

Update

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Bonus: Ex-Gratia Payment or Salary?

The Swiss Federal Supreme Court defines "*moderate*" and "*higher than average*" salaries and sets forth the criteria for the re-characterization of a bonus as salary.

Under Swiss employment law, the character of bonus payments is often unclear. Since the relevant statutory provisions offer little guidance, Swiss labor courts, in a number of precedent cases, have elaborated criteria to differentiate bonus payments that are meant to be entirely at the discretion of the employer from those that in fact constitute variable salary. In the past, labor courts have taken the view that notwithstanding the contractual wording of the provision stating that the bonus was at the absolute discretion of the employer, the employee may have a valid claim to receive a bonus if the bonus (i) was paid without any qualification about its discretionary nature for a period of at least three years, (ii) although subject to a qualification about its discretionary nature, the bonus was consistently paid for at least 10 consecutive years, or (iii) the bonus, compared to the base salary, makes up an important part of the overall remuneration and thus constitutes a compensation element which is no longer "*accessory*" to the base salary.

In respect of this last criterion regarding the *accessory nature* of a bonus, the Swiss Federal Supreme Court issued a ruling in August 2015 pursuant to which the compensation (including bonus) that exceeded 5 times the median Swiss salary of roughly CHF 70'000 (in 2015) is considered to be a "*high*" salary. In case of a "*high*" salary, any discretionary bonus payment was to be considered an *ex-gratia* payment. In

other words, if the compensation (including bonus) exceeds 5 times the median Swiss salary, *i.e.* the amount of about CHF 350'000, labor courts are not allowed to re-characterize a discretionary bonus as variable salary. In its decision, the Federal Supreme Court did not provide any guidance regarding the accessory nature of bonus payments for salaries that were lower than 5 times the median Swiss salary.

In a recent decision rendered on August 29, 2017, the Federal Supreme Court has now defined the rules that apply with respect to discretionary bonus payments for employees whose salary is below the threshold of 5 times the median salary. According to this recent ruling, a distinction is made between a "*moderate*" salary, which is deemed to be a salary of up to the Swiss median salary of today approximately CHF 70'000, and a "*higher than average*" salary which is within the bandwidth of between one time and five times the median salary. With respect to "*higher than average*" salaries, the ruling states that a discretionary bonus can potentially be re-characterized as salary only if and when the bonus is equal to or exceeds the annual base salary. Stated differently, any discretionary bonus that does not amount to or exceed the annual base salary is to be considered "*accessory*" and can therefore not be re-characterized as salary.

As for "*moderate salaries*", the Federal Supreme Court states that even a discretionary bonus which is lower than the annual base salary is amenable for re-characterization as salary.

The recent Supreme Court ruling will provide employers with a much higher level of certainty regarding the treatment of discretionary bonuses of employees who earn a "*higher than average*" base salary, since a re-characterization as salary will only be permissible if the bonus exceeds the amount of the annual base salary and is thus no longer considered to be accessory to the base salary. In this connection, it is important to note

that irrespective of the salary level a bonus labeled "*discretionary*" may still be treated as variable salary if its payout is linked to the achievement by the employer or the employee of certain targets that may be measured objectively, e.g. EBITA, net profit or sales goals, since the bonus in that case is in fact not subject to any discretion by the employer.

Please do not hesitate to contact us in case of any questions.

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