Trends and Developments

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Introduction

Corporate governance is a broad notion, blending numerous legal and economic disciplines all in one field. It is also one of the most dynamic areas in company law; constantly evolving to adapt to new legal standards, societal expectations, and market needs.

Amidst this extensive landscape, this article will analyse observable trends stemming from the revision of Swiss corporate law on 1 January 2023, discuss the latest legislative developments in connection with foreign investment controls, present the current legal framework in connection with environmental, social, and governance (ESG) topics, and examine upcoming changes and challenges in the field of ESG.

Observable Trends Stemming From the Revision of Swiss Corporate Law?

If you were among the readers of last year's edition of the Corporate Governance Practice Guide, then you are already aware of the entry into force of the Swiss corporate law reform on 1 January 2023.

Since said revision was the hot topic in 2023, this article will forgo an analysis of the new set of provisions. In a nutshell, the revised law brings greater flexibility in connection with the company capital, increases minority shareholders' rights, strengthens the board of directors' accountability, and modernises the law by explicitly authorising the use of electronic means during shareholders' and board meetings.

Among the items on the companies' to do list since the entry into force of the new law, Swiss joint-stock companies and limited liability companies will have to amend their articles of association (AoA) by 1 January 2025 so as to comply with the new provisions.

Despite the two-year transition period, most companies publicly listed on the SIX Swiss Exchange (SIX) have already amended their AoA in 2023. Said companies have not only included mandatory language in their AoA but have also introduced other optional instruments such as the so-called capital range and the possibility to hold virtual shareholders' meetings. With regard to the latter, some listed companies specified that the virtual format will only be used in specific circumstances, and that they do not intend to shift to virtual-only meetings and will continue to organise physical meetings.

Based on the information available to date, although virtual shareholders' meetings have been introduced in numerous AoA, they have not become a trend. Indeed, it seems that only a few listed companies have made use of this new instrument. Known examples are The Swatch Group AG and AEVIS VICTORIA SA, which both held virtual AGMs in 2023 and 2024.

Since little over a year has passed since the entry into force of the revised law, it is too soon to draw conclusions. It takes time for the introduction of such innovative instruments to gain social acceptance and is often associated with additional costs. Virtual shareholders' meetings and other forms of AGMs (such as AGMs abroad) may yet become a trend.

Foreign Investment Control

Although the foreign investment control topic is not strictly related to corporate governance, it is material as it may have an impact on the shareholder composition of Swiss entities in the near future.

To date, Switzerland has proven to be very liberal in connection with foreign investments and does not have overarching regulations on the review of foreign direct investments. However, there has recently been increased political pressure to establish a local legal framework for foreign investments. In March 2020, the Swiss Parliament adopted the motion "Protection of the Swiss economy through investment controls" and instructed the Federal Council to create a legal basis for the review foreign investments.

The purpose of introducing investment screening would mainly be the prevention of takeovers of Swiss companies by foreign investors should such takeover jeopardise Switzerland's "public order or security". On 15 December 2023, the Federal Council issued the dispatch on the Investment Screening Act (ISA), thereby fulfilling the Parliament's request. The Federal Council nevertheless remains of the opinion that investment screening should not be introduced in Switzerland. In its view, the cost-benefit ratio of investment screening is unfavourable, and the existing regulatory framework is sufficient. Besides, there are no known cases of past company takeovers which jeopardised public order or security in Switzerland. The Federal Council hence limited the scope of application of the draft ISA to very specific transactions.

The draft ISA regulates the prerequisites under which the takeover of a domestic company operating in a particularly critical sector by a foreign, state-controlled investor would be subject to an approval. Such approval would only be required provided certain thresholds would be reached. Sectors considered as particularly critical within the meaning of the draft ISA include defence equipment, dual-use goods, electricity transmission and production, water supply, or health, telecom and transport infrastructures. The notion of "takeover" is defined in the draft ISA and is assumed to exist when the investor has the possibility to exercise a decisive influence on the activities of another company, eg, influence executive decisions and determine the company's general business policy. In principle, the acquisition of minority stakes would not fall under the scope of such law.

Under the draft ISA, a takeover is approved if there is no reason to assume that public order or security is endangered or threatened.

The adoption of the ISA would have an impact on the Swiss M&A market, although the extent of it would probably be limited since only a small number of takeovers would be subject to an authorisation under the current draft ISA. In fact, takeovers by foreign, privately-owned investors would be allowed even if they concern a critical sector. The draft ISA will go into parliamentary deliberation and may be subject to significant changes. It is not expected to enter into force prior to 2025.

Current ESG Legal Framework

ESG is a widely used acronym standing for "environmental, social, and governance". ESG topics have become increasingly significant lately, as they reflect a growing demand from stakeholders and regulatory bodies for enhanced transparency, accountability, and ethical conduct in business operations.

The environmental aspect focuses on the impact of business activities on ecological conditions and includes topics such as biodiversity, climate change, pollution, and circular economy. The social component deals with the impact of businesses and their respective activity on society (eg, working conditions, remuneration, and child protection). And, finally, governance refers to the systems of rules, practices, and processes by which a company is controlled, directed, and managed (eg, risk management, corporate ethics, diversity at the executive level).

The legal framework in the context of ESG-related requirements and duties is rapidly evolving and its level of detail is increasing over time. Members of the board of directors, executives and in-house counsels find themselves confronted with a regulatory tsunami and now need to rapidly learn how to ride the wave.

In Switzerland, new ESG-related provisions were introduced in the Swiss Code of Obligations (CO) on 1 January 2022. Such provisions were modelled on the then already existing set of European rules and regulations and introduced two main changes. On the one hand, in the spirit of transparency, large Swiss companies will have to report on the risks generated by their activities in connection with non-financial matters (environmental concerns, social issues, employment-related aspects, respect of human rights and the fight against corruption). On the other hand, companies carrying out operations exposed to specific risks will have to comply with extended reporting and due diligence requirements in the sensitive areas of child labour, minerals and metals from conflict and high-risk areas.

Said obligations apply for the first time with respect to the financial year 2023; the corresponding reports will be available as of 2024.

Reporting obligations on non-financial matters (Articles 964a et seq CO)

The annual reporting obligations on non-financial matters apply to "large undertakings" (Article 964a, Paragraph 1, CO), ie:

- companies of public interest (mainly listed companies, banks, insurances and asset managers, as well as collective investment schemes);
- employing, together with Swiss or foreign undertakings which they control, at least 500 full-time equivalents on annual average for two consecutive financial years; and
- exceeding, together with Swiss or foreign undertakings which they control, at least one of the following figures in two consecutive financial years: a balance sheet total of CHF20 million, or a turnover of CHF40 million.

Undertakings controlled by another entity either subject to Article 964a, Paragraph 1, CO or which must draw up an analogous report under foreign law, are exempt from the reporting obligations.

In-scope undertakings must prepare a report on the impact of their business activities on non-financial matters, ie, environmental matters (in particular, CO2 objectives), social and employment concerns, respect of human rights, and the fight against corruption. Among the key topics, the report must include: a description of the business model, the policies adopted by the undertaking in relation to the aforementioned matters, including the due diligence applied, the measures taken to implement said policies and an assessment of the effectiveness of such measures. Additionally, the main risks related to non-financial matters and the methods applied by the undertaking to deal with them must be specified.

With regard to environmental matters, the new Ordinance on Climate Disclosures (OCD) entered into force on 1 January 2024, and is applicable to large undertakings having to report under Article 964a, CO. The OCD implements the internationally recognised recommendations of the Task Force on Climate-related Financial Disclosures. The environmental section of the report shall namely contain disclosures on the impact of the business activities on the climate, the company's targets for reducing direct and indirect greenhouse gas emissions, as well as how it plans to implement them.

The section on social matters shall include a description of the measures taken to protect the various stakeholders (eg, shareholders, employees, clients, suppliers, creditors, media, and authorities).

The chapter on employment matters may include information as to the working conditions, the employees' rights to be informed and consulted, the respect for the rights of labour unions, health protection, the employees' safety as well as gender equality topics.

The section on the respect for human rights shall be based on the international human rights provisions ratified and approved in Switzerland.

Finally, the report shall specify the measures taken and the instruments available to fight against corruption, ie all conducts which are punished by the Swiss Criminal Code (SCC).

Swiss law also introduces a "comply or explain" approach stating that undertakings may forgo to report on specific non-financial matters if they have not adopted a policy in connection therewith (Article 964b, Paragraph 5, CO). This may occur if, based on the activities carried out, the company is not exposed to significant risks in one of the relevant matters. If no policy is applied, the report must mention it clearly and provide the reasons thereof.

In a joint-stock company, the report on non-financial matters must be approved and signed by the board of directors. It must also be approved by the shareholders' general meeting (Article 964c, Paragraph 1, CO). The board of directors must ensure that the report is published electronically immediately after its approval and that it is accessible to the public for at least ten years. In connection with the publication of the environmental section of the report, additional requirements apply (Article 4, Paragraph 2, OCD): the electronic publication must be made in at least one human-readable and one machine-readable format for international use and must be available on the Company's website. The obligation to publish a machine-readable format must be fulfilled by 1 January 2025 at the latest.

Transparency obligations for companies operating in the raw materials sector (Articles 964d et seq, CO)

The set of provisions governing transparency obligations in the raw materials sector have been in force since 1 January 2021. Their purpose is to increase transparency in the commodities sector and reduce the risk that payments to governments in countries where raw materials are extracted or harvested will trickle away due to mismanagement and corruption or are misused to finance conflicts.

Undertakings subject to an ordinary audit by law and which are either themselves or indirectly through a company that they control involved in the extraction of minerals, oil or natural gas or in the harvesting of timber in primary forests must draw up an annual report on the payments they have made to state bodies (Article 964d, Paragraph 1, CO).

As of now, the reporting obligation does not apply to companies active in the trading of raw materials. The Federal Council has, however, the power to extend the scope of application of the provisions to such activities as part of an internationally co-ordinated procedure (Article 964i, CO).

The report shall cover any payments of CHF100,000 or more in any financial year made to state bodies (Article 964f, Paragraph 2, CO).

In a joint-stock company, the report must be approved by the board of directors. It must be published electronically within six months as of the end of the financial year and shall be accessible to the public for at least ten years.

Due diligence and transparency obligations in relation to minerals and metals as well as child labour (Articles 964j et seq, CO)

Undertakings whose seat, head office or main place of business is located in Switzerland are subject to due diligence obligations in the supply chain and must report thereon if:

- they place in free circulation or process in Switzerland minerals or metals containing tin, tantalum, tungsten or gold from conflict-affected and high-risk areas; or
- they offer products or services in relation to which there is a reasonable suspicion that they have been manufactured or provided using child labour.

The Ordinance on Due Diligence and Transparency in relation to Minerals and Metals from Conflict-Affected Areas and Child Labour (DDTrO) provides for further details on the due diligence and transparency obligations. For instance, the DDTro sets forth the conditions under which an exemption from certain obligations is possible, ie:

- the yearly determination of import quantities of minerals and metals below which an undertaking is exempt from the due diligence and reporting obligations;
- the conditions under which small and medium-sized undertakings as well as other entities presenting low risks in relation to child labour are not required to check whether there are reasonable grounds to suspect child labour and are exempt from the due diligence and reporting obligations; and
- the prerequisites under which undertakings are exempt from due diligence and reporting obligations, provided they adhere to internationally recognised and equivalent set of rules (eg, OECD principles).

Undertakings subject to due diligence and reporting obligations in connection with child labour must verify whether their products or services come from, are manufactured in or are supplied in countries which according to the latest Children's Rights in the Workplace Index (latest available version dated June 2023) are classified as "basic" (ie, presenting a low risk), and not as "enhanced" (ie, presenting a medium risk) or "heightened" (ie, presenting a high risk). Noteworthy is the fact that according to such index, Switzerland is listed as presenting a low risk for child labour. If, based on the due diligence assessments, there are reasonable grounds to suspect child labour, the undertaking must comply with the obligations set forth in the CO. Such reasonable grounds may result from internal findings (eg, on-site controls, interrogations) or external facts (eg, press articles, court judgments, other publications).

Undertakings falling under the scope of Article 964j, CO, must set up a management system which shall stipulate the following (Article 964k, Paragraph 1, CO):

- Supply chain policies on minerals and metals potentially originating from conflict-affected and high-risk areas.
- Supply chain policies for products or services in relation to which there are reasonable grounds to suspect child labour.
- A supply traceability system.

The risks of harmful impacts in the supply chain shall be assessed and identified, and measures shall be taken to minimise the identified risks.

To be noted that compliance with due diligence obligations related to minerals and metals shall be audited by an independent expert, whereas no such third-party review is required in connection with child labour (Article 964k, Paragraph 3, CO).

The due diligence findings shall then be included in a report to be drawn up annually. In a joint-stock company, the board of directors must ensure that the report is published electronically within six months as of the end of the financial year and must be accessible to the public for at least ten years. Unlike the report on non-financial matters, this report does not need to be submitted to the shareholders' general meeting for approval.

Violations of the reporting duties

Providing false information in the reports pursuant to Articles 964a, 964b and 964l, CO or failing to draw up the latter may be punished with a fine of up to CHF100,000 (Article 325ter, SCC), if the person acted intentionally. The fine is lower if the person acted negligently (ie, up to CHF50,000 according to Article 325ter, Paragraph 2, SCC). Only the persons responsible for drawing up the reports may be punished under Article 325ter, SCC. The board of directors is primarily concerned by this provision, although it may delegate certain tasks in connection with the reporting obligations to specific members, committees or third parties. Depending on the circumstances, the board of directors may be released from liability if it is able to prove that it exercised all due care and diligence when selecting, instructing and supervising the persons to whom the tasks have been assigned.

New ESG Developments and Challenges

Due to the close economic ties between Switzerland and the EU, the recent and upcoming changes in the EU-legislation impact the Swiss legal framework and the operations of Swiss entities carrying out business in the EU.

The entry into force of the new EU Corporate Sustainability Reporting Directive (CSRD) at the beginning of 2023 is a first example. So as to align Swiss statutory law to the CSRD, Swiss reporting obligations on non-financial matters will likely be revised soon. In this context, the Federal Council aims at preparing a first consultation draft by July 2024. Among the envisaged changes, a new threshold will be introduced: companies with 250 employees (instead of 500 as currently required) for two consecutive years will be expected to report on risks connected to their business activities in the areas of environment, human rights, and the fight against corruption as well as the measures taken in this regard. It is, however, not yet clear whether any other prerequisites in the scope of application will be amended. Additionally, the report will be subject to a mandatory review by an external auditor.

On 24 April 2024, the European Parliament approved the new corporate sustainability due diligence directive (CS3D). The Union's Council is expected to formally adopt the final text of the CS3D in May 2024. The CS3D will not only apply to EU entities but also to non-EU companies (ie, also Swiss undertakings), provided certain thresholds in revenue are generated in the EU. It will also apply to ultimate parent companies of groups which reach the same thresholds on a consolidated group basis. Said directive will introduce comprehensive human rights and environmental due diligence obligations, and provide for pecuniary penalties and civil liability for companies which are not fully compliant.

The aforementioned developments in the law show that a significant shift in companies' behaviour and internal policies is now inescapable when it comes to responsible business conduct. Indeed, for in-scope undertakings, compliance with ESG topics is no longer a nice-to-have, but a mandatory requirement. As a result, companies must now re-organise themselves, and set up specialised teams in charge of ensuring compliance with applicable laws and regulations. They also need to build awareness within their organisation as well as towards their contractual partners to ensure the necessary information can be collected in time, and the risks and threats are reported if and when they come up. Opposing interests, including the protection of business secrets, may stand in the way of the due diligence and transparency obligations.

Moreover, since in-scope undertakings are often large international groups, they are also faced with the challenge of determining which national standards to apply, and how to draw up the reports. Although drawing up a single report for a group would be the preferred solution, this is not always feasible due to divergent legal requirements. In public listed companies, ESG topics will increasingly be the focus of shareholder activism. ESG reports will be scrutinised by activists and weaknesses in the implementation of specific obligations will undoubtedly be used by the latter to advocate a re-organisation of a company's corporate governance.