LEXOLOGY
Getting The Deal Through

VENTURE CAPITAL

Switzerland

Venture Capital

Contributing Editor

Curtis L. Mo

DLA Piper

Generated on: December 13, 2023

LEXOLOGY
Getting The Deal Through

Explore on **Lexology**

Contents

Venture Capital

Contributors

Switzerland

VISCHER AG

VISCHER

Gian-Andrea Caprez	gcaprez@vischer.com
Christian Wyss	cwyss@vischer.com
Luzius Zumstein	lzumstein@vischer.com
Sandro Bernet	sbernet@vischer.com

MARKET AND PURPOSE

General role and purpose
How would you describe the role of venture capital in the financing markets in your jurisdiction?

Venture capital plays an ever-growing role in the Swiss financing markets. This trend is attributable, among other factors, to the strong Swiss education system with its renowned universities such as the ETH Zurich and the EPFL Lausanne. In addition, the country's tradition of boosting innovative industries and an advanced financial sector are also key factors to bring together entrepreneurs and investors. In this fertile environment, the Swiss venture capital industry has grown significantly over the last decade with a significant acceleration in recent years.

Market conditions
How would you describe the current market conditions for venture capital in your jurisdiction?

According to the Swiss Venture Capital Report 2023 published by startupticker.ch and the Swiss Private Equity & Corporate Finance Association (SECA), 383 financing rounds have been completed in Switzerland and an aggregate amount of 3.96 billion Swiss francs has been invested in Swiss start-ups in 2022 – a 29.7 per cent increase compared to 2021. This emphasises the long-term growth trend in Swiss venture capital despite challenging macroeconomic conditions. The top 20 financing rounds by size in 2022 raised 2.58 billion Swiss francs of the overall investment proceeds in 2022, led by a 600 million Swiss francs financing round by Zurich based Climeworks, a company active in direct air capture technology. Due to the relatively low boundaries to access the Swiss financial markets, a wide range of domestic and foreign investors, including dedicated venture capital funds, family offices, private investors such as business angels, strategic investors (ie, seasoned companies in the respective industries) and institutional investors (such as corporate venture capital investors) are active in the Swiss venture capital sphere.

Looking at invested venture capital relative to its population size, Switzerland ranked third in Europe in 2022 according to Swiss start-up accelerator Venturelab. This drive is underpinned by government-backed initiatives on the cantonal and federal level to foster innovation in Switzerland such as the Swiss Innovation Agency Innosuisse, the Swiss Technology Fund created by the federal government and cantonal agencies such as Innovaud or Fondazione Agire.

PARTIES AND DEAL STRUCTURES

Issuers – typical profile
How would you describe the types of companies, and their different stages of development, that typically receive venture capital investment in your jurisdiction?

In recent years, the life sciences and ICT sectors have received the bulk of the venture capital investments in Switzerland. The strength of the life sciences, pharma, and biotech sectors particularly stems from the strong footprint of the global industry leaders Roche and Novartis in the Basel area as well as the research capabilities and spin-offs of Swiss universities. The same goes for the Swiss ICT sector, which has grown substantially together with the increasing presence of global tech leaders, especially in the Zurich area, alongside a push in tech research at Swiss universities (eg, through the ETH AI Center or the EPFL Innovation Park in Lausanne, one of the six sites of Switzerland Innovation). Other prominent industries for start-up investments include fintech, blockchain (with a particular hub in the canton of Zug), consumer products and clean tech ventures.

Whereas seed stage start-ups often receive funds or similar support from angel investors, high net-worth individuals, accelerators, incubators or educational institutions, institutional investors typically enter the stage in series A rounds. For later stage ventures, the focus usually further shifts to institutional investors such as corporate venture capital investors, venture capital funds and private equity investors.

Issuers – domicile and company structures

Are there any preferred or required legal domicile or company structures for issuers in venture capital transactions?

Issuers in Swiss venture capital transactions are usually incorporated as a Swiss corporation (*Aktiengesellschaft*). Although there are alternatives such as the limited liability company (*GmbH*), the Swiss corporation is usually the favoured legal form as it provides the most flexibility for financing rounds and typical arrangements to foster the growth of the company (such as the introduction of an employee stock option plan). Swiss companies limited by shares need a minimal share capital of 100,000 Swiss francs, of which at least 50,000 Swiss francs must be paid-in at the time of the company's incorporation. Financing rounds in Switzerland are typically structured by way of an ordinary capital increase. However, through the so-called capital band that may be introduced in the articles of association, it is also possible to grant the board of directors the competence to issue new shares and raise capital on its own within certain limits set forth in statutory law.

Issuers may freely choose a Swiss canton to incorporate their company. The choice of the respective Swiss canton has some tax implications due to different tax rates on cantonal and municipal level. However, the main driver for the choice of the legal domicile within Switzerland appears to be the relevant pool of talent and the growth opportunities. Hence, the two cantons with the largest financing rounds in 2022 were Zurich and Vaud, the home cantons of the two federal universities ETH and EPFL with a deep pool of talent and dedicated spin-off opportunities for promising ventures. The Basel region is a preferred choice for biotech, medtech and digital health companies, which benefit from the vibrant life sciences ecosystem there and the talent pool of companies like Roche, Novartis, Lonza and Johnson & Johnson (formerly Actelion).

Investors – typical profile

How would you describe the types of investors that make venture capital investments, including by stage of company development, in your jurisdiction?

In Switzerland, early-stage funding for start-ups is often provided by private investors and high net-worth individuals (such as business angels, entrepreneurs with a successful exit in the past, and industry experts), whereas venture capital funds regularly join the ranks in series A rounds and later stage financing. Additional early-stage funding may be provided by institutions linked to universities in Switzerland, certain government institutions as well as certain Swiss banks (in particular cantonal banks). Due to the relatively low boundaries to access the Swiss financial markets, a wide range of domestic and foreign investors, including dedicated venture capital funds, family offices, private investors and corporate venture capital investors are active in the Swiss venture capital space.

As a rule, early-stage investments are mainly provided by domestic investors (such as high net-worth individuals and certain Swiss venture capital funds), with a limited number of European seed funds regularly investing in Swiss start-ups. Foreign investors and especially foreign venture capital funds typically become more active in subsequent financing rounds. Foreign investors often constitute the main contributors of funds in large later stage transactions (ie, rounds with proceeds above approximately 20 million Swiss francs).

Investors – structures

How are venture capital investors usually structured and does their structure affect their investment approach or terms?

Swiss venture capital funds typically invest through dedicated fund entities that are often domiciled abroad (eg, in Luxembourg, Delaware, Jersey, the Cayman Islands or Guernsey). There are also Swiss structures available to venture capital funds, which may be used under certain conditions but are generally less common in practice. A few Swiss venture capital funds also use an evergreen fund model. The investments of Swiss venture capital funds are usually managed by a Swiss based management company, often in the legal form of a Swiss corporation (***Aktiengesellschaft***). Swiss managed venture capital funds typically have a life span of up to ten years. Their structure does usually not materially affect their investment approach or terms. Corporate venture capital investors, on the other hand, usually invest through legal entities that are part of their regular group structure.

Seed financings

What structures and types of investments are typically used for seed-stage investments in your jurisdiction?

Investors in Swiss seed-stage start-ups may invest directly in equity or shares issued by the company by way of a capital increase. However, as the process of issuing shares in Switzerland is rather formal (requiring, as a rule, the cooperation of existing shareholders, notarised resolutions and commercial register filings) and issued shares may not be cancelled or resold to the company easily or without adverse tax consequences, seed-stage investments are increasingly made by way of convertible loans. With convertible loans, the issuing company may access the funds of the investor more quickly and with less paperwork, which often makes them a suitable tool for investments in pre-seed and seed-stage start-ups.

The respective convertible loan agreements typically provide for a conversion at a discount (and sometimes with a valuation cap) in the course of the subsequent financing round of the company. Important aspects to be kept in mind when setting up such convertible or hybrid financing instruments include:

- Swiss law disclosure requirements in the course of a capital increase by way of a set-off of claims;
- applicable limits for loan counterparties under the Swiss banking act and tax laws; and
- the subordination of the claims for repayment of the loan to prevent insolvency risks of the issuer.

Capital or mentorship (or both) to seed-stage start-ups in Switzerland may also be provided through dedicated start-up incubators and accelerators as well as Swiss universities that offer support for their respective spin-offs.

Early-stage and later investments

What structures and types of investments are typically used for early-stage and later investments, following seed-stage investments, in your jurisdiction?

Early-stage and later venture capital investments are usually structured by way of an issuance of new shares in the course of a capital increase. Such transactions typically entail the negotiation and execution of an investment agreement and a shareholders' agreement among the existing and the new investors. These documents provide for the terms and conditions of the investment, the general governance rules of the company and the respective rights and duties of the investors and other shareholders, including rules on share transfers and the exit. In particular and in line with their investment strategy, venture capital funds typically require a board seat in the start-up; qualified majority requirements at board and shareholder levels; and certain liquidation or dividend preferences (or both) linked to shares issued to them in the course of the financing round as well as anti-dilution protection.

Convertible loans are regularly provided to early-stage start-ups but less commonly used for later investments, although they might still be used for short term and bridge financing before a subsequent comprehensive financing round can be completed. Typically, regular bank loans are not available to Swiss start-ups insofar as they do not have positive cash flows or suitable assets (or both) to provide collateral. However, some Swiss banks (mainly cantonal banks) offer equity financing and convertible loans through dedicated venture arms. Finally, venture debt has become more popular in the recent past in Switzerland. Such venture debt, which often includes a small equity kicker, may be provided in connection with or shorty after an equity financing round to start-ups with a solid track record in funding.

PROCESS

Term sheets

Do parties normally use term sheets? If so, what is normally covered in such term sheets?

Parties will frequently negotiate and execute term sheets prior to entering into the negotiations on final documentation. Term sheets generally cover all the main economic terms and main legal considerations, including:

- investment amount;
- valuation;
- conditions to closing;
- use of proceeds;
- (sales and liquidation) preference rights;
- governance rights (including board representation);
- information rights;
- anti-dilution protection;
- employee stock option plans;
- transfer restrictions (including drag-along, tag-along, right of first refusal and call options);
- non-competition and non-solicitation undertakings;
- representations and warranties;
- exclusivity, confidentiality;
- fees and expenses; and
- governing law and jurisdiction.

In general, only the provisions on exclusivity, confidentiality, expenses, governing law and jurisdiction are binding, whereas all other sections are non-binding.

Documentation

What are the standard documents for a venture capital transaction, and who prepares them? Are there popular forms for such documentation in your jurisdiction?

Negotiations for a venture capital transaction typically begin with the signature of a non-disclosure agreement, followed by a non-binding term sheet outlining the main terms. Both documents are frequently based on the investor templates. The details of the investment part of the transaction are then set out in an investment agreement and in a shareholders' agreement. Rarely, for smaller transactions, the investment agreement is replaced by a binding term sheet or a mere subscription form (or both).

The investment agreement specifies the terms and conditions of the investors' obligation to subscribe for, and the portfolio company's obligation to issue, the shares and provides, among other provisions, for a set of representations and warranties in favor of the investors. The shareholders' agreement covers the preference rights of the new shares being issued, governance matters such as board composition and control rights, information rights, transfer restrictions (right of first refusal, tag-along, drag-along and call options), anti-dilution protection, distribution of exit proceeds and similar matters. The portfolio company's legal counsel often prepares the first draft of the shareholders' agreement and the investment agreement, but occasionally the investor's legal counsel will provide the first drafts. The model documentation of the Swiss Private Equity & Corporate Finance Association SECA provides a good outline of the terms typically included and often serves as a baseline for discussions.

Key steps and timing

What is the normal process and timing of venture capital investments in your jurisdiction?

The process for a venture capital investment typically begins with the target company providing a non-confidential slide deck or company outline to the potential investor. In case of mutual interest, the next step is a confidentiality or non-disclosure agreement and the sharing of more sensitive and detailed information about the target company. At this stage, the target company will often provide access to a virtual data room in order for the investor to conduct its due diligence review, usually once a term sheet has been negotiated. In parallel (if the initial investor does not wish to provide the full funding amount for the round) the target company may search for additional investors to complete the investor syndicate. Negotiations on the definitive agreements are often conducted in parallel to the due diligence process. The whole process from start to finish takes around three to nine months.

Closing conditions

What closing conditions are common in venture capital transactions?

Closing conditions typically include the following:

- operation of the target company's business in the ordinary course of business and in accordance with past practice;
- absence of a material adverse change with regard to the target company;
- representations and warranties being correct in all material respects;
- approval of the existing shareholders of the transaction, including waiver of subscription rights and signatures of at least a large majority of existing shareholders on the investment and shareholders' agreements;
- no action being pending or threatened seeking to block the transaction; and
- availability of the documents required for closing, including the subscription forms of investors and the bank confirmation regarding the availability of funds of the investors.

Multiple closings
Are venture capital transactions ever divided into multiple closings? If so, how and why?

For larger financing rounds, it is common for the investment to be divided into several tranches of which only the first is paid out at the initial closing. Subsequent tranches are typically paid out only upon achievement of pre-defined milestones. This split into tranches serves to reduce investors' risk. Occasionally, the investment documentation will also foresee a second 'gobble-up' closing occurring a few months after the initial closing. This may be the case if the target company is unable to close the full round it was aiming for or if it is in ongoing negotiations with an investor who joined the process only at a later stage.

DUE DILIGENCE

Legal due diligence
What legal due diligence is typically undertaken for venture capital transactions, and what specialists are typically involved?

Venture capital funds (or other professional investors such as corporate venture capital investors) generally perform a rigorous pre-screening of potential targets before entering formal due diligence, evaluating in particular the business plan, the founder team, and the target's compatibility with the investor's investment strategy. This is followed by actual legal due diligence, typically covering the following areas:

- corporate;
- commercial agreements;
- financing;
- intellectual property and information technology, (IP/IT);
- regulatory (including data privacy);
- employment; and
- real estate.

Sometimes, the process is split into a first high-level review and (if satisfactory) a more thorough investigation. A more in-depth legal due diligence is normally conducted in later stage financing rounds.

Typically, in the legal due diligence, corporate lawyers work alongside specialist legal counsel from areas such as IP/IT, regulatory or employment.

Critical due diligence areas
What are normally critical areas of due diligence focus or red flags in venture capital transactions?

Critical areas in legal due diligence typically include matters related to the capital structure (eg, share capital, participation plans and convertible loans), engagement of key personnel, a sound financial position post-closing to achieve the next stage of development (including absence of hidden liabilities or litigation), and full ownership and protection of key intellectual property rights and know-how. Depending on the sector, material contracts such as licence agreements; collaborations with industry partners or academic institutions; and relationships with key suppliers and customers will also be areas of particular focus.

Common red flags include:

- a lack of clear IP assignment to the target company by founders, consultants or freelancers (eg, those engaged also at universities or by external service providers such as software developers);
- potential infringements of intellectual property rights;
- inconsistencies in share or option issuances;
- unstable or unfavourable relationships with key suppliers or customers; or
- disputes with current or former employees and shareholders.

Other due diligence
What other types of due diligence are commonly undertaken in venture capital transactions?

Other types of due diligence typically cover the following areas: Financial, business, technology, science, regulatory, tax, IP and (if relevant) environmental matters. Sometimes the process is split into a first high-level review and (if satisfactory) a more thorough investigation.

ECONOMIC TERMS

Valuation and pricing
How is the company valuation and investors’ purchase price usually determined in venture capital transactions?

Since the majority of targets of venture capital funding are unprofitable (and possibly even without revenue in case of early-stage funding rounds), many of the classical valuation methods (eg, earnings before interest, taxes, depreciation and amortisation or revenue multiple, dividend yield) are not useful.

Venture capital investors will therefore typically base their valuation on an assessment of the target's potential. This may include the size of the addressable market, the time to market, the target's position in such market, barriers to entry for competitors and the expected growth trajectory. Comparable transactions may also be considered and the ability of the target's team to deliver on the strategy is often a relevant soft factor. Furthermore, venture capital investors will also factor-in the future funding requirements in later stage financing rounds and determine the valuation in a range that allows them to achieve their desired multiple as return on investment in a successful exit.

The target's founders and management generally also base their valuation on the target's potential and comparable transactions but will often take into account the work and resources they have invested into the business as well as the level of dilution they expect through the venture capital transaction.

The purchase price is the result of negotiations between these two approaches.

Option pool

What do investors typically require for option pools or equity incentive arrangements in connection with venture capital transactions?

Venture capital investors have to strike a balance between adequately incentivising the portfolio company's management team and their own dilution.

For this purpose, they will generally (1) insist on setting a percentage target in the shareholders' agreement for the option pool, often in the range of 8–15 per cent of the portfolio company's fully diluted share capital, and (2) insist on the adoption by the portfolio company of a formal employee incentive plan (to the extent not yet in place). In general, they are agnostic on the type of incentive plan (eg, share plan, option plan or phantom stock plan).

The percentage of the option pool is usually in the lower part of the aforementioned range for pre-seed and smaller seed financings, where the C-level management still has a high percentage of founder shares, and in the higher part of such range in later stage financings, in particular when non-founders assume important C-level roles.

Dividends, distributions and redemptions

What are the normal provisions governing dividends, distributions, redemptions or other profit distributions in venture capital transactions? Are there any legal limits thereon in your jurisdiction?

Under Swiss law, as a rule, dividends may be paid only from the disposable profit and from reserves formed for this purpose.

Most venture capital investors in Switzerland seek to capitalise on their investment through a sale of their shares in the portfolio company (eg, in a trade sale or initial public offering) rather than dividends. As such, it is common for the shareholders' agreement to specify that dividend payments are not planned and that profits should be reinvested in the business.

In the event dividends are paid out, the shareholders' agreement will generally require these to be paid first to satisfy the venture capital investors' preference rights.

As a rule, a redemption of shares is only permissible within certain limitations set forth by Swiss (corporate) law.

Company sales and liquidations

How are venture capital investments treated in portfolio company sales or liquidations?

Venture capital investors typically demand (and receive) the inclusion of a liquidation preference in the shareholders' agreement and the articles of association of the portfolio company. This ensures that in case of a sale or liquidation of the portfolio company, such investors get at least the amount invested returned to them ahead of other shareholders. There are substantial variations in the terms of liquidation preferences seen in venture capital transactions in Switzerland (eg, participating versus non-participating preferences, size of multiplication factor (return on invested capital), inclusion of non-cumulative or cumulative (ie, hypothetical) dividends and catch-up mechanics) and this is often one of the key items in negotiations.

Anti-dilution protection
What anti-dilution protections are typically built into the terms of venture capital securities?

Under Swiss law, each shareholder has in principle a right to participate in future equity financing rounds in order to maintain its pro rata ownership. This right is sometimes expanded in the shareholders' agreement or the articles of association (or both) to enable venture capital investors to subscribe shares above their pro rata amount, for example to the extent other shareholders do not participate in a financing round.

In addition, venture capital investors typically demand the inclusion of an anti-dilution adjustment clause in the shareholders' agreement, enabling them to subscribe additional shares at a lower issue price in case the portfolio company issues shares at a lower price per share than the one paid by investors (down round). Most commonly seen are anti-dilution formulas based on a weighted average price, either broad based weighted average or (more rarely) narrow based weighted average. Full ratchet anti-dilution provisions are very rare in practice.

In some instances, investors in a previous round will lose their anti-dilution rights in a subsequent round. This may be a negotiation item between investors participating in different rounds.

Future investments
What pre-emptive or pro rata investment rights do venture capital investors usually receive?

Under Swiss law, each shareholder has in principle a pre-emptive right to subscribe shares in future equity financing rounds in order to maintain its pro rata ownership in the portfolio company. This right can be withdrawn for important reasons by a supermajority vote at the shareholder meeting. Acquiring new companies and issuing shares for employee incentive programs are recognised as important reasons. The bar for other reasons to qualify as important is generally high and needs a detailed analysis of case law.

However, in practice, the shareholders' agreement often expands pre-emptive rights and enables venture capital investors (or sometimes all shareholders) to subscribe shares above their pro rata amount to the extent other shareholders do not participate in a funding round.

Insider sales
What rights do venture capital investors normally have over insider sales of securities of portfolio companies?

The shareholders' agreement will typically include a right of first refusal for the event that a shareholder wishes to sell its shares in the portfolio company (outside of specific permitted transfers). In most cases, venture capital investors will come at first or second place (after the portfolio company itself) to exercise this right of first refusal, followed by the other shareholders.

In addition, most shareholders' agreements will contain a tag-along provision, allowing venture capital investors (and possibly other shareholders) to co-sell a part of their shares in case of a proposed share sale. This tag-along right usually kicks in at a relatively low level (eg, if more than 1–5 per cent of the shares in the portfolio company are sold) but may also be limited to change of control events.

CONTROL RIGHTS

Voting rights
What voting rights, including veto or consent rights, do venture capital investors normally have as shareholders of their portfolio companies? Do they typically have special voting or consent rights as shareholders?

Venture capital investors as shareholders of the portfolio company will have the usual voting rights in their capacity as shareholders. While venture capital investors typically receive preferred shares, such preferences refer only to financial aspects and do not include preferred voting rights.

However, venture capital investors will typically demand extensive consent rights to be included in the shareholders' agreement (and possibly the portfolio company's articles of association and organisational or board regulations). Such consent rights usually cover both decisions at the shareholder level and the board level. At the board level, the consent of a certain number of board members appointed by venture capital investors will be required. Areas typically covered by the consent rights at shareholders level include certain changes to the articles of association (eg, amendments being detrimental to the investors), certain changes to the share capital, creation of new classes of preferred shares, exclusion of pre-emptive subscription rights or ceasing to do business. Consent rights at board level include for instance transferring material assets, material changes to the business plan, approving the budget and materially deviating from it, entering into agreements with major financial impacts, as well as approving employee incentive plans and the hiring and compensation of C-level managers.

Board rights
What rights to representation on the board of directors or at meetings of the board of directors of portfolio companies do venture capital investors typically receive?

Venture capital investors holding a significant share of a portfolio company will often secure the right to nominate a member of the board of directors.

Many venture capital investors also seek to appoint a board observer, either in addition to a board member or to make up for the lack thereof. Board observers may attend board meetings but have no voting rights.

Both portfolio companies and venture capital investors have an interest in keeping the board size reasonably small and manageable. Therefore, investors may lose their board seats in a later financing round, in particular if they do not invest up to their full pro-rata participation.

Board protections

What fiduciary duties and liability protections normally apply to investor directors in your jurisdiction? Do directors typically have special voting or consent rights?

Under Swiss law, all board members (including investor directors) have a fiduciary duty to the portfolio company and a duty to act in its best interest. This supersedes a potential duty of loyalty to the venture capital investor to which they report.

The board of directors has certain non-transferable duties as set out in the Swiss Code of Obligations but will otherwise at least partially delegate day-to-day management of the portfolio company to individual board members or an executive management. The board of directors is obliged to carefully select, instruct and supervise the persons to whom it delegates authority.

Board members are liable to the portfolio company, its shareholders and (in case of a bankruptcy) its creditors for damages arising from a breach of their fiduciary duties.

Most venture capital investors demand that portfolio companies put in place directors' and officers' liability insurance to cover damages caused by negligent acts and omissions of investor directors. In addition, some venture capital investors demand indemnification letters from the portfolio company to the benefit of their investor director. However, whether and to which extent such indemnification letters are enforceable under Swiss law is a matter of controversy.

Each board member has one vote, with the chairperson having a casting vote in case of a tie if so foreseen in the articles of association. For certain important board decisions, venture capital investors typically demand an increased quorum to ensure that such decisions cannot be taken without their consent. A list of these decisions is typically included in the shareholders' agreement and possibly the organisational or board regulations.

Financial reports

What rights to financial reporting or company access do venture capital investors normally receive?

Venture capital investors with a significant investment in the portfolio company typically receive a suite of financial reports from the portfolio company, including annual financial statements, quarterly financial reports and financial statements, management reports and a budget for the next financial year. In addition, they may have the right to demand access to the portfolio company's management or records (or both) upon reasonable advance notice as well as (occasionally) the right to appoint an independent auditor. The frequency of reports is a matter of negotiation and increases with the maturity of the start-up.

PUBLIC OFFERINGS AND LISTINGS

Securities law requirements
What are the securities law requirements in your jurisdiction for venture capital investors to sell their securities in the public markets?

Whether venture capital investors are allowed to sell their shares in Swiss portfolio companies in the public markets mainly depends on the listing status of the company. In the Swiss venture capital context, the shareholders' agreement usually governs share sales in public markets before the company completed an initial public offering (IPO). Post-IPO, the shares in Swiss portfolio companies may typically be sold freely after a certain lock-up period expired. Public offerings of securities and the listing of securities on a stock exchange in Switzerland usually require the publication of a prospectus, if no statutory exemption applies. The main stock exchange in Switzerland is the SIX Swiss Exchange which has a designated market segment for small and medium-sized enterprises called Sparks.

Registration and listing rights
What registration rights, listing rights or other rights do venture capital investors normally receive?

In the Swiss venture capital context, the relevant shareholders' agreement regularly stipulates that there will be no public market and no registration or listing rights for the issued shares prior to an IPO of the company's shares on a Swiss or foreign stock exchange. Many US investors insist on registration rights substantially similar to the registration rights in the National Venture Capital Association investors' right agreement. These are generally included in the shareholders' agreement in a slightly condensed form.

Other resale rights
What other resale rights in the public markets do venture capital investors usually receive?

Outside a public listing or IPO of shares in Swiss portfolio companies, venture capital investors in Switzerland do typically not receive resale rights in the public markets. However, typical shareholders' agreements in the Swiss venture capital context often contain clauses to facilitate an IPO, such as regarding listing approval, lock-up agreements and conversion of preferred shares into one class of common shares for the purposes of a public listing.

COMPANY SALES (M&A)

Standard sale structures

What are the standard structures or methods for venture capital portfolio companies to be sold in your jurisdiction?

Venture capital portfolio companies are usually sold through a share deal (ie, the sale of all or the majority of the shares in the company). A share deal is also typically favoured by the founders, as such transaction, under certain conditions, allows them to realise a tax-free capital gain. Although this makes it more difficult for venture capital funds to return their limited partners' investments in a timely manner, the consideration to be paid in these share deals is often divided between upfront, milestones and earn-out elements (eg, sales milestones, royalties).

In a distressed scenario, certain or all of the assets of a venture capital portfolio company may also be sold by way of an asset transfer shortly before or in the course of the company's liquidation.

Role of investors

What is the role of venture capital investors in a portfolio company sale? Do they have rights to force or block a company sale?

The detailed terms and conditions, under which a party may force other parties to join a trade sale or on the other hand block such a sale, are typically set forth in the shareholders' agreement. The contractual documentation governing Swiss venture capital portfolio companies usually contains a quite extensive set of restrictions on the transfers of shares. These can include general transfer restrictions for a certain period of time for some investors (lock-up), rights of first refusal and call options in case of certain triggering events. In addition, minority investors such as venture capital investors are usually granted a tag-along right in case of sale of a significant stake in the company. On the other side, the documentation often includes drag-along rights in case of certain qualified transactions, such as a change of control event. Typically, venture capital investors can neither force nor block a company sale on their own. This may be different in case the drag along right is only triggered upon reaching a certain minimum exit valuation; in such case, the venture capital investor may block a company sale.

Post-closing protections

What post-closing matters or protections do venture capital investors typically obtain, for example to address ongoing company sale indemnities or director tail liabilities?

Representations and warranties provided by venture capital investors in exit transactions of Swiss portfolio companies are often limited to fundamental representations (mainly title and capacity) without the inclusion of business representations. Also, venture capital investors are usually not willing to enter into restrictive post-closing covenants such as non-compete or non-solicitation obligations. Another important feature for venture capital investors is to limit their liability to the escrow amount and possible future earn-out payments, which allows them to return the investment to their limited partners. Finally, warranty and indemnity insurances are also becoming more common in sales of venture capital portfolio companies, frequently at the request of the selling venture capital funds.

In the context of a company sale, the directors are usually granted discharge for their time as members of the board of directors of the company, which limits their potential liability to a certain extent. In addition, buyers of a Swiss venture capital portfolio company in the share purchase agreement often forego (to some extent) their right to sue members of the company's management and the board of directors for their activities prior to completion of the transaction. Obtaining a 12 to 36-month tail coverage under the directors' and officers' liability insurance is sometimes set forth in the board member agreements between the portfolio company and the board member.

LEGAL AND REGULATORY CONSIDERATIONS

Disputes

What types of disputes typically arise in venture capital transactions and how are disputes commonly handled? What provisions normally govern disputes, including choice of governing law, choice of forum and alternative dispute resolution mechanisms?

Disputes regarding venture capital investments in Switzerland may be triggered by different circumstances. There may arise discussions about potential breaches of covenants or representations and warranties under the investment agreement. Furthermore, there may be different views regarding certain rights and obligations under the shareholders agreement (eg, with respect to minority rights, share transfer restrictions or anti-dilution protection).

Disputes among investors, founders or the portfolio company (or both) should ideally be resolved outside of formal court or arbitration proceedings by way of a mutual agreement, as it is usually in neither party's financial interest to invest time and money (which are needed for growing the company) into litigation or arbitration proceedings. The relevant documentation, particularly the investment agreement and the shareholders' agreement, are typically governed by Swiss law and disputes are referred either to Swiss state courts or an arbitration tribunal with seat in Switzerland. Such jurisdiction clauses may also contain a requirement to engage in an alternative dispute resolution mechanism such as compulsory mediation prior to the filling of a claim with a state court or arbitral tribunal.

Regulatory consents and filings

What regulatory consents, notifications and filings are required for all investors in venture capital transactions in your jurisdiction? Are there ownership restrictions?

As a rule, venture capital transactions in Switzerland do not trigger regulatory consent, notification and filing requirements, safe for very large transactions that could trigger merger control notification thresholds and transactions in regulated industries such as banking or insurance. As of today, Switzerland does not have a dedicated regulation to restrict foreign direct investment. However, a respective legislative project is pending. Finally, Swiss corporate law stipulates notification requirements by investors towards the portfolio company (ie, not towards the public) regarding the beneficial ownership of shares in the event of the acquisition of shares above a certain threshold.

Foreign investment
What foreign investment restrictions and other domestic regulatory issues arise for venture capital investors based outside your jurisdiction?

To date, Switzerland does not have dedicated rules to restrict foreign investment (apart from specific restrictions for the acquisition of certain real estate by foreigners). However, a legislative project regarding the restriction of some type of foreign investments is currently pending. As of now, this proposal only focuses on majority acquisitions by foreign state-controlled investors in specific security-critical sectors. Based on these contemplated rules, such regulation, even if adopted, should not materially impact typical venture capital transactions with participation of foreign investors.

UPDATE AND TRENDS

Key developments
What are the most noteworthy current trends and recent developments in venture capital transactions in your jurisdiction? What developments are expected in the coming year?

On 1 January 2023, the revised Swiss corporate law entered into force, which aims at modernising the corporate governance of Swiss companies, including by way of introduction of certain electronic means for shareholders and board resolutions and facilitating the funding of Swiss companies through the newly introduced capital band (ie, an authorisation of the board of directors by the shareholders to adapt the company's capital within certain statutory limits). Ongoing legislative projects include a regulation on foreign direct investment, which should, however, not materially impact typical venture capital transactions for foreign investors.