foreign company instead of its *lex societatis*; however, in light of the restrictive conditions of application of this provision, it is unlikely that the said provision would apply in this case. If necessary, the Swiss judge will try to find a *loi d'application immédiate* in Swiss substantive law instead of applying a mandatory provision of foreign law in lieu of the *lex societatis*.

### E. Exception Clause (Article 15 Swiss PIL Act)

Article 15(1) of the Swiss PIL Act provides that the law designated as applicable by the Swiss PIL Act shall, as an exception, not apply if, in the circumstances, it is obvious that the case has only a remote connection with that law, but a much closer connection with another law. Furthermore, this provision shall not apply if the parties have made a choice of law (Article 15(2) Swiss PIL Act).

Article 15 of the Swiss PIL Act allows Swiss judges to exclude the application of the law designated by the conflict of law rule without weighing the interests at stake, but only by considering the closest connection of the case with a specific State. The purpose of Article 15 of the Swiss PIL Act is not to reserve the application of public policy of Switzerland but rather to uphold the so-called *principe de proximité* (proximity principle).<sup>70</sup> It therefore follows that, if the parties have made a choice of law, there is no need to correct an inappropriate connection resulting from the blind mechanism of the conflict of law rules.

<sup>70</sup> See LAGARDE P., 'Le principe de proximité dans le droit international privé contemporain. Cours général de droit international privé', *Recueil des Cours* 1986 I (196), pp. 9-237.

Applying Article 15 of the Swiss PIL Act to correct the connection of companies to the State of their incorporation pursuant to Article 154(1) of the Swiss PIL Act would be contrary to the system of incorporation. Such a system institutes a purely formal connecting factor (the place of incorporation), without taking account of the closest connection. Since the founders are totally free to choose the place of incorporation of their company under Swiss private international law, the application of Article 15 of the Swiss PIL Act would be meaningless in company law.

Furthermore, this provision cannot apply if there is a choice of law clause. Since the formation of a company is an act which permits freedom of choice, the choice of a place of incorporation can be considered as a choice of law in the sense of Article 15(2) of the Swiss PIL Act. The application of Article 15 of the Swiss PIL Act as a corrective to the incorporation theory is therefore excluded. The Swiss Federal Court has already made such a ruling on two occasions.<sup>71</sup>

## F. The *Fraus Legis* Principle

### 1. Application of the *Fraus Legis* Principle in Company Law

Prior to the entry into force of the Swiss PIL Act in 1987, companies were governed by the law of the State designated in their Articles of Association or, in the absence of such a designation, by the law of the State where they were actually managed. This rule had been established by the Swiss Federal Court, whose decisions were indirectly based on the incorporation theory for about forty years.<sup>72</sup> However, this conflict of law rule provided a corrective to the incorporation theory called the *réserve du siège fictif* (reservation of the fictitious seat). According to this corrective, the seat designated in the Articles of Association was considered as fictitious when: (1) it had no connection with the factual reality; and (2) it was chosen only to escape the mandatory provisions of the State where the company was actually managed.<sup>73</sup> As a result, the application of this corrective meant that the foreign company was considered as non-existent from the point of view of Swiss law. Accordingly, it was denied legal capacity and consequently the capacity to be a party to legal proceedings. The *réserve du siège fictif* is a good example of the application of *fraus legis* or misuse of rights in the field of company law.

Since the Swiss legislator opted in Article 154 of the Swiss PIL Act for a conflict of law rule directly inspired by the former case law, the question arises whether the so-called *réserve du siège fictif* is still applicable today. The Swiss

<sup>71</sup> ATF 117 II 494 (501); ATF 128 III 346 (350-351).

<sup>72</sup> See ATF 76 I 150; ATF 108 II 122; ATF 108 II 398; ATF 110 Ib 213. For further comments on these cases, see GUILLAUME F. (note 3), pp. 323 *et seq.*

<sup>73</sup> See ATF 76 I 150 (159).

Federal Court answered this question negatively in 1991,<sup>74</sup> arguing that one of the principal aims of Article 154 of the Swiss PIL Act is to avoid that a foreign company could be regarded as non-existent under Swiss law. This statement deserves approval in light of the undesirable consequences of the application of the *réserve du siège fictif*. In the same decision, the Swiss Federal Court recalled that Swiss private international law refers to the incorporation theory, whose system does not include any corrective to combat *fraus legis* (in contrast to the system of the real seat). But paradoxically, the Swiss Federal Court continued its reasoning, trying to identify which provision of the Swiss PIL Act could apply as a corrective to the incorporation theory. The Federal Justices decided that Articles 17 and 18 of the Swiss PIL Act may in theory apply as correctives to the incorporation theory, but not in the case at hand. The above decision has been highly debated by legal scholars.<sup>75</sup>

Later the Swiss Federal Court held – in a matter relating to contract law – that the prohibition of misuse of rights (Article 2 Swiss CC) is part of the public policy of Switzerland and may be invoked as a *loi d'application immédiate* by way of Article 18 of the Swiss PIL Act.<sup>76</sup> In another case, the Swiss Federal Court applied the above reasoning to company law and ruled that the principle of piercing the corporate veil may not be invoked in the name of prohibiting the misuse of rights as a *loi d'application immédiate*, unless the application of the *lex societatis* would lead to a result incompatible with Swiss public policy (Article 17 Swiss PIL Act).<sup>77</sup> We can conclude from this case law that, if the prohibition of misuse of rights may be invoked as a corrective to the incorporation theory as a manifestation of public policy in Switzerland (Article 17 Swiss PIL Act), the application of the *fraus legis* principle is also possible as a corrective to Article 154(1) of the Swiss PIL Act.

<sup>74</sup> ATF 117 II 494. For further comments on this case, see GUILLAUME F. (note 3), pp. 334 *et seq.*

<sup>75</sup> All legal scholars regard the *réserve du siège fictif* as no longer applicable under the Swiss PIL Act, however, some view the *fraus legis* principle as a general principle of law in the field of company law: DESSEMONTET F. (note 57), p. 166; DUTOIT B. (note 5), ad Art. 154, No 6, pp. 495 *et seq.*, while others maintain that the *fraus legis* principle applies under cover of other correctives, such as Articles 17, 18 or 19 Swiss PIL Act: PERRIN J.-F. (note 69), p. 149; REYMOND J.-A., 'Sociétés étrangères en Suisse: exit *fraus legis*', in: DOMINICÉ/PATRY/REYMOND (eds.), *Etudes de droit international en l'honneur de Pierre Lalive*, Basel/Frankfurt am Main 1993, pp. 173-179, at p. 179; SCHWANDER I., 'Note concernant l'ATF 117 II 494', in: *Revue suisse de droit international et de droit européen* 1993, pp. 96-98, at p. 97; and others contend that the *fraus legis* principle does not apply at all in the field of company law: HEINI A., 'Note concernant l'ATF 117 II 494', in: *Revue suisse de droit des affaires* 1993, pp. 64-65; VON PLANTA A. (note 5), ad Art. 154, No 16, pp. 1143 *et seq.*; VISCHER F. (note 5), ad Art. 154, Nos 19-20, p. 1751.

<sup>76</sup> See ATF 128 III 201.

<sup>77</sup> See ATF 128 III 346 (349-350).

Two conditions must be fulfilled for a *fraus legis* to be admitted in the law applicable to companies: (1) misuse of the private international law rule, i.e. Article 154(1) of the Swiss PIL Act; and (2) the intent of the founders of the company to evade the law normally applicable in favour of another law that is more attractive.<sup>78</sup> More precisely, the application of the *fraus legis* principle implies that the main purpose of the incorporation of a company in the chosen State is to avoid the application of a specific mandatory provision relating to the legal status of companies.

## 2. Consequences of Application of the *Fraus Legis* Principle as a Corrective to the Incorporation Theory

The application of the *fraus legis* principle as a corrective to Article 154(1) of the Swiss PIL Act cannot result in the non-existence of the foreign company in Swiss law, but in a statement that the fraudulent act (i.e., the incorporation of the company in the chosen State) is not opposable to third parties. This allows Swiss judges to ignore the law of organization of the company and to apply the law of the State in which the company is actually managed instead. In this way, the law applicable to the company is no longer determined by applying the primary rule (Article 154(1) Swiss PIL Act) but by the subsidiary rule (Article 154(2) Swiss PIL Act). In such case, the connecting factor of the place of central administration acts as a corrective to the connecting factor of the place of organization.

However, when the company has been organized under a foreign law for the purpose of avoiding a prohibition existing in Swiss law, the intervention of *fraus legis* may lead to the nullity of the company because of its unlawful object.<sup>79</sup> This may cause damages to the creditors of the company. Therefore, Swiss judges must take account of the practical consequences of the sanction of *fraus legis* in the light of the circumstances of the case in hand before applying this corrective to the incorporation theory.<sup>80</sup>

<sup>78</sup> For further comments on the conditions of application of *fraus legis* in the field of company law, see GUILLAUME F. (note 3), pp. 298 *et seq.*

<sup>79</sup> See Article 52(3) of the Swiss CC, which reads as follows: 'The companies and establishments that have an unlawful or immoral object cannot acquire the status of a legal person.'

<sup>80</sup> For further comments on the sanction of *fraus legis* in the field of company law, see GUILLAUME F. (note 3), pp. 341 *et seq.*

## V. Changing the *Lex Societatis*

Swiss private international law allows the *lex societatis* to be changed without any prior liquidation of the company or new formation in the host State. There are four ways of changing the governing law of companies in Swiss private international law: (1) the international transfer of a company; (2) the international merger of companies; (3) the international demerger of companies; and (4) the international transfer of assets and liabilities.<sup>81</sup>

### A. The Law Applicable to the International Transfer of a Company

The international transfer of a company allows a company to change its *lex societatis* without any prior liquidation or new formation.<sup>82</sup> Since Swiss private international law follows the incorporation theory, the international transfer of a company cannot be realized by a single transfer of the seat of the company. Moreover, the transfer of the seat of the company is not a requirement for changing the governing law of a company; it is only a consequence of its new incorporation in the host State.

Any company wishing to change its *lex societatis* has to fulfill all the conditions of departure of the law of its State of origin, as well as all the formal requirements of establishment of the law of the host State. The private international law rules aim to determine the scope of application of both laws involved, in particular to avoid a company which is in the process of changing its *lex societatis* going through a period of time during which it is governed by neither of the two laws concerned.

<sup>81</sup> The international merger, demerger and transfer of assets and liabilities were introduced into the Swiss PIL Act by the new Swiss Merger Law, which came into force on 1 July 2004. This new law, which provides for all types of reorganization of entities under private law, has revised and amended the provisions of the Swiss PIL Act relating to the transfer of a company.

<sup>82</sup> International transfers of a company do not occur often in practice because such form of reorganization is not yet regulated in European Community law, thus limiting the possibilities of transferring a company to or from Switzerland. The pre-draft of Proposal for a 14<sup>th</sup> Company Law Directive on the cross-border transfer of the registered office of limited companies of 20 April 1997 provided for the possibility to realize an intra-Community transfer of seat; however, it has since been abandoned. The case law of the European Court of Justice concerning the transfer of a company from one Member State to another (ECJ, 27 September 1988, *Daily Mail case*, C-81/87; ECJ, 5 November 2002, *Überseering BV case*, C-208/00; see *supra*, IV.A.2.) is of course not applicable to the transfer of a company to or from Switzerland.

**1. Transfer of a Foreign Company to Switzerland (Articles 161 and 162 Swiss PIL Act)**

A foreign company may change its *lex societatis* to Swiss law without being liquidated or newly formed (i.e., an immigration) if the following prerequisites are fulfilled: (1) the law of origin must allow the international transfer of companies; (2) the prerequisites set forth in the law of origin must be fulfilled; and (3) the company must be able to adapt itself to one of the forms of legal organization provided by Swiss law (Article 161(1) Swiss PIL Act).

The company is subject to Swiss law when it has effected its adaptation to Swiss law and has a sufficient connection with Switzerland (Article 162 Swiss PIL Act). A company that is required under Swiss law to register in the Swiss Register of Commerce shall be deemed to have a sufficient connection with Switzerland when it proves that it has transferred the center of its business activities to Switzerland (Article 162(1) Swiss PIL Act), or if it is not required under Swiss law to register in the Swiss Register of Commerce, when it becomes clear that the company intends to be governed by Swiss law (Article 162(2) Swiss PIL Act).

Furthermore, a company with stated capital – which has to be registered in the Swiss Register of Commerce – must submit a report by a specially qualified auditor providing evidence that its capital stock is covered, as required by Swiss law, in order to be authorized to register in the Swiss Register of Commerce (Article 162(3) Swiss PIL Act). This obligation aims to protect the creditors of the new Swiss company.

**2. Transfer of a Swiss Company Abroad (Article 163 Swiss PIL Act)**

A Swiss company may subject itself to a foreign law without liquidation or new formation (i.e., an emigration) if the following prerequisites are fulfilled: (1) all the requirements of Swiss law are met; (2) the company must continue to exist under the law of the host State; and (3) the creditors of the company must have been protected against the risk of losing their right of action against the company (Article 163 Swiss PIL Act).

The rights of the company's creditors are secured by public notification in Switzerland announcing the imminent transfer abroad and requesting creditors to announce their claims (Article 163(2) Swiss PIL Act). Furthermore, the company cannot be deleted from the Swiss Register of Commerce, and the places of debt enforcement and of jurisdiction remain in Switzerland as long as the rights of the creditors of the company are not safeguarded (Articles 164 and 164a Swiss PIL Act).

**B. The Law Applicable to International Merger, Demerger and Transfer of Assets and Liabilities**

The international merger, demerger and transfer of assets and liabilities offer a wide range of possibilities for reorganizing corporate entities on an international level. Contrary to the international transfer of a company, these tools always imply the participation of at least two companies which are governed by different laws.

**1. The Law Applicable to International Merger**

A merger combines two or more companies in such a manner that at least one initial company (i.e., an absorption) or all of the initial companies (i.e., a combination) are dissolved.<sup>83</sup> Since an international merger presupposes that the two companies are governed by different laws, the two substantive laws are applicable in parallel, and it is necessary to distinguish between the laws governing each of the two companies involved.

**a) Merger from abroad to Switzerland (Article 163a Swiss PIL Act)**

A Swiss company may take over a foreign company (i.e., an absorption by immigration) or merge with it to form a new Swiss company (i.e., a combination by immigration).

As regards the foreign company, its *lex societatis* applies to all aspects concerning the transferring company; in particular, the following prerequisites must be fulfilled: (1) its *lex societatis* must allow the international merger; and (2) the requirements of its *lex societatis* regarding the legal aspects of merger concerning the transferring company must be fulfilled (Article 163a(1) Swiss PIL Act).

In particular, the rights of the creditors and partners of the company must be secured by the *lex societatis* of the transferring company. This law will also govern the requirements to be fulfilled before the company is deleted from the foreign Register of Commerce.

As regards the Swiss company, Swiss law and in particular the Swiss Federal Law on Merger, Demerger, Conversion and Transfer of Assets and Liabilities of 3 October 2004 (hereinafter: Swiss Merger Law) apply to all aspects which

<sup>83</sup> The international merger is not yet regulated in European Community law; however, there is a Proposal for a Directive of the European Parliament and Council on cross-border mergers of companies with share-capital of 18 November 2003 (2003/0277 (COD)), which should enter into force in the near future. Since the Directive will apply only to intra-Community mergers, it will not apply to a merger between a Swiss company and a company incorporated in a Member State. In such case, all the international aspects of the merger will be governed by the private international law of each State involved.

concern the surviving company, as well as the transfer of assets and liabilities (Article 163a(2) Swiss PIL Act). In particular, the transfer of contracts is governed by Swiss law.

*b) Merger from Switzerland abroad (Article 163b Swiss PIL Act)*

A foreign company may takeover a Swiss company (i.e., an absorption by emigration) or merge with it to form a new foreign company (i.e., a combination by emigration).

As regards the Swiss company, Swiss law applies to all aspects concerning the transferring company; in particular, the following prerequisites must be fulfilled: (1) the constitutive elements of a merger under Swiss law must be respected: in particular, the entire assets and liabilities must be transferred to the foreign company *uno actu* and the participation or membership rights must be adequately protected in the foreign company (Article 163b(1)(a) and (1)(b) Swiss PIL Act); (2) all the provisions of Swiss law applicable to the transferring company must be fulfilled (Article 163b(2) Swiss PIL Act); and (3) the creditors must be informed by public notification in Switzerland about the imminent merger and requested to announce their claims (Article 163b(3) Swiss PIL Act).

If the Swiss company is registered in the Swiss Register of Commerce, it cannot be deleted until the claims of its creditors or partners have been secured or satisfied (Article 164 Swiss PIL Act). Furthermore, the places of debt enforcement and of jurisdiction also remain in Switzerland until the claims of its creditors or partners have been secured or satisfied (Article 164a Swiss PIL Act).

As regards the foreign company, its *lex societatis* applies to all aspects concerning the surviving company, as well as the transfer of assets and liabilities (Article 163b(4) Swiss PIL Act). In particular, the transfer of contracts is governed by the foreign law applicable to this company.

**2. The Law Applicable to International Demerger**

In a demerger, portions of the assets and liabilities of the demerging company are transferred to at least one newly formed or already existing company in such a manner that the shareholders of the transferring company obtain participation or membership rights in the absorbing companies. This may occur either by the transfer of all the assets and liabilities (i.e., a division) or the transfer of one or several parts of the assets and liabilities (i.e., a spin-off) to other companies.<sup>84</sup>

The only special rule governing international demerger in the Swiss PIL Act provides that the provisions of the Swiss PIL Act concerning mergers shall apply by analogy to an international demerger (Article 163d(1) Swiss PIL Act). Since a

<sup>84</sup> The international demerger is not yet regulated in European Community law.

demerger is not a symmetrical operation of a merger, Articles 163a and 163b of the Swiss PIL Act cannot be applied by analogy without adjustments. As in the case of merger, one must distinguish between the laws governing each of the companies involved.

*a) Demerger from abroad to Switzerland (Article 163d cum Article 163a Swiss PIL Act)*

A foreign company may transfer portions of assets and liabilities to a newly formed or already existing Swiss company (i.e., a demerger by immigration).

As regards the foreign company, its *lex societatis* applies to all aspects concerning the demerging company; in particular, the following prerequisites must be fulfilled: (1) its *lex societatis* must allow the international demerger; and (2) the requirements of its *lex societatis* concerning the legal aspects of a demerger in respect of the demerging company must be fulfilled (Article 163a(1) Swiss PIL Act applied by analogy). In particular, the rights of the creditors and partners of the company must be secured by the *lex societatis* of the transferring company. This law will also govern the requirements to be fulfilled until the company is deleted from the foreign Register of Commerce.

The transfer of assets and liabilities is also governed by the *lex societatis* of the demerging company (Article 163d(2) Swiss PIL Act). In particular, the transfer of contracts is governed by foreign law of the demerging company.

As regards the Swiss company, Swiss law and in particular the Swiss Merger Law apply to all aspects concerning the overtaking company.

*b) Demerger from Switzerland abroad (Article 163d cum Article 163b Swiss PIL Act)*

A Swiss company may transfer portions of assets and liabilities to a newly formed or already existing foreign company (i.e., a demerger by emigration).

As regards the Swiss company, Swiss law applies to all aspects concerning the demerging company; in particular, the following prerequisites must be fulfilled: (1) the constitutive elements of a demerger under Swiss law must be respected: in particular, in the case of a division by emigration, the entire assets and liabilities must be transferred to the foreign company *uno actu* and the participation or membership rights must be adequately protected in the foreign company (Article 163b(1)(a) and (1)(b) Swiss PIL Act applied by analogy); in the case of a spin-off by emigration, the participation or membership rights must be adequately protected in the foreign company (Article 163b(1)(b) Swiss PIL Act applied by analogy); (2) all the provisions of Swiss law applicable to the demerging company must be fulfilled (Article 163b(2) Swiss PIL Act applied by analogy); and (3) the creditors must be informed by public notification in Switzerland about the immi-

nent demerger and requested to announce their claims (Article 163h(3) Swiss PIL Act applied by analogy).

The transfer of assets and liabilities is also governed by Swiss law (Article 163d(2) Swiss PIL Act). In particular, the transfer of contracts is governed by Swiss law.

If the Swiss company is registered in the Swiss Register of Commerce, it cannot be deleted until the claims of its creditors or partners have been secured or satisfied (Article 164 Swiss PIL Act). Furthermore, the places of debt enforcement and of jurisdiction remain in Switzerland until the claims of its creditors or partners have been secured or satisfied (Article 164a Swiss PIL Act).

As regards the foreign company, its *lex societatis* applies to all aspects concerning the overtaking company.

### 3. *The Law Applicable to International Transfer of Assets and Liabilities*

A transfer of assets and liabilities entails the transfer by law of a list of all the assets and liabilities or parts thereof, in accordance with an inventory, of the transferring company to another company.<sup>85</sup> The difference between a transfer of assets and liabilities and a demerger is that a transfer does not affect the rights of the shareholders. Except for this basic difference, a transfer of assets and liabilities is very similar to a demerger.<sup>86</sup> As for an international demerger, the only special rule of the Swiss PIL Act governing the international transfer of assets and liabilities provides that the provisions of the said Act concerning mergers shall apply by analogy to an international transfer of assets and liabilities (Article 163d(1) Swiss PIL Act). Here again, one must distinguish between the laws governing each of the companies involved.

#### a) *Transfer of Assets and Liabilities from abroad to Switzerland (Article 163d cum Article 163a Swiss PIL Act)*

As regards the immigration of assets and liabilities, a foreign company may transfer portions of its assets and liabilities to at least one newly formed or already existing Swiss company.

The same rules apply *mutatis mutandis* to a demerger by immigration.

<sup>85</sup> The international transfer of assets and liabilities is not yet regulated in European Community law.

<sup>86</sup> This form of reorganization will most probably be often chosen because it allows the same kind of reorganization as a merger or a demerger from an economic point of view, without the legal difficulties arising due to the incompatibility of the different legal forms of companies involved.

#### b) *Transfer of Assets and Liabilities from Switzerland abroad (Article 163d cum Article 163b Swiss PIL Act)*

As regards the emigration of assets and liabilities, a Swiss company may transfer portions of its assets and liabilities to at least one newly formed or already existing foreign company.

As regards the Swiss company, Swiss law applies to all aspects which concern the transferring company; in particular, the following prerequisites must be fulfilled: (1) the constitutive elements of a transfer of assets and liabilities under Swiss law must be respected: if the transferring company transfers the entire assets and liabilities, they must be transferred to the foreign company *uno actu* (Article 163b(1)(a) Swiss PIL Act applied by analogy); (2) all the provisions of Swiss law applicable to the transferring company must be fulfilled (Article 163b(2) Swiss PIL Act applied by analogy); and (3) if the transferring company transfers the entire assets and liabilities, the creditors must be informed by public notification in Switzerland about the imminent transfer of assets and liabilities and requested to announce their claims (Article 163b(3) Swiss PIL Act applied by analogy).<sup>87</sup>

The transfer of assets and liabilities is also governed by Swiss law (Article 163d(2) Swiss PIL Act). In particular, the transfer of contracts is governed by Swiss law.

If the Swiss company transfers its entire assets and liabilities, the places of debt enforcement and of jurisdiction remain in Switzerland until the claims of its creditors have been secured or satisfied (Article 164a Swiss PIL Act). Furthermore, if the Swiss company is registered in the Swiss Register of Commerce, it cannot be deleted until the claims of its creditors have been secured or satisfied (Article 164 Swiss PIL Act).

As regards the foreign company, its *lex societatis* applies to all aspects concerning the overtaking company.

### 4. *The Law Applicable to Merger, Demerger and Transfer Contracts (Article 163c Swiss PIL Act)*

The law applicable to merger, demerger and transfer contracts follows the general system existing in Swiss private international law<sup>88</sup>: the contract is governed by the

<sup>87</sup> Although the application by analogy of Article 163b(3) of the Swiss PIL Act is excluded by the last sentence of Article 163d(1) of the Swiss PIL Act, the said provision must apply to a transfer of the entire assets and liabilities to a foreign company. Otherwise, the situation of the creditors of the Swiss transferring company would be worse in an emigration of the entire assets and liabilities than in a division by emigration, although the economical situation is exactly the same.

<sup>88</sup> See Articles 116 and 117 Swiss PIL Act.

law chosen by the parties<sup>89</sup>; in the absence of a choice of law clause, the contract is governed by the law of the State with which it is most closely connected (see Article 163c(2) and (3) Swiss PIL Act). Furthermore, the Swiss PIL Act presumes that the closest connection exists with the State whose law governs the surviving company in the case of a merger (Article 163c(2) Swiss PIL Act), the demerging company in the case of a demerger (Article 163d(3) Swiss PIL Act) and the transferring company in the case of a transfer of assets and liabilities (Article 163d(3) Swiss PIL Act).

However, the nature of a merger, demerger or transfer contract is specific as it constitutes the basis of the reorganization of the companies and specifies all the rules applicable to the modification of the social structure of the companies involved. As a result, the said contract has a mixed nature: in certain aspects, it is classified in the legal category of 'contracts' and, in others, in the legal category of 'companies'.

As regards the aspects of company law, a merger, demerger or transfer contract must comply with the mandatory provisions of the company law applicable to the merging companies, including the provisions as to form, without taking account of the law chosen by the parties (Article 163c(1) Swiss PIL Act). In practice, this means that the strictest *lex societatis* is applicable to the aspects of company law of the contract, although the other aspects are governed by the law chosen by the parties or the law of the most closely connected State.

### C. Common Provisions Applicable in Cases of Emigration of a Swiss Company

The specific provisions previously described are completed by common provisions applicable to the four types of reorganization of companies. The common provisions aim to protect the rights of creditors or partners of a Swiss company which emigrates by operation of a transfer, merger, demerger or transfer of assets and liabilities.

#### 1. Protection of Rights of Creditors and Partners prior to Deletion from the Register of Commerce (Article 164 Swiss PIL Act)

As regards the rights of creditors, if a Swiss company is registered in the Swiss Register of Commerce, a specially qualified auditor must confirm that the claims of its creditors are secured or satisfied before the company is deleted or its creditors must have agreed with the deletion (Article 164(1) Swiss PIL Act).

<sup>89</sup> The choice of law by the parties is laid down in Article 116 of the Swiss PIL Act, which provides that the choice of law must be explicit or clearly evident from the contract or the circumstances. Furthermore, the contract is governed by the chosen law.

The rights of partners of a Swiss company are also protected: a specially qualified auditor must confirm that the foreign company has attributed the participation or membership rights to the partners of a Swiss company entitled thereto or has made or secured a compensation payment or a settlement (Article 164(2) Swiss PIL Act).

#### 2. Jurisdiction over Actions for Examination of Participation and Membership Rights (Article 164a(1) Swiss PIL Act)

The members of a Swiss company who deem their participation or membership rights not to have been adequately safeguarded by the operation of a merger or demerger may file a special action to examine the participation or membership rights.<sup>90</sup> According to Article 164a(1) of the Swiss PIL Act, this special action may be filed either at the foreign domicile of the overtaking company or at the Swiss domicile of the transferring company. A foreign judgment will be recognized in Switzerland on the basis of Articles 25 *et seq.* and 165 of the Swiss PIL Act.

However, if the Lugano Convention is applicable, Article 164a(1) of the Swiss PIL Act does not apply and the place of jurisdiction is determined by Article 16(2) of the Lugano Convention, which has priority over Article 2 of the Lugano Convention.<sup>91</sup> Article 16(2) of the Lugano Convention confers exclusive jurisdiction on the courts of the seat of a company whose decision on participation or membership rights is disputed.<sup>92</sup> In the case of a merger or demerger, the decision on participation or membership rights is in fact taken by all companies involved. As a result, the members of a Swiss company who deem their participation or membership rights not to have been adequately safeguarded by the operation of a merger or demerger may file the special action for examining participation or membership rights either at the foreign domicile of the overtaking company or at the Swiss domicile of the transferring company, even though the Lugano Convention is applicable.

<sup>90</sup> See Article 105 of the Swiss Merger Law.

<sup>91</sup> Although this question is debated, Article 16(2) of the Lugano Convention should be interpreted broadly; see KROPHOLLER J., *Europäisches Zivilprozessrecht*, 7<sup>th</sup> ed., Heidelberg 2002, ad Art. 22, No 37, p. 257. In our view, an action for examining participation or membership rights under Article 105 of the Swiss Merger Law falls within the scope of Article 16(2) of the Lugano Convention. Same opinion: GIRSBERGER D./RODRIGEZ R., in: WATTER/VOGT/TSCHÄNI/DAENIKER (eds.), *Basler Kommentar zum Fusionsgesetz*, Basel/Geneva/Munich 2005, ad Art. 164a IPRG, No 14, p. 1369.

<sup>92</sup> The application of Article 16(2) of the Lugano Convention means that the Lugano Convention is applicable when the seat of the company whose decision on the participation or membership rights is disputed is situated in a Contracting State of the Lugano Convention.

If the said action is filed in both jurisdictions, Article 23 of the Lugano Convention provides that the second court at which the action was brought shall decline its jurisdiction in favour of the first court. The judgment shall then be recognized in the other contracting State without any special procedure being necessary (Articles 25 *et seq.* of the Lugano Convention).

### 3. **Retention of the Place of Debt Enforcement and Jurisdiction in Switzerland (Article 164a(2) Swiss PIL Act)**

The rights of the creditors and members of a Swiss company are protected by retaining the place of debt enforcement and jurisdiction in Switzerland until their claims are secured or satisfied (Article 164a(2) Swiss PIL Act). As a result of this protection, the creditors or members of a dissolved company are not obliged to bring an action based on company law against the overtaking company abroad.

However, if the overtaking company has its seat in a contracting State of the Lugano Convention, the courts of the seat of the overtaking company have in principle exclusive jurisdiction (Article 16(2) Lugano Convention).<sup>93</sup> The above assertion, although true in cases of an international transfer of company, has to be qualified in the case of a merger, demerger or transfer of assets and liabilities because the organs of all the companies involved have taken the disputed decision. In such cases, action may be brought either at the foreign domicile of the overtaking company or at the Swiss domicile of the transferring company, even though the Lugano Convention is applicable. If action is brought in both courts, the second court at which the action was brought shall decline its jurisdiction in favour of the first court (Article 23 Lugano Convention).

A foreign judgment will be recognized in Switzerland on the basis of Articles 25 *et seq.* of the Swiss PIL Act or Articles 25 *et seq.* of the Lugano Convention.

### D. **Recognition of International Transfers of a Company, Mergers, Demergers or Transfers of Assets and Liabilities among Foreign Companies (Article 164b Swiss PIL Act)**

Swiss private international law allows the recognition in Switzerland of international transfers of a company, mergers, demergers or transfers of assets and liabilities among foreign companies if they are valid under each law involved in the transaction (Article 164b Swiss PIL Act). Accordingly, any reorganization made abroad which does not involve a Swiss company will be recognized in Switzerland, regardless of whether the reorganization involves companies incorporated in different States.

<sup>93</sup> See *supra*, V, C.2.

## VI. Conclusion

The place of organization of a company is the primary rule chosen by the Swiss legislator. This connecting factor is directly inspired by the incorporation theory. In principle, the place of incorporation of the company is where the company has fulfilled publicity or registration provisions (see Article 154(1) Swiss PIL Act). However, the Swiss legislator developed this connecting system by adding two important characteristics.

The fact that the founders of a company are allowed to choose the State of incorporation shows that the Swiss legislator favours the freedom of choice. When choosing this purely formal connecting factor, the legislator was aware that it implied a certain risk of corporation law shopping between States. When making their choice, the founders will take account of the possibilities offered by the legal framework of the particular State. As regards the Swiss connecting system, the first important characteristic is the restriction of the freedom of choice in cases of abuse or fraudulent conduct as a means of protecting the interests of third parties, such as the creditors of a company whose business is carried out in Switzerland despite its incorporation abroad. Thus, Swiss private international law contains rules safeguarding the rights of the creditors of pseudo-foreign companies (see Articles 158, 159, 17 and 18 Swiss PIL Act). These provisions are complemented by the general principle of *fraus legis*, which is to be applied with caution, taking account of the possible effects on the rights of creditors in practice.

The second important characteristic of the Swiss connecting system is the possibility for companies to change their governing law without any prior liquidation or new formation. This can be done in four ways: (1) the international transfer of a company; (2) the international merger of companies; (3) the international demerger of companies; and (4) the international transfer of assets and liabilities. The last three are in place only since 1 July 2004 and thus it is difficult to predict how they will work in practice. At present, there are no corresponding provisions in European Community law providing for the international transfer of a company, the international merger or demerger of companies, or for the international transfer of assets and liabilities. Therefore, one can expect that these tools will not be used very often until corresponding regulations enter into force in European Community law. The absence of legislation governing corporate restructuring and mobility within the European Union prevents the realization of such operations between companies incorporated in a Member State and in Switzerland or at least makes it contingent on complicated legal arrangements. The number of cases of international reorganization involving companies incorporated in a Member State and in Switzerland will probably remain small until the Member States have grown accustomed to reorganizing companies on an international level within the European Union. However, thanks to its progressive law on this matter, Switzerland is ready to actively participate in the international reorganization of companies, which will most probably occur in the near future.

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