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Newsletter Banking and Securities

Federal Supreme Court Finds Share Swap Transaction Not A Voidable Preference

Facts:

On May 28, 2009 the Federal Supreme Court held the share swap transaction entered into by SAir Group not to be a voidable preference under Swiss insolvency law. [1]

In December 2000 SAir Group sold 250'000 of its own shares to X at the then market price of CHF 275 per share ("Initial Price"). The agreement provided for a cash settlement of the final purchase price; the difference between the Initial Price paid and the final purchase price at the end of the agreed one year period was to be paid by (i) either X, if the share price was above the Initial Price, or (ii) SAir Group, in case the share price was lower than the Initial Price.

There was no obligation on SAir Group to buy back the shares. In addition, SAir Group had the right to terminate the transaction prior to the expiration of the one year period under certain circumstances.

During the term of the agreement, SAir Group had to pay interest and X had to transfer the dividends to SAir Group received under the shares transferred. X was further entitled to payments ("Collaterals") if the market price for the shares fell below 50% of the Initial Price and X was under an obligation to make payments to SAir Group, if the market price increased again to 60% of the Initial Price. SAir Group made payments in excess of CHF 60 Million and X made payments in the amount of CHF 12.1 Million to SAir Group under this clause of the agreement.

The liquidator of the SAir Group challenged the payments made by SAir Group to X as a voidable preference arguing in substance that the agreement entered into with X was a loan agreement and that the payments made by SAir Group constituted subsequent collateral posted or a repayment of the loan by SAir Group to the detriment of the other creditors.

Decision:

The Federal Supreme Court rejected the appeal of SAir Group and upheld the decision of the court of lower instance ("Commercial Court") rejecting the claim filed by the liquidator.

The Federal Supreme Court argued that the agreement was to be qualified as a so called "*Innominatkontrakt*" *i.e.* a contract which is not particularly dealt with in the Swiss Code of Obligations and which consisted of several elements.

The Federal Supreme Court reasoned that the basic structure of the share swap transaction was one of a purchase of shares which contained an adjustment of the final price at the end of the agreed period. In addition, the agreement also had a term element, during which the parties were under an obligation to make certain payments and which element distinguishes the agreement from a plain-vanilla purchase agreement.

The Federal Supreme Court also found that the only element which the agreement had in common with a loan agreement was the element of certain duration but that the central element were the mutual obligations to make payments during the term. The Federal Supreme Court also found the agreement to be a full two way contract ("*vollkommen zweiseitiger Vertrag*"), unlike a loan agreement, and further argued that the agreement was not one of a fiduciary transfer of title under which X was under an obligation to retransfer the shares received to SAir Group. The parties' intent was a full transfer of title to the shares.

The Federal Supreme Court then proceeded to analyze, whether the "Collaterals" are subject to challenge as a voidable preference. As mentioned above, the Federal Supreme Court stated that the

[1] http://jumpcgi.bger.ch/cgi-bin/JumpCGI?id=28.05.2009_5A_420/2008

transaction was not one of a loan agreement and the only resemblance of the transaction to a loan agreement was the element of a certain duration. It also concluded that the share swap transaction fulfilled all the criteria of a full two way contract and that therefore the Collaterals cannot be qualified as a (partial) repayment of a loan.

The Federal Supreme Court also rejected the argument that the Collaterals should be qualified as the subsequent posting of a security and characterised the Collaterals as a periodical adjustment of the final price during the term and as consideration for the continuing provision of liquidity and as a so called "synallagmatic contract".

The Commercial Court had held that the agreement could be terminated by X in the case of a default by SAir Group under the periodical payment obligation and that by reference to the ISDA Master Agreement the transaction was even terminated automatically. Therefore, the Federal Supreme Court concluded that the financial situation of SAir Group would not have been any different had the Collaterals not been provided and the agreement terminated. Furthermore, the Federal Supreme Court did find relevance in the fact that neither party could directly influence the share price and therefore the amount of Collaterals to be exchanged. In addition, the Federal Supreme Court found that the development of the share price was not foreseeable at the time of the entering into the transaction.

The Federal Supreme Court finally rejected SAir Group's claim since it found no damage. Consequently, the question of whether or not there was an intent to harm other creditors or whether such effect was foreseeable was not to be dealt with.

Comment:

The decision of the Federal Supreme Court appears to be the first one where it had to deal with an avoidance action of a share swap transaction.

The Federal Supreme Court's decision hinges upon the fact that the agreement was qualified as a full two way contract and not a loan agreement.

Whether or not this qualification can be upheld also in respect of other swap transactions must be analysed in each and every single case.

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