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Magazine

No 3 | January 2015

Swiss Venture Capital Report

In cooperation with S·E·C·A
Swiss Private Equity & Corporate Finance Association

Recent exits: key learnings from a legal perspective

In the last couple of years, Switzerland has seen many successful exits (Doodle, hybris, kooaba, Covagen and many more). That's great news. However, we have encountered several pitfalls that require careful thought, predominantly in the shareholders' agreement.

Beware of ROFR

A right of first refusal (ROFR) undoubtedly has advantages. In an exit scenario, though, potential acquirers may either ask for an advance waiver of the ROFR beneficiaries (in order to establish deal uncertainty), or even shy away from the deal because they are not willing to buy into the transaction (which has cost implications and requires management attention). Strategic investors may benefit from the ROFR, since they remain the only exit route for all other shareholders; needless to say, this can have a severe impact on the purchase price.

Avoid tax issues

The overall aim in a disposal of the start-up should be (i) to preserve a tax-free capital gain for Swiss resident sellers, and (ii) to avoid any unforeseen tax / social security consequences. Our practice shows, however, that in virtually every exit tax omissions or non-ideal tax structuring pop up. Facts that could jeopardise such aims include, for example, salaries of employee-shareholders that are not at market, share transfers between (employee-) shareholders not at arm's length, transfer of intellectual property not at market value, old employee stock option plans (ESOP; the law changed about two years ago) and so on.

Consider DAP carefully

A simply phrased drag-along provision (DAP) obliges the minority shareholders to co-sell their shares with the majority shareholders at the same terms and conditions. This may lead to the result that such minority shareholders would need to give the same representations and warranties as the other shareholders and/or the company (and are hence also liable for misrepresentation or breach of warranty, perhaps even on a joint and several basis), or it may result in a severe tax issue in a share swap transaction for shareholders resident in the US, or last but not least, a non-competition obligation could be imposed on minority shareholders. Even though these are all issues that the shareholders concerned may dislike, they remain contractually bound by the DAP and have to behave accordingly (if not, liquidated damages in line with the SHA may apply).

SHAs should be flexible

Most start-ups undergo difficult times, perhaps because they run out of money, the management team needs to be adjusted, or for many other reasons. In such a scenario, amendments to the shareholders' agreement (SHA) with unanimous consent of all shareholders may prove to be too onerous – in the sense that this might endanger further, urgently needed, funding. It is also legally questionable whether (qualified) majority decisions are able to change a contractual relationship for all shareholders. It's of paramount importance for the Swiss venture ecosystem, though, that it works legally.

The French saying 'gouverner, c'est prévoir' applies to the drafting of SHAs as well: learnings as stated above (and many others) should be taken into consideration on a case-by-case basis, discussed with the parties involved to avoid unpleasant surprises, and be reflected accordingly in a professional manner in the SHA.

Wenger & Vieli Ltd.

We are a leading law firm with offices in Zurich and Zug. One of our strengths is in the area of venture capital (VC), where we advise investors, companies and founders alike through the whole life cycle: on tax-efficient fund structures, acquisition of portfolio companies, exit routes, etc. As a one-stop shop, we take care of intellectual property, regulatory, employment, general contract and corporate law. We offer the full range of all notarial services needed in the VC business.

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