Foreign bankruptcies in Switzerland: recovering assets may have just become easier

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Following a proposal by the Swiss Federal Council,[1] the Swiss Parliament has recently adopted amendments of the provisions governing the recognition in Switzerland of foreign bankruptcies in the Federal Act on Private International Law of 18 December 1987 (PILA). These amendments, which result from almost unanimous criticism from scholars and practitioners alike, significantly modify current legislation governing the recognition of foreign bankruptcies. Subject to an unlikely optional referendum,[2] the new legislation should enter into force most probably on 1 January 2019.

With these new amendments, the Swiss Federal Council hopes to facilitate the recognition of foreign bankruptcies in Switzerland by reducing the cost of such proceedings and waiving the condition of reciprocity, one of the main obstacles to the recognition of foreign bankruptcies in Switzerland. This should allow for an easier recovery of assets, which are today unavailable to some foreign bankruptcies, putting them at risk of enforcement proceedings undertaken by individual creditors.

Current state of the legislation and issues

Foreign bankruptcies in Switzerland

As Switzerland applies the principle of territoriality, a foreign bankruptcy ruling does not deploy any effects in Switzerland. This implies that the trustee/foreign liquidator of the bankruptcy is not entitled to act in Switzerland on behalf of the foreign bankruptcy estate, let alone attempt to recover any of the bankrupt's assets. In fact, any of trustee's/foreign liquidator's activities in Switzerland that aim to recover assets or enforce claims of the bankrupt could constitute a criminal offence.[3]

The only measure that the trustee/foreign liquidator may undertake in Switzerland is petitioning for the recognition of the foreign bankruptcy ruling, which results in the opening of a 'mini' or 'ancillary' bankruptcy before the Swiss court that has jurisdiction, that is, the court where the assets are situated/found. This petition can also be filed by a creditor, but not by the bankrupt itself (although some scholars for a long time have pleaded for the bankrupt to be allowed to do so).

The Swiss courts recognise the foreign bankruptcy ruling rendered in the country of the bankrupt's seat or registered office provided that the following conditions are met:

- the foreign bankruptcy ruling is enforceable in the country of the bankrupt's seat or registered office;
- there are no grounds to deny recognition pursuant to Article 27 of the PILA, that is, the decision is not incompatible with Swiss public policy; and
- reciprocity is granted in the country in which the decision is rendered. According to this principle, a foreign bankruptcy is only recognised in Switzerland if the state in which the foreign bankruptcy ruling was rendered also recognises Swiss bankruptcies and their effects.

If the aforementioned conditions are met, then the Swiss courts formally recognise the foreign bankruptcy by issuing a ruling that is published in the Swiss Official Gazette. This publication triggers specific deadlines, including the two-year period to file an avoidance action in Switzerland.

Once the foreign bankruptcy has been recognised, the local bankruptcy office is in charge of the bankruptcy proceedings, keeping in mind that the foreign trustee/foreign liquidator is merely considered as a creditor/third party. The bankruptcy office calls the creditors and draws up the schedule of claims with only the Swiss and foreign secured creditors (provided the security is situated in Switzerland) and the Swiss privileged creditors that have a priority claim (eg, employees of the bankrupt for their salary). The schedule of claims can only be challenged by these creditors. As a consequence, the trustee/foreign liquidator cannot contest such a schedule of claims.

The surplus of the proceeds of the mini-bankruptcy after distribution to the secured and Swiss privileged creditors in Switzerland are then available to the foreign bankruptcy provided the foreign schedule of claims is recognised, which is regularly the case if the court considers that the regular Swiss creditors have been treated fairly in the foreign bankruptcy proceedings. It is worth noting that scholars consider, in the absence of regular Swiss creditors, the recognition of the foreign schedule of claims should be a mere formality. It is only after this final step that the remaining assets seized in Switzerland are transferred abroad.

De lege lata there is no way around the aforementioned proceedings, whether Swiss creditors exist or not. Consequently, the recovery of assets in Switzerland may prove to be time-consuming, and is greatly dependent on the debtor's behaviour and its dilatory actions.

Issues

As previously mentioned, current legislation and the resulting practice have been criticised in the past. Legal scholars have addressed various loopholes in the current PILA, while legal practitioners have denounced the impracticability of certain legal provisions. Growing discontent among the legal community has led the Swiss Federal Council to propose amendments to the PILA that aim primarily at simplifying costly and time-consuming proceedings.

In particular, the condition of reciprocity has seen its fair share of criticism. When analysing whether this condition is met, Swiss courts have to ensure that the country of the foreign bankruptcy recognises a Swiss bankruptcy under the same conditions. This has led to the drawing up by scholars of an informal list of countries that offer said reciprocity (or not). This list is, however, now outdated because many countries have amended their bankruptcy legislation, in particular, to reflect the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border legislation. In practice, however, local Swiss courts are often reluctant to recognise a bankruptcy from a country not included on the aforementioned list, even though such a country's legislation has been modified in the meantime. Costly legal opinions from both Swiss and foreign scholars analysing and comparing foreign legislation are thus necessary if there is no precedent pertaining to the specific country. Often, a trustee/foreign liquidator has to go all the way to the Swiss Supreme Court to have a foreign bankruptcy recognised, which means considerable effort and cost.

Given this strict and often overwhelming condition, foreign bankruptcies are often quickly discouraged from recovering assets in Switzerland and give up doing so. This allows for individual creditors to freely recover assets in Switzerland by the means of individual debt enforcement proceedings, thus creating inequality among creditors, namely creditors who undertake recovering actions in Switzerland on the one hand and those who do (or can) not on the other hand.

While the goal of such a condition was initially to favour collaboration between countries in the matter of bankruptcies, it has in fact excessively complicated

the process. The Swiss Federal Council therefore came to the conclusion that the objective initially sought had not been met and that the only consequence of the reciprocity condition was an over-complication – if not a barrier – to recognition.

Finally, the recognition proceedings in Switzerland, which are currently mandatory (regardless of the existence of Swiss creditors) were designed to protect Swiss creditors. These proceedings are, however, costly and ineffective when such Swiss creditors simply do not exist, and are thus unnecessary.

These issues were the main reason that led to the revision of provisions in the PILA governing the recognition of foreign bankruptcy. The main elements of this revision are briefly exposed below.

Proposed modifications

Waiving of the provision pertaining to reciprocity

As explained, the waiving of the condition of reciprocity shows a clear failure of the objectives set forth when this condition was introduced: to favour collaboration between countries in the matters of bankruptcy. The waiving of such a condition does not come as a surprise because reciprocity has been consistently criticised by almost every concerned party or practitioner and at every level.

Furthermore, the recognition proceeding of the schedule of claims and the condition pertaining to Swiss public policy, which remain unchanged, offer sufficient safeguards against abusive or politically motivated bankruptcies, which was also a concern of the Swiss legislator.

Possibility of recognising a foreign bankruptcy ruling from the country of the bankrupt's centre of main interest (COMI)

Current legislation precludes many European bankruptcy estates from undertaking the appropriate measures and proceedings in Switzerland aimed at recovering assets. This is mainly due to the fact that European Union Regulation 2015/48 provides that the main insolvency proceedings may be opened where the debtor/bankrupt has the centre of its main interest, which is a notion currently unknown under Swiss law.

This situation is highly unsatisfactory given that Swiss and EU economies are greatly linked, which is apparent in the fact that the vast majority (nearly 80 per cent) of the ancillary bankruptcies opened in Switzerland arise from European countries. In view of Switzerland's growing need to have 'EU-compatible' legislation, the suggestion now is to amend the PILA to include foreign bankruptcy rulings rendered from the courts of the country of the bankrupt's COMI (and not only the country of its seat/registered office).

Waiver of the compulsory ancillary proceeding

As of today, an ancillary bankruptcy must, in any case, be opened in Switzerland to recover assets located there. The reason behind such a requirement is to protect privileged and secured creditors. As a result, ancillary proceedings are mandatory even if there exist none of the aforementioned creditors, resulting in unjustified and complicated proceedings. Under the revised legislation, it will be possible for the trustee/foreign liquidator to request that the ancillary bankruptcy proceeding be skipped. A petition in this sense has to be addressed to the Swiss courts, which will decide to forego said proceeding if, after the publication of the foreign bankruptcy in the Swiss Official Gazette, neither secured nor privileged creditors have come forward. The Swiss courts will, however, continue to make sure that regular Swiss creditors (if any) are treated fairly in the foreign proceeding.

If this simplified 'recognition process' is allowed by the Swiss court, then it will be possible for the trustee/foreign liquidator to act before Swiss courts in Switzerland, as well as begin debt enforcement proceedings, free from any risk of committing unlawful acts on behalf of foreign states.

As the ultimate safeguard, it will be possible for the Swiss courts to require the recognition of the foreign schedule of claims before allowing the transfer abroad of the assets seized in Switzerland.

Possibility for the debtor/bankrupt to file for its bankruptcy

Under the current PILA, only the trustee/foreign liquidator and/or a creditor can petition for the recognition of foreign bankruptcy. This situation is unsatisfactory because the bankrupt often has exclusive and extensive knowledge of its assets and may have an interest for a quick recognition of its foreign bankruptcy.

With the amended PILA, it will not be possible for the debtor/bankrupt to petition itself for the recognition of the foreign bankruptcy, once again with the goal of accelerating and simplifying the transfer abroad of the assets seized in Switzerland.

Protection of the creditors of a branch in Switzerland

Under current Swiss insolvency law, Swiss creditors of the Swiss branch of a foreign debtor may petition for the branch's bankruptcy in relation to its activity and its assets in Switzerland. Therefore, two parallel

proceedings – the bankruptcy limited to the branch ('branch bankruptcy') and the ancillary bankruptcy – have to coexist, which creates issues regarding the allocation of assets between the two.

The amendments to the PILA will codify the interaction and regulate the relationship between these two proceedings. Pursuant to these new provisions, provided the foreign bankruptcy has not been published in the Swiss Official Gazette, the branch bankruptcy remains possible. However, after such a publication, the branch bankruptcy will either be stayed and the creditors of the branch bankruptcy transferred into the ancillary bankruptcy (if the branch bankruptcy is already opened but its schedule of claims is not yet final) or will no longer be possible (if the branch bankruptcy proceedings have not yet started).

The clear limitation between both proceedings and their potential interaction will hopefully contribute to reducing the costs of recovering assets in Switzerland.

Avoidance actions

The last key amendment of the new PILA is undoubtedly the possibility to have foreign rulings on avoidance actions recognised in Switzerland. To date, foreign rulings concerning an avoidance action have not been considered 'foreign bankruptcy rulings' under the PILA, which therefore precluded their recognition. With the new amendments, a foreign avoidance action ruling will be recognised in Switzerland, provided it was rendered in the country of the main bankruptcy and that the defendant to the avoidance claim is not a Swiss resident.

Final remarks

It is quite clear that the Swiss Federal Council's objective with the revised PILA aims both at ending Switzerland isolation in foreign insolvency matters, and reducing the complication and cost of recovering assets located in Switzerland.

The waiving of the condition of reciprocity is a very welcome improvement of Swiss foreign bankruptcies legislation because it will certainly entice trustees/foreign liquidators to begin proceedings in Switzerland. However, it remains to be seen whether the amendments proposed will allow the satisfactory achievement of one of the main goals of this revision. Indeed, the cost of proceedings in Switzerland greatly depends on the bankrupt's behaviour and – the simplified proceedings aside – it is difficult to predict whether the amendments will limit a bankrupt from considerably delaying the proceedings in Switzerland, which is one of the reasons of costly proceedings.

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Notes

1 Swiss Government.
2 The deadline to request a referendum expired on 5 July 2018.
3 Swiss Penal Code Art 271.1. Felonies and misdemeanours against the state / Unlawful activities on behalf of a foreign state