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The protected cell company

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At the beginning of 2015 Liechtenstein company law is to be expanded with the introduction of the *segmentierte Verbandsperson* or protected cell company (PCC), also known as the segregated portfolio company (SPC). This means that, when structuring their assets, economic actors will in future have recourse to a legal entity which gives enhanced flexibility and legal certainty with regard to the distribution of liability. The PCC is not so much a new legal entity as rather a legal arrangement that allows additional organisational structures within existing legal entities.

The possibility of segregating legal entities is not an entirely new departure for Liechtenstein, since it is already envisaged by the existing statutory provisions, e.g. of the Investment Undertakings Act *(Investmentunternehmensgesetz)*. Current law also allows for asset segregation through the formation of multiple legal (sub-) entities, trusts or trust companies with compartments that are dedicated to certain types of business.

Legal entities which are either required by law or choose voluntarily to be entered in the commercial register and which exclusively pursue one or more of the following purposes may be set up as PCCs (hence the foundation *[Stiftung]* is included):

1) charitable or public utility purposes within the meaning of Art. 107 para. 4a CPCL (Liechtenstein Code of Personal and Company Law, *Personen- und Gesellschaftsrecht, PGR)*;
2) the acquisition, administration and realisation of holdings in other companies (subsidiaries);
3) the commercial realisation of copyrights, patents, trademarks, models or patterns;
4) deposit guarantee and investor protection systems that implement the applicable EEA regulations.

In this article we are mainly interested in the use of the PCC as holding company.

It is already customary practice for companies to be structured as parent/subsidiary entities which pursue the same economic objectives, although this currently involves a great deal of administrative, bureaucratic and hence financial expenditure. In practice, moreover, combinations consisting of an umbrella foundation and multiple sub-foundations often carry statutory liability risks. The optimal, cost-effective way to achieve this structure is by means of a PCC.

Thus in many cases the PCC can fulfil the same purpose more elegantly and with less expenditure than the standard parent / subsidiary structure. Many other jurisdictions permit segregation in one form or other. In essence its purpose is to improve risk management, more specifically by spreading risks appropriately, cost-effectively and with maximum efficiency.

An important feature of the PCC is that, because it is a corporate structure formed by the combining of cells, it can acquire corporate substance and be endowed with the required volume of material assets (infrastructure, personnel, technical expertise) at a modest level of expenditure that is compatible with a small country of domicile. In certain jurisdictions at least this makes it possible to meet specific minimum asset volume requirements for affiliated companies. It is worth noting here that, in the case of Liechtenstein, generating corporate substance by arranging for specialist personnel to take up residence in the country – a practice that is relatively common and poses no particular problems in other countries – is subject to very tight restrictions. Accordingly, the introduction of the PCC solution into Liechtenstein company law is a sensible and proportionate adjustment which potentially counteracts the competitive disadvantage imposed by the Principality's restrictive policy on residence. At best, therefore, it may succeed in turning a distinct local disadvantage into a modest local advantage. Our assumption is that the proposed amendment to company law will achieve this objective.

A PCC consists of:
- a core or non-cellular part, and
- one or more separate cells.

A distinctive feature of the PCC is that the assets of the individual cells and the assets of the core are always kept separate from each other.

Individual asset portfolios (cells) can be assigned to a certain area of business, e.g. the management of assets for a specific charitable purpose. The area of business to which the cell is dedicated may also relate to the operation of a manufacturing firm, or the management of an occupational pension scheme, etc.

A PCC may have one or more cells. A PCC with only one cell may serve, among other things, as a way of hiving off the risks of a given area of business and / or concentrating them in an entity that is ring-fenced in terms of liability.

Both the core assets and the individual cells of the PCC constitute separate, mutually independent bodies of assets. The assets of a cell are attributable to that cell only and not to any other cell or to the PCC's core assets. This clear attribution of assets, either to a particular cell or to the core assets, forms the basis for their segregation into individual cells.

Because their assets are clearly segregated the individual cells of the PCC can conduct their business independently of one another. In so doing they may engage in certain activities which must be defined in detail in their articles of association or regulations. However, the areas of activity of the individual cells must not run counter to or conflict with the purpose of the PCC. Moreover, a cell's area of activity must not conflict with that of another cell.

Although the individual cells operating in their particular areas are treated as if they were independent companies, they do not have the status of separate legal entities. Only the PCC counts as a separate legal entity.

The articles of association of a PCC must without fail state that the entity is a protected cell company. The articles of association must also set out provisions governing the PCC's organisation and representation.

In addition, the articles of association must designate the individual cells by name and describe the areas of activity they are to pursue.

Alternatively, the cells may be designated and the areas of activity they pursue may be described in the regulations enacted on the basis of the articles of association. In this case the PCC's articles of association must contain an indication that this information can be found in the regulations enacted on the basis of the articles of association.

When setting up a PCC there is thus a choice as to whether the details of the segregation are set out in the articles of association or in the regulations. This makes it possible to avoid the major financial and administrative expenditure that repeated amendments of the articles of association would entail, especially for PCCs which administer a large number of (smaller) asset portfolios.

Despite this freedom of choice, creditors cannot be disadvantaged. In every contact constituting a legal transaction with third parties, those parties must be informed that the entity is a PCC and also which cell is liable for the legal relationship concerned.

Where advantage is taken of the option of designating the cells and describing their areas of activity in the regulations, those regulations must be submitted to the Office for Justice when the application is made for entry in the Commercial Register. However, the regulations do not have to be lodged with the Office for Justice.

The articles of association of the PCC generally determine how the PCC is to be organised and represented. They must without fail comply with the provisions governing the organisation of the relevant legal form (e.g. public limited company *[Aktiengesellschaft]*, private limited company *[GmbH]*, establishment *[Anstalt]*, foundation *[Stiftung]*). Thus the provisions set out in the articles of association governing how PCCs are to be represented and administered will vary according to the legal form adopted.

Because they do not constitute legal entities the individual cells lack governing officers of their own. Likewise it is not possible to confer signing authority in respect of one particular cell only or for certain cells and not others. This means the individual cells will be represented externally exclusively by those authorised to represent the PCC. Thus the individual cells are able to act only through the PCC and / or the officers authorised to represent the PCC. Hence all external dealings are conducted exclusively by the PCC, which in the process must state that it is acting for a particular cell. Internally, by contrast, the individual cells may be given their own business management units to which responsibilities are assigned accordingly.

Because the individual cells do not in themselves constitute legal entities, the governing officers of the PCC bear responsibility and liability in accordance with the general provisions of company law.

The minimum capital is already covered by the core of the PCC. This ensures that a PCC cannot be established without complying with the rules on minimum capital.

For each individual cell a legal reserve must be formed in an amount equal to the minimum capital prescribed for the legal entity concerned. The purpose of this obligation is to ensure that the creditors of a particular cell are not disadvantaged by the fact that, as a general rule, any claims accruing to them may only be asserted against the assets of that cell. This is achieved by ensuring that the cell assets available to creditors for coverage of their damages are at least equal in amount to the statutory minimum capital envisaged for the PCC. Moreover, creditors of a particular cell are better placed than creditors of the core PCC insofar as each cell is required to form a legal reserve equal in amount to the minimum capital requirement.

With regard to contractual and non-contractual liability claims it should be noted that, unlike contractual claims, non-contractual third-party claims (e.g. claims arising in tort) may only have recourse to the core assets. However, if the core assets are not sufficient to satisfy such a claim, subsidiary recourse may be had to the assets of the cell in whose area of activity the PCC gave rise to the claim. For the creditor to assert the claim the PCC management must furnish him / her with the requisite information. To make enforcement of the claim possible, if the management fails to supply the required information, an application may be made for a court order instructing the management to provide that information as well as all documentation necessary to bring the claim.

Overview of a PCC in practice

In practice a PCC might look like this:

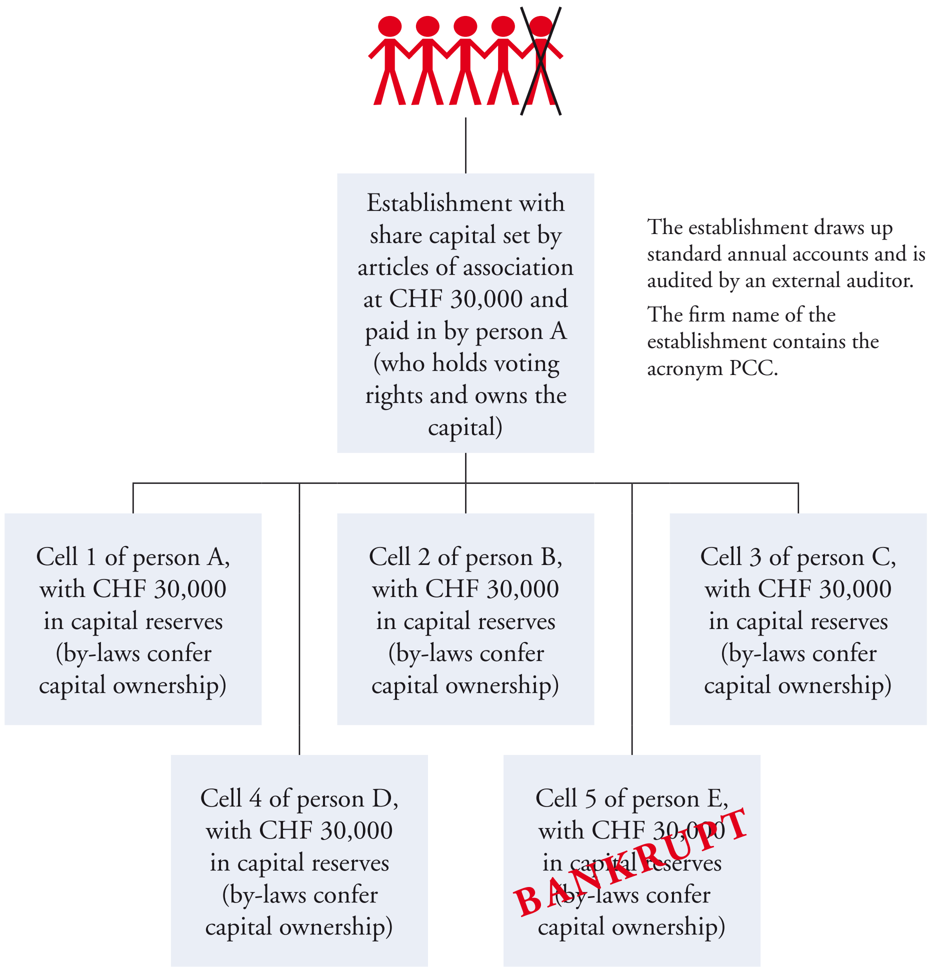
1) Person A sets up an establishment *(Anstalt)* with five holding cells.
2) The share capital of the core is CHF 30,000.
3) Person A makes a capital contribution to cell 1 and four business partners make their capital contributions to cells 2 – 5. Five capital reserves of CHF 30,000 each are deposited.
4) Because the equity participations are held via cells, the partners are not exposed to the risk that any insolvency, default, etc., of one cell might affect the other cells.
5) Combining the equity participations into one legal entity gives the establishment a certain critical mass. A number of different participations are held, management meetings are necessary, and it may be worth renting business premises and recruiting an employee. In this way the entity acquires corporate substance.
6) Thanks to this formation of corporate substance the establishment can take advantage of the network of double taxation agreements.
7) The establishment pays ordinary income (corporation) tax at the rate of 12.5 %, with dividends and capital gains on shares always being tax-exempt. The establishment files only one tax return because the PCC is a company and the basic concept of unity is consistently applied.
8) The equity of the establishment is owned by person A. The investors in cells 2 – 5 are known as asset contributors and are at most the beneficial owners of those assets. Such beneficial ownership is stipulated in the cell's by-laws. A bank account is set up for each cell and in the process the identities of the asset contributors and, where applicable, beneficial owners are disclosed to the banks concerned. It remains to be seen whether the disclosure of any or all of this information would be necessary outside Liechtenstein. Person A remains the sole owner and shareholder of the legal entity.

Since the purpose of the PCC is limited to acting as a holding company, its holding activities do not come under the provisions of the Liechtenstein UCITSA governing investments in undertakings for collective investment in transferable securities, the provisions of the Liechtenstein IUA governing investment undertakings for other assets or real estate, the provisions of the Liechtenstein AIFMA governing investments in alternative investment funds or the provisions governing investments in comparable accumulation CIUs established in other national jurisdictions, regardless of the number of parties involved.

Free movement of capital and freedom of establishment

A Liechtenstein legal entity can take advantage of the free movement of capital and the freedom of establishment within the EEA providing it does actually engage in some form of economic activity. For this to apply the entity must have some form of physical presence (office, etc.) in the EEA at which a person conducts business by providing a service (management of group affiliates / holdings) against remuneration for an indefinite duration specifically through that fixed physical location. Such business is to be conducted at the entity's headquarters as defined in its articles of association or alternatively at its administrative head office, and depending on the size of the business concerned, an appropriate number of employees must be recruited. If the entity lacks an appropriate level of resources in terms of premises, personnel and equipment within the EEA, it probably will not count as providing an economic service. If the legal entity is involved in managing a group of companies or in other group activities (e.g. resource management) and if the way it is currently incorporated reflects those activities, there is a presumption of actual economic activity because a physical presence is thereby established within the EEA. In this way, a Liechtenstein legal entity can benefit from the free movement of capital and the freedom of establishment. Hence the corporate substance requirement can be fulfilled faster and more cost-effectively by means of a PCC.

Investors A-E (where investment E goes bankrupt)



The author of this article, Roger Frick, Allgemeines Treuunternehmen, will be pleased to provide you with further information.

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