Termination Agreements (Employment) (Switzerland)

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A Practice Note setting out the key considerations and legal issues when an employer is entering into a mutual termination agreement with an employee on termination of employment in Switzerland, including drafting guidance for the mutual termination agreement.

An employer may decide to terminate employment in Switzerland and want to enter into an agreement with the affected employee(s). There are a number of important legal issues that arise when entering into such an agreement. This Note provides an overview of the key aspects of a mutual termination agreement on termination of employment in Switzerland. It considers:

- The form and scope of settlement.
- Any statutory obligations in relation to the mutual termination agreement.
- The timing of when the mutual termination agreement should be provided to employees.
- The admissibility of pre-agreement negotiations and whether they are legally binding.
- The common provisions which should be included in the mutual termination agreement, including possible issues surrounding the effective date of termination and garden leave.
- Termination payments, including any mandatory payments required.
- The inclusion of restrictive covenants.
- The execution formalities for mutual termination agreements.

Form of Settlement

In Switzerland, mutual termination agreements can be written, verbal, or even implied (*Article 115, Federal Act on the Amendment of the Swiss Civil Code, SR 220 (Swiss Code of Obligations) (CO)*). However, some clauses in mutual termination agreements must be in writing to be enforceable, like *non-compete provisions* (*Article 340, CO*). For this reason, and for practical evidentiary purposes, practitioners should always record a mutual termination agreement in writing.

The names for these agreements are:

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- In English, "mutual termination agreement" or "settlement agreement."
- In German, "*Aufhebungsvereinbarung*."
- In French, "*accord de résiliation*."
- In Italian, "*accordo di risoluzione*."

In court proceedings, the parties can also request that the court record a mutual termination agreement in the court minutes. The court will then set out the mutual termination agreement in its order dismissing the proceedings. A settlement during court proceedings has the same effect as a binding court decision.

Statutory Obligations

For a termination agreement to be enforceable, Swiss Federal Supreme Court precedent requires that:

- Both parties must make real concessions.
- The employee must have a justifiable reason for entering into the agreement.

(See, for example, *Federal Supreme Court, First Civil Chamber, 21 July 2021 (4A_57/2021*) and *Federal Supreme Court, First Civil Chamber, 23 October 2018 (4A_13/2018* and *4A_17/2018*).)

The employee must have a justifiable reason to enter into a termination agreement because, by doing so, the employee foregoes the protection under Swiss law of an extended pre-termination notice period in case of accident, illness, or pregnancy.

In practice, the employer's payment of adequate severance generally satisfies the justifiable-reason requirement.

Scope of Settlement

There are no restrictions on the types of disputes that the parties can settle in a mutual termination agreement, if the agreement complies with the statutory requirements (see *Statutory Obligations*).

The parties do not need to refer expressly to any claims or disputes in the termination agreement. However, depending on the circumstances, it may make sense to mention any disputed matters in the recitals to the termination agreement.

Limitations

If the agreement complies with the statutory requirements, the parties generally can release:

- Existing and future claims.
- Claims that are known to the parties.

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- Claims of which the parties should be aware.

However, a party cannot release the other party from a claim unless the party is aware of the claim or at least considers its existence to be possible (*Article 60, paragraph 1, CO*; see, for example, *Federal Supreme Court, First Civil Chamber, 23 October 2018 (4A_13/2018* and *4A_17/2018)*). Therefore, a release clause will not cover claims of which the employee both:

- Was unaware.

- Should not have been aware.

Employers should inform less experienced employees and employees not advised by a lawyer about their possible claims under the employment relationship to reduce the risk of a court later determining that the release clause does not apply to those claims.

A broad mutual release is enforceable under Swiss law when it favours the presumption of a comprehensive release clause that definitively terminates all disputes between the parties.

Timing

When the company should provide the termination agreement to the employee depends on the circumstances of the individual case.

If the employer wishes to give the employee notice of termination and simultaneously offer a termination agreement, the employer generally can do so. However, the employer should always give the employee sufficient time to review the termination agreement before signing it. There is no precedent in Swiss law on how much time the employee must have, but three to five days should be sufficient.

Pre-Agreement Negotiations

Pre-Agreement Negotiations: Documents and Communications Used as Evidence

Under Swiss law, the concepts of "settlement privilege" or "without prejudice privilege," which prohibit the use of negotiations as evidence in later proceedings, do not apply automatically to termination negotiations and settlement terms. However, the parties can make a "without prejudice and not for court use" reservation during termination negotiations when exchanging a settlement proposal or documents. The parties should mark materials that they do not want to be used in any court proceedings with "without prejudice and not for court use."

If a party clearly states this reservation during termination negotiations and the parties' correspondence reflects the reservation, the other party must comply and cannot use the marked proposals or documents as evidence in any legal proceedings. Courts generally accept "without prejudice and not for court use" reservations and do not consider the parties' proposals or the documents and communications the parties exchanged during the settlement negotiation. However, "without prejudice and not for court use" reservations bind only the parties participating in the settlement negotiations and will not override a court order for disclosure in proceedings involving other parties.

When the parties are having settlement negotiations in mandatory conciliation proceedings before court proceedings, or during "instruction hearings" before the court, statements the parties make in those negotiations cannot be recorded, used in court

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proceedings, or considered in the court's decision (*Article 205, Schweizerische Zivilprozessordnung, AS 2010 1739 (Swiss Code of Civil Procedure)*). Therefore, in those contexts, the parties do not need to make a "without prejudice and not for court use" reservation.

Pre-Agreement Negotiations: Legally Binding?

Though termination agreements can be oral or implied, a court is unlikely to treat pre-contractual negotiations of a termination agreement that do not result in a signed document as legally binding because of the far-reaching consequences that the termination of the employment relationship usually has for the employee.

Nevertheless, Swiss law recognises a pre-contractual obligation for the parties to act in good faith towards each other when negotiating a potential settlement agreement, even before they conclude any agreement (*Article 2, Swiss Civil Code of 10 December 1907, SR 210*). A party that breaches this obligation is liable to the other party for any resulting damage.

Termination Agreement: Subject to Contract and Without Prejudice

The parties to a mutual termination agreement can include a provision stating that the agreement is without prejudice (or without prejudice and not for court use) and subject to contract until both parties sign it (see *Pre-Agreement Negotiations: Documents and Communications Used as Evidence*). The clause is valid under Swiss law, but including it is not common practice because it is so unlikely that a court would deem negotiations legally binding absent a signed agreement (see *Pre-Agreement Negotiations: Legally Binding?*).

Mutual Termination Agreements

It is not standard practice in Switzerland to mention any reason for the mutual termination agreement, even "ordinary business reasons."

Parties

There are no legal requirements about what information a mutual termination agreement should include about the parties, though the parties should be clearly identifiable. The usual practice is to include:

- The employee's full name and address.
- The company's full name and address.

Also, mutual termination agreements sometimes include the employee's date of birth and the employer's Swiss company identification number (UID).

The mutual termination agreement cannot end any other employment relationships that the employee has with other group companies unless the other companies are also parties to the agreement.

Termination Date

The parties can agree on the end date of the employment relationship in a mutual termination agreement. The end date can be before the contractual notice period would expire. However, for the employee to have a justifiable reason for entering into a

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termination by mutual consent, the employer must pay the employee's salary until the expiry of the contractual notice period, in addition to any severance payment (see *Statutory Obligations*). Therefore, when entering a mutual termination agreement, the parties can agree on a payment in place of the notice period, which would not be possible if one party had terminated the relationship unilaterally.

Garden Leave

The parties to a mutual termination agreement can agree that the employer will place the employee on garden leave before the termination date even if the original employment agreement did not allow that possibility.

Whether an employee is released from work duties before the agreed termination date depends on the specific agreement. However, a release from work at full pay before the termination date is usually considered an additional benefit for the employee, which counts towards the requirement that the employee have a justifiable reason for entering into the mutual termination agreement. Any set-off of the employee's outstanding vacation entitlements against the release period would be seen as reducing the necessary concession that the employer must make (see *Statutory Obligations*).

However, the Swiss Federal Supreme Court has ruled that if the parties agree to a leave of absence with a duration that significantly exceeds the employee's remaining leave entitlement, the leave is considered lost as part of the employee's compensation (*Federal Supreme Court, First Civil Chamber, 12 February 2002, BGE 128 III 271, consid. 282 E.4 (4C.57/2001)*). The Zurich Labour Court has established a rule of thumb that the agreed leave of absence must be at least three times longer than the employee's outstanding leave for the leave to be considered compensated (*Zurich Labour Court, 25 January 2011 (AN090311)*, and *Zurich Supreme Court, 22 February 2012 (LA1100013)*).

If the parties agree, it is possible to offset against the garden leave period:

- Overtime.
- Time off in lieu, which means compensation for overtime work in the form of time off instead of extra pay.

Termination Payment

In Switzerland, the termination payment usually includes:

- Salary through to the end of the contractual notice period, including if the parties agree to a termination date earlier than the contractual notice period expiration.
- Bonus payments.
- Payments due to the employee based on an employee participation programme, which enables the employee to participate in the company's capital or success.
- Remuneration for outstanding vacation entitlements.
- To the extent they are not compensated by a garden leave period:

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- overtime hours; and
- time off in lieu.

(See *Garden Leave*.)

- Compensation for involuntary early retirement. Some employers make additional contributions to their employees' occupational benefits insurance when terminating employees close to retirement. There is no set formula for this calculation and the compensation is entirely at the employer's discretion.
- Compensation of at least one to two months' salary, if the employee falls sick or has an accident during the notice period and waives their statutory right under Article 336c CO to have the notice period suspended. There is no statutory formula or requirement for compensation in these circumstances, however, employers commonly pay an additional amount of one to four months' salary, depending on length of service.
- Compensation for any other claim or entitlement to which the employee is entitled under their employment agreement.

The amount due to the employee varies from case to case. The termination agreement can include either:

- Separate amounts for each individual entitlement.
- A single, combined amount as a "severance payment."

Amounts Payable to Employee: Termination With or Without Cause

Generally, an employer does not pay severance when it terminates an employee for cause. In a for-cause termination, the employment automatically ends immediately, and the employee no longer has any protection if they fall sick, have an accident, or get pregnant.

The employer still must pay all entitlements accruing until the termination date, for example, salary, vacation, and overtime.

Taxes on Income

The parties should include the following sentence in the mutual termination agreement:

> "The Termination Payment is subject to the usual deductions for tax and social security contributions."

Severance payments to employees who are Swiss tax residents are usually subject to Swiss income taxation. The employee must self-declare the severance payment for Swiss income tax purposes.

The severance payment is subject to a preferential income taxation rate if the employee is all of the following:

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- Older than 55.
- Giving up their professional activity.
- Facing a gap in pension fund contributions due to early retirement.

Foreign nationals living and working in Switzerland are subject to wage tax at source, meaning that the company must withhold wage taxes on the severance payment if the employee:

- Does not hold a permanent residence permit ("permit C").
- Is a Swiss tax resident but is not married to a Swiss national.

The employer deducts the wage tax at source directly from the gross amount of the severance payment.

For non-Swiss tax resident employees who work in Switzerland but live abroad, for example, international weekly commuters or cross-border commuters, tax treatment depends on the period for which the severance payment is remuneration:

- The portion that is remuneration for the period before the termination of the employment contract is subject to wage tax at source.
- For the portion that is remuneration for the post-termination period, for example, early retirement or the loss of future income, Swiss taxation may be restricted under the applicable double tax treaty with the employee's country of residence.

Social Security Taxes

Severance payments the employer makes to the employee on termination of employment are usually part of the employee's salary and are subject to social security contributions. The employer must deduct the employee's part of the social security contributions from the severance payments before transferring any amount to the employee.

The termination agreement should indicate payments that are subject to social security contributions by indicating the amount payable as "gross." That is, the overall amount stated in the agreement should be described as gross, and the employee will receive a lower net amount after deduction of social security contributions.

Time Limits on Payments

All claims arising from the employment relationship become due at the latest on termination of the employment relationship (*Article 339, paragraph 1, CO*). Therefore, unless the parties agree to a later payment date in the mutual termination agreement, the employer must make all payments to the employee no later than the last day of employment.

References

The employee is entitled to a final work certificate or reference letter on termination of the employment relationship (*Article 330a, CO*).

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The best practice is to set out the final text of the work certificate or reference letter in the mutual termination agreement or in a schedule to it. However, in practice, termination agreements often mention only the employer's obligation to issue a favourable certificate to the employee at termination and do not set out the text of the certificate or letter.

Whether an employer can decline to give the agreed reference if new circumstances come to light depends on the specific circumstances, including the specific wording of any release clause in the mutual termination agreement.

In Switzerland, it is not standard practice to mention in the mutual termination agreement the employer's right to decline to give the agreed reference if new circumstances come to light that would have affected the employer's decision to provide a reference in the form set out in the agreement. However, if new facts and circumstances did arise, the employer can revise the wording of the reference letter.

There is no obligation to file a reference with any authority in Switzerland.

Return of Company Property

The agreement should include a clause requiring the employee to:

- Return property belonging to the company.
- Delete any information relating to the business and its contacts.

Swiss law requires parties to an employment relationship to return property received when the employment relationship ends (*Article 339a, CO*). Therefore, the agreement should not contain a clause relieving the employee from the duty to return property and delete information because the clause would be unenforceable.

Confidentiality

There are no confidentiality formalities or requirements in Switzerland. A clause that requires the parties to use reasonable efforts to keep the agreement confidential is valid and enforceable under Swiss law.

Restrictive Covenants

The parties can restate restrictive covenants from the original employment agreement in the mutual termination agreement to guarantee that the covenants remain in force after termination. The parties can also agree on new restrictive covenants in a termination agreement even where the employment agreement did not include them, though doing so is rare in practice. However, such new covenants would be seen as reducing the necessary concession that the employer must make (see *Statutory Obligations*), but this could be compensated by a correspondingly higher severance payment.

Restrictive covenants are valid and enforceable if:

- They are appropriately limited regarding:
    - place;

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    - time; and
    - prohibited activity.

- The employee had insight into the employer's client base or manufacturing and business secrets.
- The employee's use of their knowledge is likely to cause considerable damage to the employer.
- Their duration is not greater than three years unless special circumstances are present.

(*Articles 340 and 340a, CO*.)

Separability

Mutual termination agreements in Switzerland commonly include separability clauses. However, if part of the agreement were held void or unenforceable, a court would need to determine whether and to what extent the remaining agreement still complies with the legal requirements to be valid and enforceable in light of the parties' intent (see *Statutory Obligations*).

Execution Formalities

Although Swiss law does not prescribe a specific form for a mutual termination agreement, the parties should record a mutual termination agreement in writing (see *Form of Settlement*).

The parties to the termination agreement, usually the employer and the employee, need to sign it. The employer's signature must be by a person legally entitled to sign on the employer's behalf. The employer can either:

- Give an explicit power of attorney to the individual signing.
- Register the individual in the commercial register as having signing authority for the employer.

A wet ink signature is only required if the mutual termination agreement contains provisions, like restrictive covenants, that require a written signature. Swiss law does not require that the signatures be witnessed, notarised, or apostilled.

The parties do not need to obtain court approval of the settlement agreement or file it as a matter of public record.

Swiss employment law does not require that a termination agreement be drafted in an official language (generally German, French, or Italian). Rather, a termination agreement can be drafted in any language if both parties understand that language and can grasp fully the content of the agreement.

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