

KEY POINTS

- In March 2020, the Swiss government launched a programme for government-backed bridge loans to support Swiss SMEs experiencing liquidity shortages due to the COVID-19 pandemic.
- Eligible businesses may apply for bank loans with a term of five to seven years that bear no or very little interest and are secured by the Swiss Confederation.
- The structure of the programme allowed for a rollout overnight, with thousands of loans being made within 48 hours of the launch.
- Borrowers should be aware that participation in the programme entails various restrictions, and that non-compliance with those restrictions may have harsh consequences.

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Masterclass in Swiss efficiency: spotlight on Switzerland's government-backed COVID-19 loan programme for SMEs

This article provides an overview of Switzerland's government-backed bridge loan programme for SMEs experiencing liquidity shortages due to the COVID-19 pandemic and discusses selected legal issues that are connected with it. Additional loan schemes that were launched in Switzerland on a Federal and Cantonal level to support specific businesses and industries will not be addressed.

INTRODUCTION

Like most other European countries, Switzerland gradually went into lockdown in mid to late March 2020 in order to combat the outbreak of the COVID-19 pandemic. All restaurants and most shops were closed, and the entire economy was – and still is – strongly affected. A defining factor of the Swiss economy is its dependence on small and medium-sized enterprises (SMEs), many of which are driven by local demand and have small liquidity reserves. These businesses were hit particularly hard by the lockdown. In order to help them bridge their liquidity shortages, the Swiss government launched a CHF20bn bridge loan programme on 25 March 2020, which was later increased to CHF40bn. Within the programme's first week of operation, more than 75,000 loans were made. Additional loan schemes were launched on a Federal and Cantonal level in April and May 2020 to support specific businesses and industries. They will not be discussed in this article.

BASIC CONCEPT OF THE PROGRAMME

Two types of loans are available under the Swiss COVID-19 loan programme: COVID-light loans with a principal amount of up to

CHF500,000 and COVID-plus loans with a principal amount of up to CHF20m, in each case capped at an amount equal to 10% of the applicant's annual turnover. Both types of loans are provided via the Swiss banking system and secured by sureties of the Swiss Confederation. Each loan has a term of five years, which may be extended by up to two years if repayment at the original maturity date would result in considerable hardship for the borrower.

Applicants can apply for both types of loans by submitting a simple online declaration to a participating Swiss bank. Each bank is free to decide whether or not to participate in the programme. As the Swiss National Bank grants preferential conditions to Swiss banks for the refinancing of COVID-19 loans, the participation in the programme can be financially attractive for the banks – although it must be noted that many banks announced that they will donate any profit made in connection with the programme to a charitable cause.

The fact that both facilities are provided via the banking system and that the COVID-light loans are structured in a way that no further review or assessment of the applicant's creditworthiness is required before the loan is made, meant that Switzerland was able to roll out the programme almost overnight,

with thousands of loans being made within 48 hours of the launch. Accordingly, the programme has received a lot of praise from market participants for its efficiency and unbureaucratic processes.

COVID-LIGHT LOANS

Applicants can apply for COVID-light loans by submitting a simple one-page declaration (which can be downloaded from a government website) to a bank participating in the COVID-19 loan programme. The declaration also serves as the credit agreement. Upon receipt of the declaration, the relevant bank will perform a completeness check, but it need not carry out a credit assessment or perform any further review. It also does not check whether the information provided by the applicant is correct. The bank may reject the application without provision of grounds.

Only sole proprietorships, partnerships or legal entities domiciled in Switzerland are eligible for a COVID-light loan. Swiss branches of foreign companies are not eligible. In the declaration, the applicant must confirm that it:

- has been established before 1 March 2020;
- is not subject to any bankruptcy or composition proceedings or in liquidation at the time the declaration is submitted;
- is economically severely impaired due to the COVID-19 pandemic, in particular in terms of turnover;
- has not already received liquidity guarantees in the areas of sport or culture; and

Feature

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- had no more than CHF500m turnover in 2019.

The turnover of the relevant applicant is determined on the basis of its stand-alone financial statements. As a result, COVID-light loans are in principle also available to entities that belong to a group of companies, even if the consolidated turnover of the group exceeds CHF500m.

The principal amount of a COVID-light loan may not exceed 10% of the turnover of the applicant and is capped at CHF500,000. Borrowers are obliged to use the proceeds of their COVID-light loans exclusively to cover their ongoing liquidity needs. Each COVID-light loan is fully secured by a surety provided by the Swiss Confederation. Currently, the interest rate on COVID-light loans is 0% per annum. However, the Swiss Federal Department of Finance has the right to adjust the interest rate once a year based on market developments.

COVID-PLUS LOANS

As is the case for COVID-light loans, the process for obtaining a COVID-plus loan can be initiated by submitting a simple declaration (which is accessible at a government website) to a bank participating in the COVID-19 loan programme. Unlike under the COVID-light loan facility, the bank will perform a customary credit assessment of the applicant upon receipt of the application and the loan will be documented in a normal credit agreement. The bank's assessment may take into account the limited surety by the Swiss Confederation, which is further described below.

While the eligibility criteria for COVID-plus loans are the same as for COVID-light loans, the principal amount may be as high as CHF20m, provided that it does not exceed 10% of the applicant's annual turnover. Borrowers are obliged to use the proceeds of their COVID-plus loans exclusively to cover their ongoing liquidity needs. 85% of the principal amount outstanding under each COVID-plus loan and the interest for one year are secured by a surety provided by the Swiss Confederation. The secured part of the loan bears interest at a rate of currently 0.5% per annum. For the other part of the loan, ie 15%, the bank may charge a competitive interest rate

to be agreed upon between the bank and the borrower. The bank may also ask for additional securities for this part of the loan.

THE DOWNSIDE OF PARTICIPATION: HEAVY RESTRICTIONS FOR BORROWERS

Participation in the Swiss COVID-19 loan programme comes with strings attached. Borrowers may not take the following action while they have amounts outstanding under a COVID loan:

- distribute dividends or reimburse capital contributions;
- make loans or refinance "private loans" or shareholder loans;
- repay intra-group loans;
- transfer funds made available under the COVID-19 loan programme to an affiliate domiciled outside of Switzerland; or
- use funds made available under the COVID-19 loan programme for new investments in fixed assets, unless these are replacement investments.

The restrictions listed in para. (a) to (c) above apply irrespective of whether the respective payments are made from funds made available under the COVID-19 loan programme. The restrictions will have a limiting effect on the borrower's freedom to operate, which must be weighed against the benefits of participating in the programme.

No distribution of dividends and no reimbursement of capital contributions

First of all, a borrower may neither distribute dividends nor reimburse capital contributions. The primary purpose of this restriction is to secure the assets available for debt service. For this reason, this prohibition also applies to non-cash dividends and most probably also to the distribution of dividends that were resolved before the COVID loan was made to the borrower. There is a high likelihood that the repurchase by the borrower of its own shares would be treated akin to a dividend payment.

Under Swiss corporate law, the enforcement of any guarantee or security provided by a Swiss company for liabilities

of its affiliates (other than its wholly owned subsidiaries) would likely be treated akin to a dividend distribution. For this reason, borrowers of COVID loans may no longer provide such guarantees or securities, unless their enforcement is subject to the prior repayment of the respective loan. This will limit the ability of borrowers under the COVID-19 loan programme to participate in group financing arrangement.

No making of loans

Borrowers of COVID loans may not make loans to any person. According to the Swiss Federal Department of Finance, an exception applies for loans that are made to a Swiss affiliate of the borrower (in particular to its parent) for the purpose of enabling such affiliate to meet its existing interest payment obligations and, as of 1 February 2021, its existing obligations for scheduled amortisations.

No refinancing of private loans or shareholder loans

In addition to the prohibition to make loans, borrowers must not refinance any private loans or shareholder loans. The term "private loan" is not commonly used in Switzerland, but it is most likely intended to cover all loans that are not made by the public sector.

The prohibition to refinance private loans and shareholder loans does not apply to the refinancing of account overdrafts made on or after 23 March 2020 with the bank making the COVID loan. This exception was introduced in order to prevent companies from being unable to make timely salary payments, as the COVID loan facilities were not available before 26 March 2020. Furthermore, pursuant to the template surety agreement to be used in connection with COVID-plus loans, any loans made by financial institutions shall not qualify as "private loans". Based on this and a related clarification issued by the Swiss Federal Department of Finance, the scheduled repayment of loans made by financial institutions is permissible. The same should apply to repayments prior to maturity based on an event of default, provided that the credit relationship already existed when the COVID loan was taken out.

No repayment of intra-group loans

Borrowers of COVID loans may generally not repay any intra-group loans. The Swiss Federal Department of Finance has communicated two important exceptions to this rule: First, payments based on pre-existing contractual obligations to maintain operations, such as scheduled amortisations, remain permissible. Second, repayments to Swiss affiliates (in particular to the borrower's parent) are permitted if they are made exclusively for the purpose of enabling such affiliates to meet their existing interest payment obligations and, as of 1 February 2021, their existing obligations for scheduled amortisations.

No transfer of funds to an affiliate domiciled outside of Switzerland

Borrowers may not transfer any funds made available to them under the programme to an affiliate domiciled outside of Switzerland. On that basis, one could assume that not only loans made to foreign affiliates, but also interest payments and payments for the provision of goods and services, are prohibited. Accordingly, the Swiss Federal Department of Finance issued a statement clarifying that payments based on pre-existing contractual obligations to maintain operations remain permissible, in particular ordinary interest payments and ordinary payments for the provision of goods and services.

No use of funds for new investments in fixed assets

Funds made available under a COVID loan facility may not be used for new investments in fixed assets, unless they constitute replacement investments. In our opinion, the term "new investment" only comprises investments to which the borrower has not already committed itself before taking out a COVID loan. For example, if a borrower has an ongoing construction project and suffers a liquidity shortage due to the COVID-19 pandemic, then the borrower should be permitted to pay the costs of this ongoing construction project with funds that were made available under the COVID loan. Otherwise, the construction would have to be stopped, which would have a negative impact on the borrower's creditors. It should also be noted that only the direct use of

the funds made available under a COVID loan for such new investments is prohibited.

Implications on cash pooling arrangements

Based on the restrictions described above, it is unclear to what extent a borrower of COVID loans may continue to participate in cash pooling arrangements. In a landmark decision, the Swiss Federal Supreme Court held that receivables of a Swiss cash pool participant vis-à-vis the pool leader under a physical cash pooling arrangement qualify as loans (decision 4A_248/2012 of the Federal Supreme Court dated 7 January 2013). Accordingly, each sweep from an account of a Swiss cash pool participant in the context of a physical cash pooling arrangement constitutes a loan to the pool leader, which is prohibited under the Swiss COVID-19 loan programme. If the Swiss cash pool participant has incurred indebtedness vis-à-vis the pool leader, repayment of that indebtedness would constitute a repayment of a loan. Such a repayment is only permitted under the programme if it is made in accordance with the rules for the repayment of intra-group loans set out above. The same considerations apply if a Swiss cash pool participant provides funds directly to another participant, rather than via the pool leader.

A different regime applies to notional cash pooling arrangements. Although they typically do not entail intra-group loans between cash pool participants and the pool leader, they usually provide that each participant guarantees payment of each other participant's liabilities. Upon enforcement, such guarantees may be treated akin to dividend distributions from a Swiss corporate law perspective, which would again be prohibited under the COVID-19 loan programme. If the guarantee was granted at arm's length terms, the claim for recourse may be treated akin to a loan, which would also be prohibited under the programme.

Criminal and civil liability in case of non-compliance

Potentially harsh consequences may apply in case of a borrower's non-compliance with the terms and conditions of the COVID-19 loan programme. Accordingly, anyone who deliberately obtains a COVID loan with

false information or uses the proceeds of a COVID loan in contravention of the restrictions imposed by law is liable to a fine of up to CHF100,000.

In addition to the criminal sanction, the borrower's corporate bodies and all persons entrusted with the management of its business may be held personally, jointly and severally liable for damages suffered by creditors (including the lending banks) and the Confederation if the proceeds of a COVID loan are used in any way other than for its lawful purpose. It should be noted that this liability extends to every member of the board of directors, the management, the auditors and – although the scope is unclear – potentially also the shareholders or partners of a limited liability company. Persons who fall within the ambit of the civil liability regime should ensure that the borrower does not use the loan proceeds unlawfully. In certain cases, this may require a separation of the amounts borrowed under a COVID loan from the borrower's other funds and close monitoring or even approval of each individual appropriation.

CONCLUSION

The Swiss COVID-19 loan programme has received a lot of praise from domestic and international market participants, and rightly so. It offers efficient and unbureaucratic relief for Swiss SMEs that are experiencing liquidity shortages due to the COVID-19 pandemic. Nevertheless, participation in the programme comes with strings attached. Borrowers should carefully weigh the benefits of their participation against the restrictions imposed and ensure their compliance with those restrictions in order to avoid potentially harsh consequences. ■

Further Reading:

- COVID-19 measures from a lender's perspective (2020) 7 JIBFL 460.
- COVID-19 relief measures and international financings: the law of unintended consequences? (2020) 4 JIBFL 267.
- LexisPSL: Banking & Finance: Coronavirus (COVID-19) – implications for Banking & Finance lawyers.