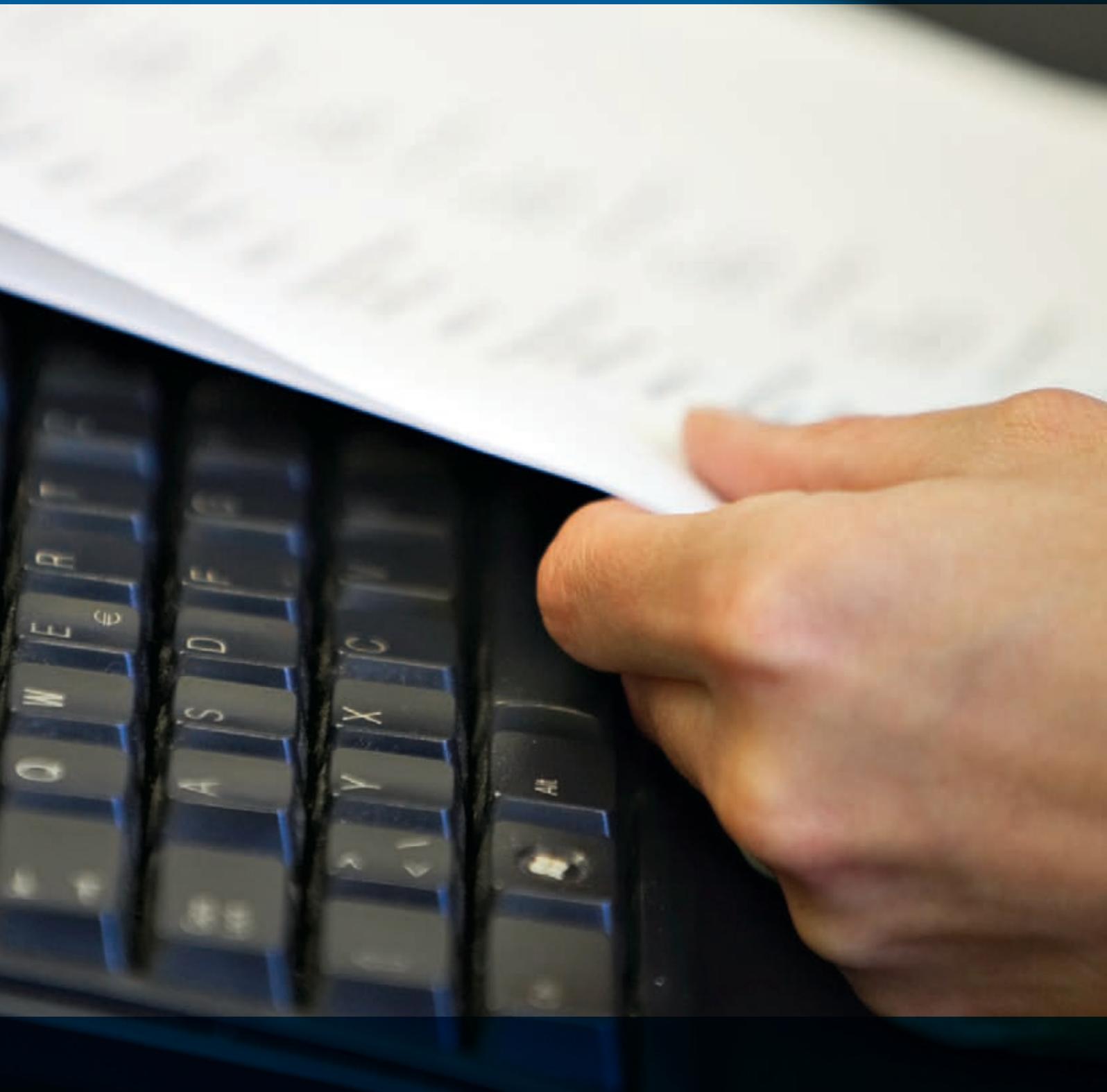




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Federal Audit Oversight Authority FAOA

Activity Report 2008



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1 Introduction

1.1 Foreword

«Trust is good – control is better». This expression, wrongly attributed to Lenin, is often used, to legitimise government regulatory agencies that are designed to ensure the transparency of financial markets and the solvency and honesty of those subject to oversight in the interests of investors and consumers. This calm before the storm is, however, deceptive. Despite the tightening-up of regulatory mechanisms in recent years, in 2008 a financial crisis that spread like wildfire rocked the business world on a scale that hardly anyone had thought possible or had even really foreseen. Did government regulatory authorities fail? Many people think that the answer to that question is «yes» and accuse the regulatory authorities of not being able to cope with the situation. The Federal Audit Oversight Authority, hereinafter referred to as the FAOA, will probably not be spared such accusations either.

However, not everything that precedes something that happens is necessarily its cause. Attributions of this kind are erroneous conclusions based on false logic, and what has long been common knowledge in philosophy may not necessarily be also the true for the field of economics. But the duties, activities and legal capabilities of auditors must also be seen and evaluated in the light of this perception. Legal reality, however, often reveals a different picture. It is well known that all the bodies representing a company are liable for any damages that they culpably cause in the exercise of their office. Hence the liability for failing to meet the appropriate level of responsibility applies not only to the Board of Directors and management but also to the auditors. Experience teaches us that it is not uncommon for the auditors to be sued as a matter of priority because the sum sought to cover the losses exceeds the financial resources of management. The last one has to carry the can, the prominent company law expert Professor Peter Forstmoser graphically complained, regretting that, viewed from this perspective, it is the former that bear the responsibility and the latter that suffer the consequences. But as a rule, it is first and foremost management that is responsible for corporate malpractice and secondly the non-executive Board members. Only a relatively low level of blame is generally attributable to the auditors: they are not responsible for the management of the company, but have merely to perform an audit and to issue their report. Due to their statutorily prescribed independence from the management, they act only after the event and can at best only pull the emergency brake

in order to limit the loss or damage, but are hardly ever able to prevent it occurring. Although this role is little more than that of the warning tail-light at the back of the business train, disappointed creditors prefer to see it as a headlamp mounted at the front of the responsibility locomotive and turned full on. In addition to which, under current law, where responsibility for one and the same loss or damage lies with a number of parties, the principle of joint and several liability applies. Regardless of how much he is to blame, anyone who contributes to the damage is therefore liable for the total loss, and his share of the liability is reduced only by way of recourse, and even then in many cases only legally but not financially, since, as that well-known saying has it, you can't get blood out of a stone. The Swiss Federal Council has duly acknowledged this paradox in the apportionment of blame and liability and, in its Message of December 21, 2007 to the National Council and Council of States, proposed limiting the company-law liability for negligence of the persons entrusted with auditing to the amount for which they would be liable according to recourse vis-à-vis third parties. If the provision becomes law, it will take due account of the principle that it is not the loss or damage that makes one liable for compensation, but the degree of blame, a principle which the great legal scholar Rudolf von Jhering expounded as far back as the 19th century.

Does an audit oversight authority become superfluous in these circumstances? Definitely not, since regulatory law, like law generally, has not only a repressive function but also, and more importantly, a preventive or control function. The requirements imposed on auditors were fundamentally redefined by the Company Law Amendment Act, which came into effect on January 1, 2008. On the one hand, some rules were relaxed, in that small and medium-sized enterprises (SMEs) are now subject merely to a limited audit requirement and very small enterprises are exempted from the mandatory audit requirement altogether. On the other hand, some rules were tightened up qualitatively, with not only the introduction of a licensing procedure for all individuals and firms that wish to provide ordinary or limited audit services but also particularly strict substantive state oversight of the auditors of public companies. This is intended to ensure that only experienced and well-trained auditors and audit experts audit accounts and compliance with accounting standards and that financially significant audits are regularly checked to ensure

compliance with the Act and that they have been performed professionally both from an organizational as quality standpoint. The requirements governing the independence of auditors from the companies they are auditing were also made more stringent. In the interests of shareholders and stakeholders, close connections between accounting and auditing are no longer tolerated. But all these rules risk rapidly becoming not worth the paper they are written on if compliance is not monitored regularly. This is the function of the Federal Audit Oversight Authority (FAOA).

In the year under review the FAOA further developed its operations in its three major areas of activity. The first manifested itself in the comprehensive examination of the licensing conditions for auditors, audit experts and audit firms for which only provisional authorizations had until then been granted and those for which licenses were being granted for the first time. The second concerns itself with the legal organization of supervisory activity and international coordination. Finally, the third is the substantive supervision of audit firms which audit public companies or have voluntarily subjected themselves to substantive state oversight. For the purpose of these inspections, the Authority examines both the organization of the audit firm with regard to fulfilment of its statutory duties (firm review) and also, on a random test basis, the audit services it provides (file review). Information on the individual activities is provided in the following chapters of this Annual Report.

The FAOA is well aware that its activities bring those under its supervision, in particular the auditors of public companies, not only pleasure and satisfaction but also ties up resources and brings additional cost. These consequences are, however, inseparably connected with the introduction of government oversight. They are also a prerequisite for the much sought-after broad international recognition of Swiss audit firms, and ultimately they are a means of reassuring those being supervised themselves. Where necessary, the attention of firms is drawn to omissions, carelessness and possible improvements that may ensure or even improve their reputation and the quality of their services. For its part, the FAOA seeks to keep within reasonable bounds the inconveniences it causes in terms of time and money for the audit firms it examines. In particular, it attempts to do this through optimal coordination of its activities with other regulatory agencies and painstaking planning and preparation of the individual inspections. So it was also with great pleasure that it learned of the laudatory comments in the «Schweizer Treuhänder», the industry's specialist journal, according to which «in a very short time a skilled regulatory authority [has] emerged which is making its mark with transparency, clarity and agreeably modest fees». The FAOA is keen to preserve and enhance this reputation in the future.

Berne, 13 March 2009



Hans Peter Walter
Chairman of the Board of Directors



Frank-Oliver Schneider
Executive Director

1.2 The FAOA in brief

In its first full business year since commencing operations on 1 September 2007, the FAOA was essentially faced with three core tasks: commencing the final evaluation of all individuals and firms which had initially been granted provisional licenses; preparing and commencing oversight and inspection activities; and stepping up the pace of negotiations with foreign counterpart regulators on mutual recognition.

Overcoming these challenges and commencing the FAOA's inspection activities in April 2008 required an increase in staff numbers from 14 full-time equivalent positions at the end of the previous year to 19.5 full-time equivalents, split between 23 employees, at December 31, 2008. A further four persons have also been hired on an hourly basis to assist in the reviews of state-regulated audit firms. These individuals are experienced auditors (ex-partners of «Big Four?» audit firms) who bring their many years' experience into the inspections. The number of persons employed by the FAOA is expected to reach its plan target in 2009 and will increase only slightly.

As a decentralised administrative unit that is assigned, administratively, to the Federal Department of Justice and Police (FDJP), the FAOA is self-financ-

ing: it charges fees and levies supervisory charges and spends no taxpayers' money. The FAOA endeavours to manage its operations and fulfil its duties as efficiently and cost-effectively as possible. Its accounts are audited by the Swiss Federal Audit Office, which acts as the FAOA's statutory auditor and as part of its activities also carries out an economic efficiency audit¹. The FAOA's operating costs in 2008 of approximately 4.2 million Swiss francs (excluding the creation of a reserve pursuant to Art. 35, para. 3 of the Audit Oversight Act [Revisionsaufsichtsgesetz – RAG]) were within the budgeted figures and lower than original expectations; the Federal Council's Message originally projected operating costs in the region of 7–10 million Swiss francs².

¹ A summary of the key financial data may be found in Appendix 1.

² See p. 4096 Message regarding the amendment of the Code of Obligations (company law audit requirement) and the Federal Act relating to the Authorization and Oversight of Auditors of 23 June 2004.



2 Licensing

2.1 Introduction

After the end of the provisional licensing procedure at December 31, 2007³ the main task lying ahead in 2008 was the conversion of provisional licenses into final ones. The approximate 10,000 applications that in late 2007 and early 2008 resulted in provisional licenses being granted after a summary examination are being subjected to an in-depth assessment; if the outcome is positive, authorization final license is granted.

The number of applications which were submitted after December 31, 2007 and which, contrary to the lawmakers' expectations, had to be assessed by way of the «regular» procedure was unexpectedly high. For these new applications, which numbered approximately 1,250, the possibility of issuing a temporary provisional license no longer existed, which of necessity required an immediate full examination. In order that these applicants could provide audit services without any major interruption if at all possible, their applications had to be moved to the head of the queue. This tied up a considerable amount of resources and also impacted adversely on the conversion of applications that had only been given provisional approval.

The demand for the highest possible type of license for audit firms, that of state-regulated audit firm, was surprisingly high. Of the total of 48 applications received by the end of December 2007, 37 resulted in provisional licenses. Audit firms which submitted

an application to become a state-regulated audit firm cannot be granted a final license until after a first inspection has been completed (cf. Section 3 below). For that reason, by the end of the period under review only two of these audit firms could be granted full authorization. One major reason for this very high number of applications for state-regulated audit firm licenses is likely to be the fact that for certain special-law audit services a (basic) authorization as a state-regulated audit firm is prescribed (such as, for example, for the auditing of investment trusts or audit activities in the financial markets arena; cf. table below Sub-section 2.8).

In addition to newly-filed applications, the FAOA has set itself a target to complete the final assessments of all applications that have been given provisional approval by December 31, 2009. Whether this ambitious timetable can be met depends not least on how many additional applications continue to be submitted in the regular procedure and have to be assessed with high priority.

³ Cf. FAOA Activity Report for 2006/2007, pages 11–12.



2.2 Statistics

By December 31, 2008 the FAOA had received a total of 10,909 license applications. Of these, 4,349 were given full approval and 5,209 provisional approval. In total, therefore, 9,558 applications were given provisional or full approval and resulted in licenses being granted. Just under two-thirds of these were in respect of individuals (6,454), with the remaining licenses (3,104) being granted to audit firms.

In 987 cases no license could be granted, either because the applications were withdrawn by the applicant or because they did not meet the licensing conditions. As of December 31, 2008 1,351 applications were still pending, including applications which had not yet been processed and those that were incomplete.

Type of license	Auditor	Audit expert	Total
Individuals	1 020	1 592	2 612
Sole proprietorships	216	268	484
Audit firms	533	1 545	2 078
State-regulated audit firms	–	35 ⁴	35
Total provisional licenses	1 769	3 440	5 209
Individuals	600	3 242	3 842
Sole proprietorship	55	134	189
Audit firms	78	238	316
State-regulated audit firms	–	2	2
Total final licenses	733	3 616	4 349
Total licenses	2 502	7 056	9 558

⁴ Of the provisionally authorized state-regulated audit firms at December 31, 2008 (35), 6 firms withdrew their license applications for in this category in the last quarter of 2008. As the corresponding changes to the the applications were not legally binding at 31.12.2008, these 6 audit firms are still listed as state-regulated audit firms.



2.3 Provisional licensing

The overwhelming majority of the individuals and audit firms working in the audit industry in Switzerland availed themselves of the opportunity of provisional licensing and filed a license application prior to December 31, 2007. The selection of the applications which are now gradually being examined in detail has nothing to do with the qualifications of the individual or audit firm concerned, but is dependent solely on parameters that allow the FAOA to fully assess the applications as efficiently as possible. For that reason, it cannot be deduced from the fact that it takes a comparatively long time until final full licensing that the individual or audit firm concerned is regarded by the FAOA as a «problem case». It is therefore not unusual if applicants have not yet been requested to complete their application for full assessment for some time after provisional authorization.

For individuals or audit firms that for the time being have only a provisional license, no legal or competitive disadvantage arises. All audit services that have been performed by provisionally licensed individuals and audit firms retain their full validity, irrespective of the FAOA's final decision (cf. Art. 47, para. 7 of the Audit Oversight Ordinance [Revisionsaufsichtsverordnung]). In addition, holders of a provisional license are not obliged to inform their clients or third parties of the status of their licensing procedure. There need be no reference to the provisional nature of the license on business stationery and business cards, for example. For reasons of transparency, interested parties can, however, ascertain the current licensing status of any individual or audit firm at any time and free of charge by consulting the publicly accessible Auditors Register on the FAOA's website⁵.

At December 31, 2008 just under a half of all applications received by the FAOA were in «provisional license» status, which represents approximately 5,000 case-files (cf. Sub-section 2.2 above).

2.4 Final licensing procedure

At the end of the period under review, 3,842 individuals and 507 audit firms had final licenses from the FAOA. The comparatively low number of audit firms with final licenses can be explained by the fact that the members of the executive bodies and the senior auditors must themselves have the appropriate full licenses before the firm's application can be conclusively assessed. For this reason, applications from firms can only be assessed after a certain time-lag from the date the applications from the individuals concerned were processed.

The length of time it takes to process an application up to final licensing depends heavily on the complexity of the case and the quality of the documentation received. Since, for example, only professional experience under the supervision of a recognized practitioner is regarded as sufficient for the purposes of the Act (cf. Art. 4, para. 4 and Art. 5, para. 2 of the Audit Oversight Act), the eligibility of professional experience is often dependent on whether the practitioner supervising the applicant has the necessary final license. It will naturally take some time for this license to be obtained. For professional experience obtained up to two years after the Act came into force, the practitioner supervising the applicant does not, however, necessarily need to be licensed (either provisionally or finally) – it is sufficient to provide evidence that the practitioner supervising the applicant has the necessary training or would have been able to be recognized as «especially qualified» under the law prevailing beforehand (cf. Art. 43, paras. 4 and 5 of the Audit Oversight Act). Gathering the appropriate documents may take some time and delay the licensing procedure. Further factors that prolong the processing time might include having to obtain additional or more precise information on applicants' details and clarifications regarding their reputation or their ability to perform proper auditing.

⁵ <https://register.revisionsaufsichtsbehoerde.ch/search.aspx?lg=de>

2.5 Experience in the FAOA's first year

Generally, though, applicants can expect their applications to be processed promptly if they are complete and do not depend on a third party being licensed. If applicants have to rely on their applications being assessed urgently, they can request for them to be treated urgently (in return for a fee; cf. Art. 40, para. 2 of the Audit Oversight Ordinance). However, even when the treatment and assessment of an application is being fast-tracked, the FAOA cannot guarantee that an authorization decision will be taken by a particular date. The fast-tracking relates only to the FAOA's internal handling of a case-file. If the application is incomplete or a decision cannot be taken for any other reason, the procedure cannot be fast-tracked.

The time resources required for the final assessment of applications which had been provisionally approved in the first stage of the FAOA's operations turned out to be greater than expected. Depending on the circumstances, substantiating the professional experience requirement is a particular challenge, as the periods that are having to be assessed may go back as far as 28 years. For the purpose of the provisional licensing procedure the FAOA had relied solely on self-declaration by the applicants regarding their professional experience. For the purpose of the final assessment of applications this information has to be supported by documentary evidence.

On the question of professional experience, it was also often necessary for terms used in the Act to be clarified. For example, a more precise definition had to be found for what activities are to be regarded as activities in the fields of accounting and auditing, since the lawmakers' intention was that only such experience is eligible as professional experience within the meaning of the Act. Essentially, the crucial consideration here is that the practical experience provided a comprehensive understanding of external accounting and was acquired during the course of a statutorily prescribed audit and in accordance with the relevant professional standards.

In a number of cases there was the problem that the person being supervised was not formally accountable to a more senior person. Professional



experience is deemed to have been acquired under supervision only if the applicant was formally accountable to a practitioner who meets the statutory requirements and the activity was exercised under appropriate instruction (Art. 7 of the Audit Oversight Ordinance). Professional experience under supervision by a person at the same hierarchical level cannot, therefore, be recognized as such.

The requirements governing evidence of professional experience acquired in some cases in the distant past also had to be defined. In these cases the FAOA always endeavoured to find practical solutions within the statutory rules. Evidence of professional experience is therefore in principle not linked to any particular document but can be provided in various ways. Forms are in the meantime available for submitting evidence, but in certain cases it is no longer possible to submit forms at all. One example of this is supervision by a person who died a long time ago. For that reason, in exceptional or hardship cases, instead of providing hard evidence, it is sufficient merely to furnish plausible evidence of professional experience. As a rule, though the appropriate form for evidence of professional experience should be filed (the forms can be downloaded from the FAOA's website⁶).

The FAOA's verification of professional experience should not be equated with actual quality control – that is, a substantive examination of the applicant's audit record. This would in many cases no longer be possible for practical reasons. It is in fact an examination, not of substance, but of form, in which applicants must substantiate that they have actually acquired the professional experience. If, however, any misconduct is identifiable which casts doubt on the applicant's impeccable reputation or their ability to perform proper auditing, the FAOA seeks further clarification.

In a number of cases, moreover, it was shown that, in the case of restructurings, insufficient thought had been given to the consequences for licensing under the Audit Oversight Act. For instance, in the case of the conversion of a sole proprietorship, in which only the proprietor provides audit services, into a public or private limited company, it should be borne in mind that a new licensing application is required for the newly-established company. It goes without saying that the examination of a new application will take a certain amount of time. In order to forestall the possibility of not being able to provide

audit services due to the lack of a license, if there are any uncertainties, the FAOA should be contacted in good time well ahead of the planned restructuring. It should be noted that there is no longer any possibility for newly-established companies to be granted a temporary provisional license. New licensing applications from audit firms cannot be assessed until all the relevant individuals have themselves received their final licenses. If an audit firm is converted in accordance with the provisions of the Mergers Act, depending on the structure, it is possible that the existing license can be retained or a license can even be transferred, subject to consent from the FAOA. Early contact with the FAOA is recommended in such cases (see also Sub-section 2.6 below).

The FAOA frequently receives queries about uncertainties concerning the interpretation of particular provisions of the Act. In such cases the FAOA is only too happy to give its opinion – but it should be pointed out that the interpretation of imprecise provisions of the Act, especially in the new audit law enshrined in the Code of Obligations, is ultimately a matter for the courts. In addition, the cantonal commercial registries and the Federal Commercial Registry Office (FCRO) have developed a process for responding to particular questions.

⁶ http://www.revisionsaufsichtsbehoerde.ch/docs/content_blau.asp?id=30679&domid=1063&sp=D&addlastid=&m1=30479&m2=30511&m3=30679

2.6 Reporting and disclosure requirements

Many applicants assume that once authorization final license has been granted, there are no more obligations vis-à-vis the FAOA. That is incorrect and may, depending on the circumstances, lead to considerable difficulties, as the Act prescribes three reporting requirements for licensed individuals and audit firms:

- The first reporting requirement relates to the data entered in the Auditors Register. All licensed individuals and audit firms are obliged to notify the FAOA of any changes in such data (Art. 15, para. 3 of the Audit Oversight Act). These include in particular any change of address, telephone number or e-mail address. Due to the fact that the FAOA communicates mainly by e-mail, failure to notify it of the new e-mail address may result in the individual or audit firm being cut off completely from communication with the FAOA. The legal consequences arising from this are borne by the individual or firm concerned. In practice, a change of employer may also lead to problems. In this case the electronic link with the former employer must be terminated and the connection with the new employer established.
- Furthermore, from the time the application is filed, all individuals and audit firms are obliged to notify the FAOA with the least possible delay of any fact of relevance to the assessment of the licensing conditions (Art. 13, para. 1 of the Audit Oversight Ordinance). The notification requirement applies not only to the actual licensing procedure but for an indefinite period of time or the license no longer exists. The information that must be reported includes, in particular, criminal and administrative offence proceedings once they have been declared final and absolute; the issuance of certificates of unpaid debt in bankruptcies; civil or administrative law proceedings before administrative and judicial authorities in connection with statutorily prescribed audit services once they have been declared final and absolute; and proceedings before special-law regulatory bodies, stock exchange sanctions bodies or professional standards bodies.
- State-regulated audit firms are subject to a more comprehensive reporting requirement: in addition to the aforementioned information, they must also report all pending court or administrative offence proceedings. They are also obliged to inform

the FAOA with the least possible delay, in writing, of any matters that might be relevant for audit oversight (Art. 14, para. 2 of the Audit Oversight Act). These include, in particular, changes in the composition of top management, Board of Directors or Supervisory Board, a change of lead auditor (stating the reasons) or the early termination of or decision not to renew an audit engagement (stating the reasons). The latter applies, however, only to public companies audits. This list is not exhaustive, however; an intended merger must also be reported.

The disclosure requirement is met if the entry in question is altered in the relevant FAOA user-account within 10 working days or if the necessary details and documents are sent to the FAOA within 10 working days. For routine changes of lead auditors, due for example to rotation requirements, reorganizations, retirements or deaths, state-regulated audit firms have an extended reporting period of 30 working days.

Since breaches of the aforementioned reporting requirements are liable to prosecution, it is recommended that contact be made with the FAOA in good time if there are any uncertainties.

2.7 Register

The FAOA maintains an electronic register of licensed individuals and audit firms which may be inspected free of charge on its website (Art. 15, para. 2 of the Audit Oversight Act). Only individuals and audit firms that appear in this «Auditors Register» may be entered in the commercial register as auditors by the relevant commercial registry (cf. Art. 61, para. 1 of the Commercial Register Ordinance; SR 221.411). In the case of new registrations, the registrar verifies this by inspecting the FAOA's Auditors Register. In connection with the filing of audit reports in respect of ad hoc audits (such as audits of company formations, capital increases, capital reductions or mergers etc), the only audits that the commercial registry can accept are those that have been performed by licensed audit firms.

In order to ensure that auditors that had already been registered by a commercial registry before the new audit law came into force also meet the licensing requirements, a reconciliation between the commercial register and the Auditors Register will be undertaken in the near future (cf. Art. 27 of the Audit Oversight Ordinance). This will, in particular, filter out audit firms that have no licensed auditors.

If a company registered on the commercial register lacks any of the prescribed organs or any such organ is not properly constituted, the Commercial Registry Office requires the company to rectify the deficiency. If such action is not taken within the designated time, the commercial registrar applies to the court to take the necessary measures. Depending on the circumstances, the court may order the dissolution and winding-up of the company (cf. Art. 154 of the Commercial Register Ordinance (CRO) and Art. 731b of the Code of Obligations).

In addition, the FAOA's Auditors Register also lists any special-law licenses in the Swiss audit arena (see below).

2.8 Modular system

A license under the Audit Oversight Act entitles the holder to provide audit services in accordance with the applicable federal legislation, provided no special-law audit licence conditions also apply (cf. Art. 1, para. 3 of the Audit Oversight Act). Special-law licenses are prescribed only for individuals and firms in respect of whom a special regulatory body oversees the licensing and activities of auditors in the public interest. In so doing, these special-law licensing bodies work on the basis of the basic license granted under the Audit Oversight Act and demand in addition only evidence that the additional special-law license conditions are met (known as «modules», these build on the FAOA's basic license). In this way, duplications can be avoided and costs reduced for both applicants and the oversight authorities involved (cf. Art. 22 of the Audit Oversight Act, Art. 21 of the Audit Oversight Ordinance).

Following a basic authorization granted under the Audit Oversight Act, a special-law authorization must be obtained for activities in areas such as banking, securities trading and insurance in particular. Appendix 3 provides a summary overview of these areas.

There are special conditions to be observed relating to the auditing of housing cooperatives: in principle the audit requirement for these is governed by the provisions of the Code of Obligations. Although an audit may in principle be dispensed with (opting-out), as provided for by the Code of Obligations, for housing cooperatives with more than 30 residential units the Federal Office for Housing (FOH) requires a limited audit to be carried out by a person licensed by the FAOA even after the opt-out. If a housing cooperative has no more than 30 residential units, the FOH may permit an auditor's review of the annual accounts in accordance with its specifications if the person conducting the audit review has the necessary professional expertise. The foregoing does not, however, apply to umbrella organizations and central bond-issuing institutions, which in each case must have a full audit performed⁷.

⁷ See Art. 40 of the Housing Promotion Ordinance [Wohnförderungsverordnung] of November 26, 2003 (SR 842.1), Art. 17 of the Ordinance of the Federal Department of Economic Affairs of May 19, 2004 relating to Housing Cooperatives of Federal Employees (SR 842.18) and Art. 59a of the Ordinance of November 30, 1981 relating to the Act Promoting Residential Construction and Home Ownership [Wohnbau- und Eigentumsförderungsgesetz].

The Federal Council has decided to harmonize special-law licences with the Audit Oversight Act by September 1, 2009 (cf. Art. 52, para. 3 of the Audit Oversight Ordinance). This is likely to be largely achieved following the enactment of the new financial market legislation on January 1, 2009. The legal bases in the area of retirement pension and survivors' insurance have still to be coordinated by September 1, 2009.

On November 14, 2008 the FAOA adopted the Ordinance on Electronic Access to Data not in the Public Domain (FAOA Data Ordinance; SR 221.302.32). The Ordinance governs electronic access by special-law regulatory authorities to data on individuals and firms that have applied to these authorities for special-law licenses. Electronic access facilitates the transfer of data and documents that have already been filed with the FAOA as part of the basic licensing process and thereby reduces unnecessary administrative costs for applicants. The FAOA Data Ordinance comes into force on January 1, 2009.



3 Oversight

3.1 Introduction

The primary objective of the FAOA's oversight activities is to ensure the quality of audit services in respect of public companies by means of independent oversight. This is intended to promote trust – in financial reporting directly and in capitals market indirectly.

Further regulatory structures came into effect on April 1, 2008 in the form of the FAOA Ordinance on the Oversight of Audit Firms (FAOA Oversight Ordinance [Aufsichtsverordnung]; SR 221.302.33) and Circular No. 1/2008 on the Recognition of Audit Standards (Circular 1/08). In addition to the existing legal structures (Audit Oversight Act, Audit Oversight Ordinance), since spring of 2008 the FAOA has also had the necessary specific technical implementing regulations for its inspection activities. At the same time as these implementing regulations came into force, in April 2008, the FAOA commenced its inspections of state-regulated audit firms.

The FAOA has already described the general procedure for inspections in its first Activity Report – for 2006/2007⁸. This Report comments on the first experiences and findings of the FAOA's inspection activities. The structure of state-regulated audit firms and the effect on the frequency of future inspections are also discussed.

As a matter of general principle, reports on individual inspections are not published. The objective of the Activity Report is to present information of general relevance and to comment where there is room for improvement. This Report therefore presents the findings only in part and in condensed form and makes no claims to completeness.

⁸ See FAOA website:
<http://www.revisionsaufsichtsbehoerde.ch/bausteine.net/file/showfile.aspx?downaid=7422&sp=D&domid=1063&fd=2>



3.2 Market structure

The Enron accounting scandal of 2002 resulted in the break-up of the international audit network Arthur Andersen. Since then, the greater part of the public company audit market in Switzerland has been divided between three audit firms: PricewaterhouseCoopers AG, KPMG AG⁹ and Ernst & Young AG. It is estimated that these three audit firms cover in excess of 95 percent¹⁰ of the market capitalization in Switzerland.

Whether it is the number of all public companies audited (see Chart 1) or the number of listed companies audited (see Chart 2) that is compared, a similar picture emerges. In quantitative terms, too, the three major audit firms thus cover the overwhelming majority of the public-company audit market, although their percentage share is slightly lower than in a simple comparison of market capitalization.

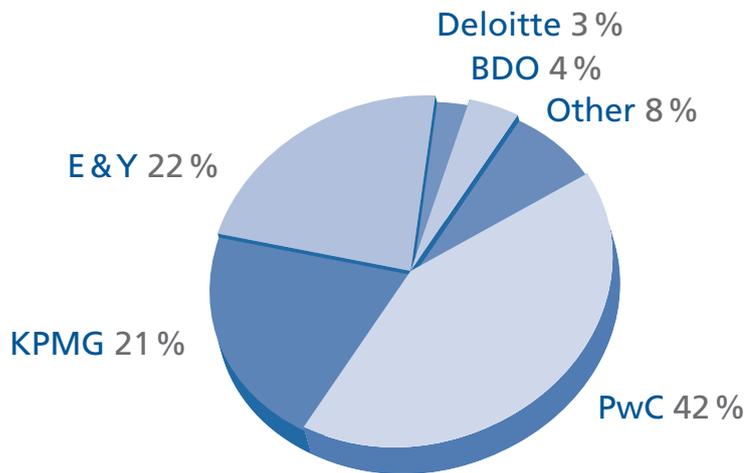
⁹ Incl. KPMG Klynveld Peat Marwick Goerdeler

¹⁰ Position at December 31, 2007

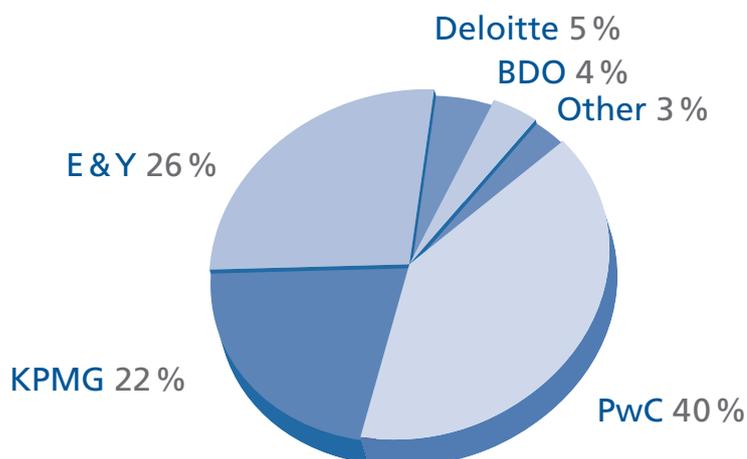


Chart 1:

Number of public companies audited per state-regulated audit firm as per FAOA register entry (all public companies)¹¹.

**Chart 2:**

Number of public companies audited per state-regulated audit firm (listed companies only)¹².



¹¹ Data as per FAOA register entries of state-regulated audit firms (state-regulated audit firms' self-declaration). As at December 31, 2008 the total population amounts to 504 public companies (incl. significant subsidiary companies: 151). The data for KPMG include the companies that are audited by KPMG AG and KPMG Klynveld Peat Marwick Goerdeler SA.

¹² Data as per http://www.six-swiss-exchange.com/admission/being_public/financial_reporting/bodies_de.html (position based on the 2007 Annual Reports; analysis for financial year 2008 not yet available). In the case of joint audits, both audit bodies are included in the statistics.

Because of the sheer scale and economic importance of the three major Swiss audit firms, the FAOA aims to examine these firms on an annual basis. The remaining state-regulated audit firms will be examined at least once every three years, as prescribed by law. These cycles may of course be interrupted by ad hoc inspections in cases of suspicion of breaches of statutory obligations. In cases of suspicion of breaches of statutory obligations the FAOA also has the option of carrying out an immediate investigation. Basing the frequency of inspections on the economic importance and capabilities of the audit firms further ensures that no unnecessary distortions of competition arise in the public company audit market.

3.3 Experience of the first inspections

3.3.1 General

As of December 31, 2008 2 audit firms have final licenses and 35 audit firms have provisional licenses as state-regulated audit firms, of which 13 have submitted to regulation voluntarily¹³.

10 inspections were carried out in 2008, although as of December 31, 2008 the inspection had been fully completed and final licenses granted in only two cases. In total, working papers for 23 audits were examined (file reviews).

In its first inspection year the FAOA subjected the three largest Swiss audit firms to a detailed examination. For these audit firms, in addition to their quality assurance systems, the working papers of 17 public companies were also examined. The findings summarised below (Sub-sections 3.3.2–3.3.3) relate solely to these three audit firms.

In addition, 2 smaller state-regulated audit firms and 4 which had submitted to state regulation voluntarily were subjected to a detailed examination. As the analyses of the findings on these inspections had not been complete by December 31, 2008, only a summary assessment is provided for this category of audit firms (see Sub-section 3.4).

In the course of these first-time inspections the proportion of the total time spent on the big audit firms' internal processes (firm reviews) was approximately 50%. The remaining 50% was accounted for by the inspection of working papers (file reviews). This high proportion of firm reviews is due to the fact that the internal processes and licensing documents were being reviewed and assessed for the first time. In future inspections resources will be shifted in favour of file reviews.

¹³ Cf. Sub-section 2.2 footnote 4

3.3.2 Firm reviews

In connection with the inspection of the internal processes of state-regulated audit firms (firm review), the FAOA based on the statutory requirements, covered the following areas:

- a. Examination of quality assurance systems (ISQC1 or Swiss Audit Standard 220), incl. independence
- b. Checking licensing documents

For these firm reviews, as they were all being performed for the first time, the FAOA undertook a comprehensive review of all elements of ISQC1.

In respect of selection and design of the internal quality assurance system by the audit firm depends on the accounting standards used and the size of the audit firm. The following table sets out the audit and quality assurance standards that must be applied:

Chart 3:

Summary of applicable quality assurance system audit standards¹⁴

¹⁴ Cf. FAOA Audit Oversight Ordinance and FAOA Circular 1/2008.

Financial statements according to	Swiss Audit Standards (AS 220)	IAASB audit standards (ISQC1 and ISA 220)	US audit standards (Statements on Quality Control Standards)
Code of Obligations	X	X*	X*
Swiss GAAP FER	X	X*	X*
IFRS	X**	X	
US GAAP	X**		X

Legend to Chart 3:

* IAASB audit standards and US audit standards may be used in addition to Swiss Audit Standards, use of which is mandatory.

** Applies only to audits by audit firms having their registered office in Switzerland (Art. 3, para. 3 of the FAOA Oversight Ordinance).

3.3.2.1 Assessment of the corporate culture at senior management level («tone at the top»)

Due to its example-setting function, the corporate culture at senior management level (Board of Directors and Executive Board), or «tone at the top», exercises a considerable influence on quality-consciousness among staff throughout the whole firm. In addition, the conduct of senior management is fundamental for all other components of an effective quality assurance system.

Basically, these quality aspects are accorded the necessary attention by senior management at the three largest audit firms. This is evident in, for example, the nature and frequency of internal staff communications and in the scale of training in quality standards.

Staff resources devoted to the implementation of and compliance with quality assurance measures have been increased in the past few years. In one case additional resources are, however, needed in order to ensure complete compliance with all quality assurance measures.

The three largest audit firms have formalised performance assessment processes for partners and audit staff. In respect of the members of senior management and also the partners, in some instances it was found that quality criteria were being inadequately addressed in the performance assessment process.

The compensation schemes that are currently in place do not always allow a clear link between quality criteria and the setting of remuneration levels. This link must be further improved in the future.

3.3.2.2 Ethical principles and independence

Ensuring independence and ethical principles is extremely important for the quality of audit services and the reputation of audit firms. If independence is compromised, this may render an audit almost worthless.

As a basic condition, it is essential that the partners and staff of audit firms know and comply with the applicable laws and standards relating to ethical principles and independence. The large audit firms examined have appropriate training programmes for this. In addition, annual and engagement-related processes for confirming the independence of partners and staff are used.

In its inspections, the FAOA ascertained that the audit firms have systems commensurate with their size and complexity in order to ensure compliance with the legal provisions on independence. As a rule, this involves IT-based systems for ensuring compliance with the independence rules relating to the financial investments and personal relationships of staff and the systematic recording of client relationships and client structures in databases.

Because of previous events in Switzerland and abroad, the independence of their partners is already more closely controlled internally by the three major audit firms. For instance, securities lists attached to the tax returns of the partners and other senior staff of all departments of the large audit firms are inspected on a random sample basis.

The FAOA found that in certain instances additional controls on the compliance with these systems need to be implemented or existing controls strengthened. Furthermore, post facto detective controls should be replaced by preventive controls in order to render any conflicts of independence impossible and to prevent them from being identifiable only after the event.

In particular, the FAOA identified breaches of the independence rules currently in force in the following areas:

- Staff failing to file individual confirmations of independence or failing to do so on time;
- Financial investments (purchases/sales) not reported in the systems provided for this or not reported promptly;
- Unauthorized financial investments held.

If an audit firm identifies a breach of the provisions relating to independence, appropriate measures should be taken to rectify this. In serious cases or in the event of repeated breaches, effective sanctions should also be imposed on staff and partners. In this respect, the FAOA is of the opinion that sanction measures should be imposed more rigorously in future.

In one instance there had been a breach of the 10% rule prescribed by the Act¹⁵. The annual fees from audit and other services provided for a single company and the companies associated with it through single management (a group) may not exceed 10% of an audit firm's total fee income. The 10% rule has to be observed at the level of the state-regulated audit firm and not just at a higher consolidated level.

3.3.2.3 Acceptance and continuance of client relationships and engagements

The internal processes for the acceptance and continuance of client relationships and engagements is the first step towards carrying out an audit assignment. The gathering of information for the purposes of assessing the acceptance of new client relationships or the continuance of existing engagements by the audit firm, including documentation of the thought processes behind the decision, is a key procedure.

At the large audit firms this process is carried out by means of computer-based applications which ensure that specific questions are addressed and ensure a systematic risk-weighting of the individual answers. In this way a consistent evaluation and weighting of the relevant risk-categories per client and engagement is guaranteed. This does mean, however, that the pre-set questions have to be answered with the necessary care and attention. In this respect the FAOA found a number of instances where the pre-set questions were being answered inconsistently or incompletely. In some cases this may very well influence the client and/or engagement risk as it forms the basis for deciding whether or not to accept or continue client relationships or engagements.

Furthermore, the process and procedure for accepting and continuing client relationships and engagements, right up to the creation of client numbers, depends on the networking of various IT systems. The networking of these systems needs to be accelerated in order to avoid manual interfaces and associated reconciliation or process errors.

3.3.2.4 Human Resources

The know-how of the persons involved in the audit work is reflected in the quality of the audit services provided. For audit firms it is thus essential to have their most important resource, their personnel, available in adequate numbers and with the necessary skills.

The lead auditor plays an important role in the assignment of the engagement teams; he/she must have the necessary abilities, skills, authority and time to do justice to this role. The majority of the audit firms do not have a comprehensive analysis to check whether lead auditors are sufficiently involved in the performance of audit assignments (number of partner hours in relation to the total reported hours per audit assignment). This is important as far as the FAOA is concerned as in some instances the partner's involvement proved to be very low. This can have a significant effect on the quality of audit services.

Compared to client-related and financial targets, addressing quality-related targets in the target agreement process and performance assessment process of the staff involved in the provision of audit services at all levels of the hierarchy is sometimes still a matter of secondary importance.

¹⁵ Art. 11, para. 1 (a) of the Audit Oversight Act

3.3.2.5 Proper performance of assignments

An audit firm must ensure that its audit assignments are executed in accordance with professional as well as regulatory requirements. The audit opinion, as the end product of the audit procedures, must be appropriate to the situation.

For the auditing of listed companies in particular, ISQC 1.60 requires the participation of a person who is responsible for monitoring the progress of audit work in a supporting capacity (known as an Engagement Quality Control Reviewer, or EQCR). The EQCR is generally an experienced audit partner who must be independent of the audit team and have the necessary qualifications. The FAOA found that the nature and scale of such monitoring activities was often too limited and that it is not clear from the working papers that the EQCR was sufficiently involved in the audit. Furthermore, the monitoring was sometimes not carried out continuously throughout the audit, as required, but only shortly before the audit certificate was issued. In some cases the FAOA questioned the independence of the EQCR from the audit team¹⁶. The FAOA believes that the monitoring of proper documentation is one of the areas sometimes neglected by the EQCR.

According to the audit firms' internal guidelines, as a rule it is the engagement partner who is responsible for deciding whether internal consultation is required. The FAOA gained the impression that this pragmatic latitude was rather overstretched in certain situations. Enlisting the support of internal specialists for specific audit areas should be clarified on the basis of existing guidelines and be a requirement in particularly complex situations.

Audit firms must also implement essential processes and controls in order to ensure compliance with the documentation requirements of ISQC1 and ISA 230 in audit working papers. The controls applied to ensure timely documentation, the archiving of working papers and the prevention of unauthorized changes to such papers need to be improved. At audit firms which mostly perform paper-based audit assignments, the existing processes and controls exhibit weaknesses in this regard and are sometimes inadequate to guarantee compliance with these requirements.

3.3.2.6 Internal monitoring

Internal monitoring ensures that quality assurance system directives, guidelines and processes are adequate and effective. This involves on the one hand assessing the internal quality assurance system and on the other periodically assessing the quality of the audit services provided.

For the FAOA, the effectiveness of internal monitoring is an important basis for determining the scale of its own inspections. If an audit firm's internal monitoring system is effective, the FAOA can reduce its own reviews of audit services (file review).

For the purpose of assessing the objectivity of internal monitoring, the use of reviewers from foreign network firms («non-local reviewers») at the big audit firms was investigated. This is important as far as the FAOA is concerned, due to the relatively small size of the national partnerships and the fact that the partners are as a rule well acquainted with each other in Switzerland. Employing non-local reviewers therefore increases the objectivity of internal monitoring systems significantly. At the big audit firms inspected, the employment of non-local reviewers ranged from 20% to 100%. The FAOA generally recommends that the proportion of foreign reviewers be kept as high as possible where public companies are concerned. Swiss resources should, however, be used for local issues (Swiss GAAP FER/AS, reporting under Article 725 of the Code of Obligations, implementation of IAS 19 in Switzerland etc).

Although internal monitoring identified a large number of significant findings in some cases, the FAOA felt that the rating assigned internally was too generous. Strict internal monitoring is in general essential for further enhancing the quality of audit services.

¹⁶ The major audit firms treat the requirements governing the independence of the EQCR in different ways. For example, one audit firm does not allow the EQCR to have any contact with the client, while other audit firms explicitly permit this.

3.3.3 File reviews

The selection of working papers inspected by the FAOA (file review) is based on an in-depth risk analysis and consideration of other specific aspects (e.g. different lead auditors). In its reviews the FAOA does not perform an «audit of the audit» but limits itself to the main risk areas, which are published in the Activity Report.

Of the numerous findings identified by the FAOA in connection with its inspection of the three big audit firms, the main findings, listed by the FAOA's main risk areas, may be summarized as follows:

a. High-risk audit areas (based on a review of the annual consolidated financial statements of the public company audited)

The audit areas with a high risk of misstatement in the financial statements should be dealt with by means of comprehensive audit procedures. In the opinion of the FAOA, the risk positions in the annual consolidated financial statements were generally covered with the necessary audit care.

Breaches of accounting regulations are investigated and punished by the SIX Swiss Exchange. In such cases the FAOA merely examines the role of the audit firm. For example, the FAOA verifies whether the shortcomings established by the SIX were identified by the audit firm and whether the necessary procedures (e.g. enlisting the assistance of experts) were observed. Ir-

respective of this division of responsibilities, the FAOA identified only occasional minor breaches of accounting standards which were not discovered by the auditors or were not corrected on materiality grounds.

For example, in this connection the FAOA found that the key assumptions used in assessing the carrying value of goodwill or other intangible assets (impairment test according to IAS 36) were in some cases not adequately challenged by the auditor.

b. The auditor's responsibility to consider fraud in an audit of financial statements (ISA 240)

The auditor must conduct extensive audit procedures and discussions relating to fraud and must consider comprehensively its effect on the financial statements in respect of misstatements. In its reviews the FAOA found the following:

- The auditor must always maintain a basic professional attitude of scepticism. This attitude is required in both the planning and the performance of the audit procedures. Sometimes the auditors relied heavily on past experience with the client, which runs counter to the principles of ISA 240.
- Discussions with management, the Board of Directors, Internal Audit or the audit team on the subject of fraud were sometimes not conducted to the extent required by ISA 240 and were also



inadequately documented in the working papers. Furthermore, the interviews were not carried out at the proper time during the planning stage but only shortly before the audit report was issued.

- Fraud risks identified by the audit firm should be covered by appropriate audit procedures. The audit procedures performed were, however, not always appropriate to adequately cover the risks identified.
- According to ISA 240, revenue recognition should as a matter of principle be regarded as a fraud risk. If revenue recognition is not considered a risk, then, according to ISA 240, the reasons for this should be documented. In a number of cases, however, the corresponding documentation was insufficient.
- In addressing the audit procedures to cover fraud, the auditor must, amongst other matters, incorporate an element of unpredictability into his/her audits. The required unpredictability of audit procedures was not planned and implemented by the audit teams to the desired extent, which increased the risk of fraudulent actions not being recognized.

c. Enlisting the services of internal and external specialists and network firms, using the work of third parties (ISA 600, 610 and 620)

The use of the work of third parties is an important element in the audit of financial statements, especially in complex and international relationships.

Regarding the use of the work of another auditor by the group auditor (inter office reporting under ISA 600), it was found that in some instances the professional competence and work of the other auditor was not properly challenged and assessed even though in some cases they had made a considerable contribution to the auditing of the financial statements. In general, moreover, the documentation of the conclusions resulting from the review of the other auditors' reporting was not documented (or not adequately documented) in the working papers of the group auditor.

The auditor has to acquire an adequate understanding of the work of the internal audit function in order to be able to assess any influence on the audit (ISA 610). This assessment has to be undertaken

even if there is no intention to rely on the work of the internal auditors. In some instances the auditor had not acquired such an understanding.

In assessing the work of an expert (ISA 620), the auditor has to assess the latter's competence and objectivity. The appropriateness of the assumptions and methods are to be questioned and assessed by means of appropriate audit procedures. In a number of instances this was not done to the required degree or with the necessary critical attitude. Furthermore, the source data (input data) used by the expert were not checked or not adequately checked.

d. Documentation of audit work (ISA 230)

From the perspective of the law (Art. 10 of the FAOA Oversight Ordinance) and of the audit standards, the requirements relating to the scope and degree of detail of working papers are comprehensive. This is relevant as in its reviews the FAOA was often referred by the auditors of the financial statements to audit procedures carried out but not documented. It is important to emphasize at this point that non documented work on audits of financial statements or documents submitted after the event cannot be assessed or taken into account by the FAOA.

It was also ascertained that the working papers did not always meet the requirements of ISA 230, since the nature, time and scope of the audit procedures was not clearly evident. Adequate steps had not always been taken, especially in the documents produced in paper-based audits, to ensure that it is clear from the working papers who performed the audit procedures and by whom and to what extent they had been reviewed.

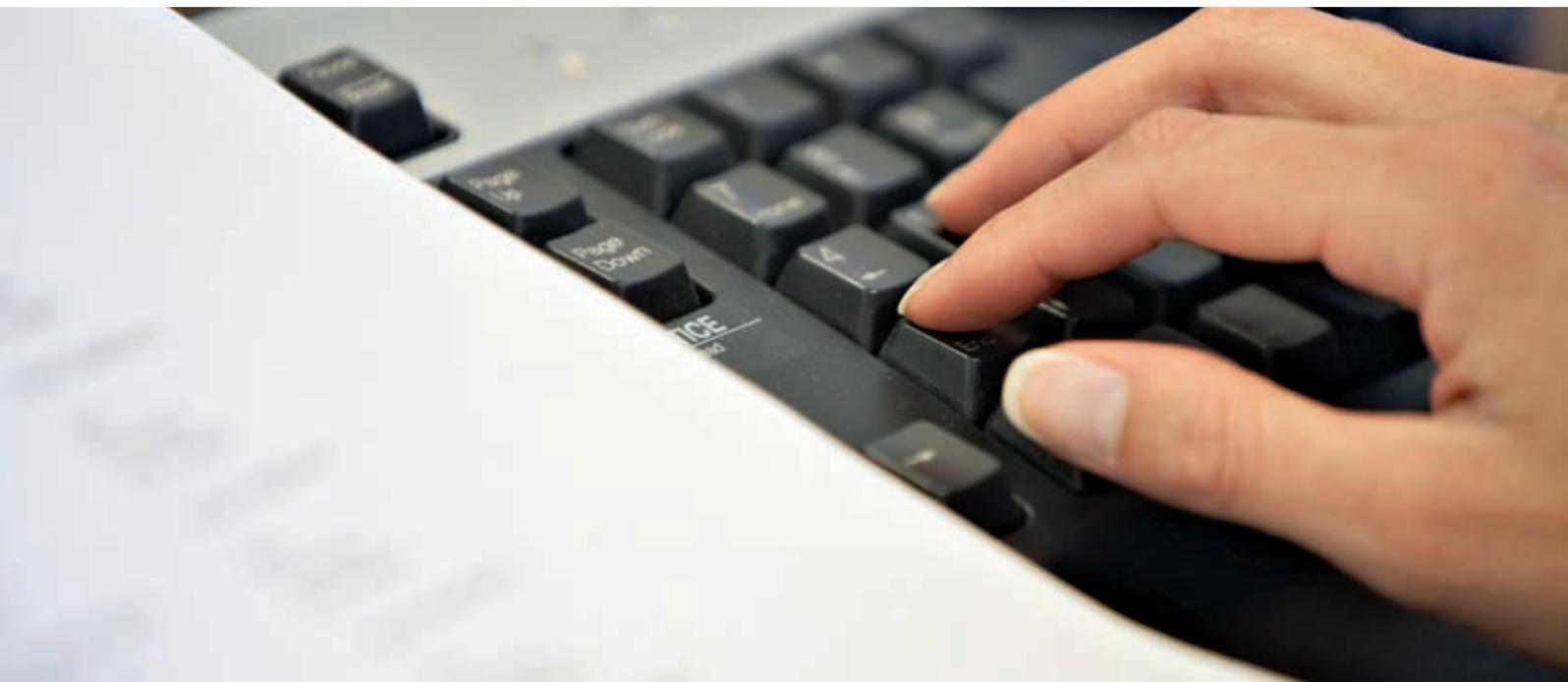
The FAOA considers that the completion of the working papers within the meaning of ISA 230.25 («Assembly of the Final Audit File») is a problem area, particularly with all paper-based audit documentation. With the controls actually in place, in the cases in question there was no assurance that only additions for administrative process purposes were made to the working papers after the date of the report and that the working papers were archived within the standard 60 days (ISQC 1.73b). The FAOA will take due account of this in future by increasingly giving the state-regulated audit firms concerned no notice of the working papers it plans to review (so-called «surprise file»).

3.3.4 Conclusion

The first-ever cooperation with the state-regulated audit firms went well. The audit firms provided the FAOA with all the documents needed for the inspections. Furthermore, there is great readiness amongst the firms inspected to permanently improve the quality of the audit services they provide still further by taking appropriate measures.

Fundamentally, the standard of the existing quality assurance systems (firm review) and the quality of the audit services (file review) at the three major audit firms is adequate. During the course of 2008 the FAOA identified no serious system deficiencies at the three large audit firms which would cast doubt on their ability to execute audit assignments. In addition, no sanctions needed to be imposed as a result of the first inspection.

In specific areas the existing quality assurance processes need to be further developed and the deficiencies revealed by the FAOA eliminated. To this end, measures were agreed upon with the audit firms which are to be implemented within a pre-defined time period. The FAOA will carry out appropriate monitoring of the elimination of the deficiencies identified and the implementation of the measures.



3.4 Reviews of smaller audit firms and audit firms which have volunteered to be state-regulated

In addition to the three major audit firms, the FAOA carried out inspections of a further six state-regulated audit firms in 2008. Of these, four were audit firms which had volunteered to be state-regulated.

Compared to the three major audit firms, these inspections resulted in more serious findings. These relate in particular to compliance with the independence rules; meeting the documentation requirements for working papers on audit work; and the nature and scope of the audit procedures relating to significant financial statement positions.

The existing quality assurance systems do not always meet the regulatory requirements. This applies, firstly, to the implementation and monitoring of compliance with the audit firm's quality assurance procedures and measures in general. Secondly, the existing systems for monitoring the progress of audit work during the audit or the random-sample monitoring of working papers after the audit have not been implemented or not adequately implemented.

Generally speaking, the FAOA found that in many cases an appropriate quality assurance system had not been implemented until the Audit Oversight Act had come into force and the inspection activities had commenced. This was problematic inasmuch as the professional standards (the Swiss Audit Standards or ISQC1) required such quality assurance systems to be in place before the Audit Oversight Act came into force.

The FAOA's inspections revealed that the high requirements imposed on the state-regulated audit firms were sometimes under-estimated by the audit firms concerned. It can be assumed that in specific cases the FAOA will not be able to grant final licenses until appropriate improvement measures have been implemented.

3.5 Cooperation with other Swiss agencies and stock exchanges

In the year under review the FAOA coordinated its inspections with other federal agencies (the Swiss Federal Banking Commission (SFBC) and the Federal Office of Private Insurance (FOPI) in order to avoid duplications of effort. In order to achieve this objective, the FAOA carried out a number of joint inspections with the SFBC and in one case with the FOPI as well. In these cases the firm review was performed by the FAOA. The file reviews carried out were shared – i.e. the SFBC and the FOPI reviewed the working papers of banks and insurers, while the FAOA reviewed the working papers of public companies from the industrial, retail and other sectors. This cooperation worked very well in practice and will be continued with the new Federal Financial Market Supervisory Authority¹⁷ FINMA in 2009.

In connection with the sanctions published by the SIX Swiss Exchange in respect of breaches of accounting standards, the FAOA independently investigated the role played by the auditors in each case. In these cases the FAOA chose not to re-assess the breaches of accounting standards¹⁸.

¹⁷ The Federal Office of Private Insurance (FOPI), the Federal Banking Commission (SFBC) and the Anti-Money Laundering Control Authority were merged into the Federal Financial Market Supervisory Authority as at January 1, 2009.

¹⁸ In particular, the materiality of breaches was not re-assessed.

3.6 Main areas to be covered by inspections in 2009

The previous year's emphasis on inspecting working papers is being carried forward unchanged because of its importance and the previous year's findings. As far as the follow-up inspections at the three major audit firms are concerned, a shift of resources from firm reviews to file reviews can be expected.

Due to the current state of the economy, the following areas will also be reviewed in-depth (where applicable):

- The auditing of fair values in respect of valuations and disclosures (ISA 545)
- Going concern (ISA 570)

In addition to the proper implementation of the applicable quality and audit standards and accounting rules, the FAOA will also be assessing the auditing of the new requirements of the Code of Obligations. This comprises in particular the following elements:

- Verifying the existence of an internal control system (Art. 728a, para. 1, indent 3 of the Code of Obligations / AS 890)
- Details on the performance of a risk assessment (Art. 663b, indent 12 of the Code of Obligations)
- Comprehensive report to the Board of Directors (Art. 728b of the Code of Obligations)

One of the main focuses in 2010 will be verifying the implementation of IFRS 8 («Operating Segments») in connection with segmental reporting in consolidated financial statements under IFRS (applicable for financial statements which began on or after 1 January 2009).

3.7 Standard-setting

Article 28 of the Audit Oversight Ordinance stipulates that the FAOA determines which audit standards state-regulated audit firms must adhere to when auditing public companies. In so doing, the FAOA refers to nationally and internationally accepted standards. If there are no standards or if any standards are inadequate, the FAOA can issue its own standards or add to or partially annul existing standards. In order to implement this provision, on April 1, 2008 the FAOA enacted the Ordinance relating to the Oversight of Audit Firms (FAOA Oversight Ordinance; SR 221.302.33) and Circular 1/2008 of March 17, 2008 (Circular 1/08) relating to the Recognition of Audit Standards.

The principle body responsible for developing internationally accepted auditing standards is the International Federation of Accountants (IFAC), which issues what are known as International Standards on Auditing (ISA) through the International Auditing and Assurance Standards Board (IAASB). An independent institution known as the Public Interest Oversight Board (PIOB) is responsible for monitoring the IFAC standard-setting process. Through its Oversight Ordinance, the FAOA has declared as binding all ISAs governing the auditing of annual and consolidated financial statements prepared in accordance with international accounting standards. The individual ISAs are listed in Circular 1/08.

In its Oversight Ordinance the FAOA also stipulates that, for the auditing of annual and consolidated financial statements prepared in accordance with US Generally Accepted Accounting Principles (US GAAP), US Generally Accepted Auditing Standards (US GAAS) and the Auditing Standards of the Public Company Accounting Oversight Board (PCAOB) are recognized as being equivalent to ISA.

As a basic principle the FAOA has adopted the ISA and the US GAAS/PCAOB standards in their entirety and has neither added to nor partially annulled them. Swiss legislation providing otherwise may continue to apply. In this context it should be noted that for companies having their registered office in Switzerland, even when their annual and consolidated financial statements are audited in accordance with ISA or US GAAS/PCAOB standards, the Swiss Audit Standards of the Swiss Institute of Certified Accountants [Treuhand-Kammer] (AS) must also always be applied.

In its Oversight Ordinance the FAOA has also stipulated that ordinary audits of annual and consolidated financial statements prepared in accordance with the provisions of the Code of Obligations or Recommendations relating to the Presentation of Financial Statements [Fachempfehlungen zur Rechnungslegung] (Swiss GAAP FER) must be audited in accordance with the Swiss Audit Standards recognized by the FAOA.

The issuer of these audit standards is the Swiss Institute of Certified Accountants. As a member of the IFAC, it has undertaken to implement the pronouncements of the IAASB in Switzerland provided this is permissible under Swiss law. Where the ISA are adopted in their entirety into the Swiss Audit Standards, the FAOA has no reason not to recognize them. The FAOA does, however, exercise a certain monitoring function with regard to the timing aspect of the implementation of the ISA. One of the main causes of delay in the implementation is the necessity to have them translated into German and French, a task which is carried out by the professional associations in Germany and France.

The adoption of the ISA into the Swiss Audit Standards is a particular challenge for small and medium-sized audit firms which would like to carry out ordinary audits as audit experts. For ordinary audits of annual and consolidated financial statements in accordance with the Code of Obligations or Swiss GAAP FER, small and medium-sized audit firms must comply with and implement the Swiss Audit Standards in their entirety. Since the FAOA oversees only state-regulated audit firms, it cannot, however, verify the effective implementation of these standards in ordinary audits of non-public companies.

The Institute of Certified Accountants is also drawing up new audit standards covering specific Swiss audit topics (e.g. AS 890 on Verifying the Existence of the Internal Control System). In these cases the FAOA is taking on a more active role. By so doing, the FAOA recognizes that the national audit standards are drawn up and issued by the professional association as part of self-regulation. It is bringing its own concerns into the development process at an early stage and is ensuring that what it believes to be the necessary provisions are factored into the standard.

As a basic principle, the FAOA sees no reason to develop its own audit standards. But under Article 28 of the Audit Oversight Ordinance it has the right to do so if no standards exist or if those that do must be considered inadequate. The FAOA would be reluctant to exercise this right since self-regulation in Switzerland has fundamentally stood the test of time.

Under this heading of standard-setting, the FAOA's activities in 2008 may be summarised as follows:

- On March 17, 2008 the FAOA issued the Ordinance relating to the Oversight of Audit Firms (FAOA Oversight Ordinance) and Circular 1/2008 relating to the Recognition of Audit Standards;
- The FAOA approved the Audit Standard on Verifying the Existence of the ICS pursuant to Article 728a, paragraph 1 of the Code of Obligations (see commentary in the FAOA's Activity Report for 2006-2007);
- The FAOA approved the wording of the revised audit opinion pursuant to Article 728b of the Code of Obligations. Changes to the existing wording were necessary because of the amendments to the Code of Obligations that came into effect on January 1, 2008.
- Under Article 6 of the Audit Oversight Act and Article 9 of the Audit Oversight Ordinance all audit firms must have an internal quality assurance system. For ordinary audits of annual and consolidated financial statements AS 220 – «Quality Assurance in Auditing» – or where necessary ISA 220 and ISQC1 of the IAASB should be applied. There is no defined quality assurance standard for limited audits. The Swiss Institute of Certified Accountants and Treuhand Suisse (Swiss Fiduciary Association) have therefore drawn up a quality assurance guide for small and medium-sized audit firms. The FAOA has recognized this guide as a basis for the licensing of small and medium-sized audit firms. It should be emphasized, however, that this guide is applicable only for the licensing of audit firms to carry out limited audits. For audit firms that perform ordinary audits AS 220 applies without restriction and in its entirety. Furthermore, according to an FAOA Notice, it should be borne in mind that in the case of ordinary audit engagements, in addition to monitoring the progress of

work during the course of an audit, random-sample after-the-event monitoring by an audit expert who was not himself involved in the audit should be provided¹⁹. For audit firms that perform only a limited number of ordinary audits, that are on a small and manageable scale, the guide can be used as an aid in implementing AS 220.

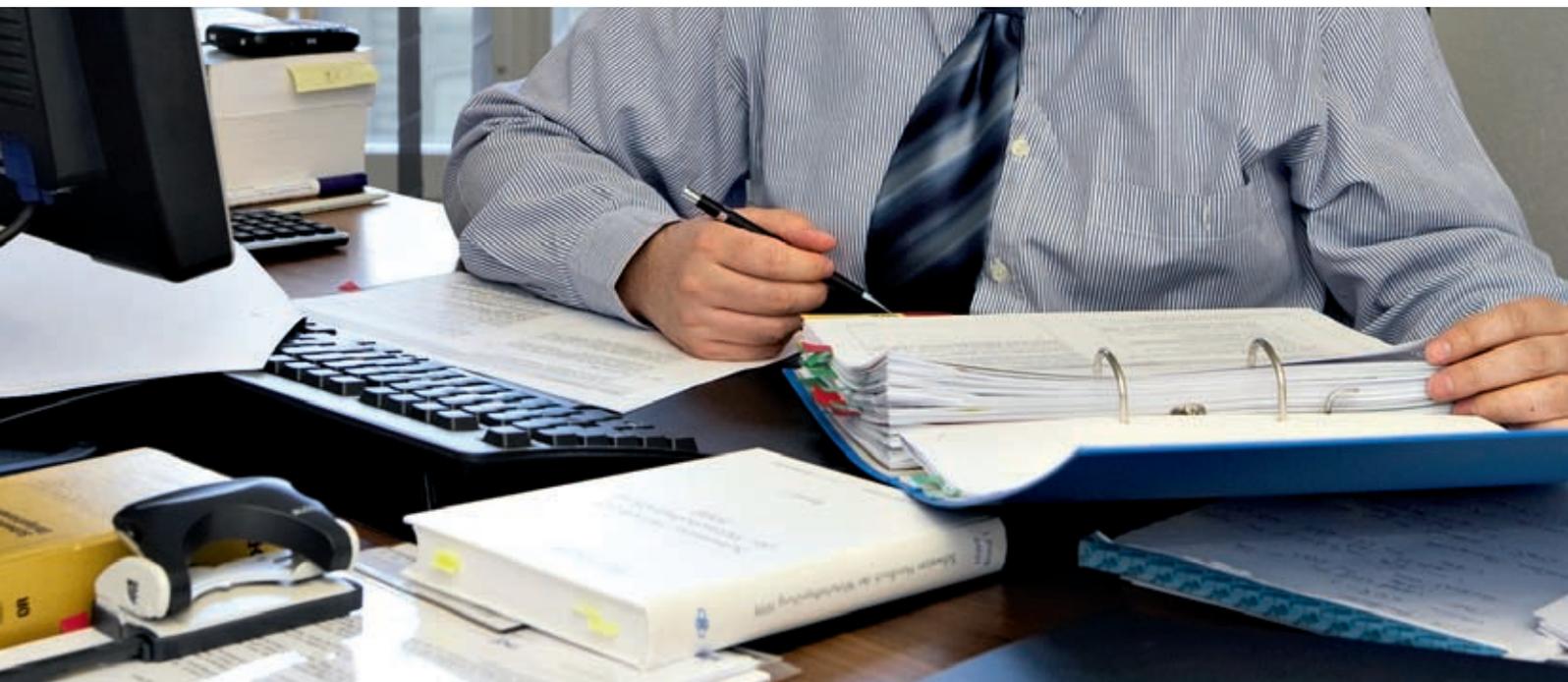
In 2009 the following topics are currently being dealt with by the FAOA in accordance with the principles presented above:

- Due to the amendments to the Code of Obligations as of January 1, 2008 it has become necessary to bring the existing audit standards into line. In 2009, the Swiss Institute of Certified Accountants has launched a project to that end and will issue a supplement to the Swiss Audit Standards, which date from 2004.
- Under Article 728b of the Code of Obligations the auditors must now provide the Board of Directors with a comprehensive report. The Institute of Certified Accountants has no plans to draw up an audit standard for this comprehensive report. AS 260 – «Communicating with Management on the Auditing of the Financial Statements» – is, however, being redrafted and added to. According to the Institute of Certified Accountants, the minimal content of the comprehensive audit report.

The FAOA oversees state-regulated audit firms by way of direct inspections. Such inspections will in the future also include a review as to whether the comprehensive report to the Board of Directors complies with the statutory provisions. So that the FAOA can assess this without leaving any room for doubt, the contents of the comprehensive report needs to be defined. For that reason the FAOA is planning to issue a Circular setting out the contents of the comprehensive report for public companies. In so doing, it has no intention of prescribing a binding template for auditors. The form the reports take remains at the discretion of the auditors – non-applicable subject-matter need not be commented on. The FAOA is of the opinion that the Boards of Directors of public companies would also want the FAOA to define the contents.

- Under the Swiss Stock Exchange Act, auditors fulfil important functions in public takeover bids. There is, however, no audit standard covering this. At the suggestion of the Takeover Board and the FAOA, the Institute of Certified Accountants has launched a project designed to rectify this omission. An audit standard defining the auditors' audit procedures in connection with takeover bids is to be developed during the course of 2009.

¹⁹ This is to be taken into account for ordinary audits of annual financial statements for 2008 and later. Proper implementation of independent after-the-event monitoring will be checked by the FAOA within five years at the latest, in the context of the renewal of the license of audit firms pursuant to Art. 3, para. 2 of the Audit Oversight Act.



4 International

4.1 Introduction

The trend towards even closer international integration of audit networks that had already been identifiable in 2007 strengthened further in 2008. As of October 1, 2008 KPMG Schweiz completed the merger with national member firms in Germany, the UK and Spain to form KPMG Europe LLP²⁰. Ernst & Young Schweiz agreed to merge with 86 other national member firms to form Ernst & Young EMEA (Europe, Middle East, India, Africa)²¹. PricewaterhouseCoopers intends to organize itself into three global regions (West, Central and East Clusters); the national ownership and management structures of the national member firms would remain unchanged²².

The increasing internationalization and globalization of audit networks is forcing audit oversight authorities to harmonize their oversight and quality assurance mechanisms and to develop, through closer cooperation and mutual recognition, into an international oversight system that is as efficient as possible²³.

Switzerland recognized this at an early stage and has already decided at the legislative level to adopt an efficient and internationally-oriented audit oversight system. The Audit Oversight Act makes it possible to offset the extraterritorial effects of Swiss law through a system of cooperation based on the principle of mutual recognition (cf. Art. 8 of the Audit Oversight Act). This recognition presupposes equivalence of the foreign audit oversight system, with the Federal Council being able to invoke pre-existing recognition by other countries or international bodies (cf. Art. 10, para. 1 of the Audit Oversight Ordinance). For the time being the Federal Council has not yet brought Article 8 of the Audit Oversight Act into force. As a result, the FAOA is being given sufficient time to find viable solutions for future cooperation with its main counterpart authorities in other countries. In 2008 the FAOA initiated dialogues with the European Union and the USA in particular. Detailed negotiations on mutual recognition are currently taking place with both economic areas (Sub-sections 4.2 and 4.3).

But mutual international recognition also demands a certain harmonization of the accounting and auditing standards applicable. Only high-quality and uniform accounting and auditing standards will meet with the necessary acceptance of preparers of financial statements, analysts, investors, accountants and oversight authorities. By recognizing and accepting the standards of the International Auditing and Assurance

Standards Board (IAASB), the FAOA has given a clear signal of its support for this convergence process (cf. Art. 3 of the FAOA Oversight Ordinance; Sub-section 3.7).

4.2 Relations with the European Union

Like the Swiss legislation, the 8th EU Directive (2006/43/EC) follows the principle of home country oversight, according to which it is the supervisory authority of the country in which audit firms have their registered office – their «home country» – that is responsible for the licensing and oversight of those audit firms, provided this oversight system is recognized as being equivalent.

In early 2008 the EU Commission, with the technical support of the European Group of Auditors' Oversight Bodies (EGAOB), undertook a preliminary evaluation of the oversight systems in the most important non-member countries. This also included an assessment of the Swiss system. The EU Commission came to no final decision regarding equivalence; but it did divide the oversight systems evaluated into two groups. The first group comprises non-member countries that already have public oversight of the auditing of financial statements. The second group consists of non-member countries which, although they might be able to introduce oversight, have not yet adopted or implemented the necessary legal foundations. Switzerland belongs to the first group, along with Australia, Canada, China, Japan, Singapore, South Africa, South Korea and the USA, and is thus in pole position, as it were, for recognition of equivalence.

²⁰ Cf. KPMG Schweiz media release of October 7, 2008.

²¹ Cf. Ernst & Young Schweiz media release of June 4, 2008.

²² Cf. PricewaterhouseCoopers Schweiz media release of August 20, 2008.

²³ Cf. article by Reto Sanwald/Sabine D'Amelio Favez, *Internationale Zusammenarbeit zwischen Revisionsaufsichtsbehörden [International cooperation between audit oversight authorities]* in: *Der Schweizer Treuhänder* 2008, pp. 872 et seq.

4.3 Relations with the USA

On 29 July 2008 the EU Commission decided to grant auditors and audit firms from certain non-member countries a transitional period for their respective audit activities. Accordingly, audit firms from 33 non-member countries (including audit firms having their registered office in Switzerland) are being allowed to continue their audit work companies registered in non-member countries that are listed on European markets. The transitional period runs until July 1, 2010 and is intended to allow the EU Commission to come to a final decision about the equivalence of the third country oversight systems in the interim.

A further evaluation of the Swiss audit oversight system has been taking place since the autumn of 2008 which will be crucial for the final assessment of equivalence by the EU. The decision on equivalence will also depend, amongst other matters, on whether and to what extent Switzerland recognizes the oversight systems of various EU member states as being equivalent. The FAOA is currently examining how the procedure for the recognition of European oversight systems by Switzerland can be designed and what criteria have to be met from a Swiss perspective for an equivalent system to be assumed to exist.

Audit firms which registered with the US Public Company Accounting Oversight Board (PCAOB) in 2003 and 2004 must, under US law, be inspected by the Board no later than four years after registration²⁴. The PCAOB originally intended to carry out the first joint inspections with the FAOA in Switzerland in 2008. But on December 4, 2008 the PCAOB published a draft amendment of a Rule allowing it to extend the deadlines for such joint inspections²⁵. Accordingly, inspections which were to have taken place in 2008 will have to be carried out in 2009. According to a number of criteria, inspections scheduled for 2009 can be postponed up to 2011. Consultations are currently taking place. The rule-change cannot come into force until the PCAOB adopts a final Rule and this is approved by the US stock exchange supervisory authority, the Securities and Exchange Commission (SEC).

The purpose of the joint inspections by the PCAOB and FAOA is to evaluate the Swiss audit oversight system with regard to full recognition by the PCAOB. The PCAOB published the criteria for «full reliance» on inspections by foreign authorities in a Policy Statement issued on December 5, 2007²⁶.

²⁴ Cf. Rule 4002 (d) (1) of the PCAOB Bylaws and Rules.

²⁵ PCAOB Release No. 2008-007, Rule Amendments Concerning the Timing of Certain Inspections of Non-U.S. Firms, and Other Issues Relating to Inspections of Non-U.S. Firms, of December 3, 2008, downloadable at: www.pcaob.org.

²⁶ PCAOB Rel. No. 2007-011, Guidance Regarding Implementation PCAOB Rule 4012, of December 5, 2007 (see also FAOA Activity Report for 2006-2007, p. 28).

The Policy Statement states that the examination of the criteria for full reliance can only be undertaken by way of joint inspections. If these establish that the foreign counterpart authority meets the quality, integrity, independence and transparency criteria, the PCAOB can grant the foreign counterparty authority full reliance status in a second stage. The final version of the Policy Statement has yet to emerge. For that reason, it is not beyond the bounds of possibility that the system as outlined will be further amended.

In March 2008 the FAOA informed the PCAOB that it agreed in principle to joint inspections, but made this subject to the proviso that, for reasons of legal security, a Memorandum of Understanding between the FAOA and PCAOB be concluded first. In addition, the FAOA is only prepared to carry out joint inspections with the US audit oversight authority if they are subject to a time limit. As mentioned, as far as Switzerland is concerned, joint inspections are only intended to be an interim solution while the PCAOB's confidence in the work of the FAOA is built up. As soon as this confidence has been created, the provisional system of joint inspections must be replaced by a full and final system of mutual recognition.

The negotiations on the necessary framework of legal conditions for joint inspections could no longer be brought to a conclusion in 2008. It is expected that a Memorandum of Understanding will be agreed in 2009, as a result of which the FAOA and PCAOB will carry out joint inspections in Switzerland later that same year.

4.4 Relations with third countries

Because Swiss firms have such a strong presence in EU member states and the USA, the FAOA concentrated in 2008 on recognition by and cooperation with these countries. But contacts with other countries were established and maintained at the same time. The first evaluation processes are currently taking place, especially in relation to Japan, which requested the FAOA in the summer of 2008 to complete a first questionnaire.

4.5 IFIAR meeting in Switzerland in 2009

2008 was an important year for the International Forum of Independent Audit Regulators (IFIAR). At its meeting in Cape Town in September 2008 the IFIAR adopted its Charter. The 27 member countries have thus created the basis for the further development of the IFIAR. The IFIAR's objectives – the exchange of know-how and experience between audit oversight authorities, the promotion of international cooperation and the creation of a contact point for other international organizations with interests in the field of auditing – were confirmed. The Charter also lays down the IFIAR's internal organization and contains rules for its internal decision-making.

The FAOA also played an increasingly more active role within the IFIAR in 2008. By now it is represented on two important IFIAR working groups. The aim of the Standards Coordination Working Group is to follow the work of the IAASB and to feed into it IFIAR members' experience and information. The International Cooperation Working Group seeks to promote international cooperation between the members of the IFIAR.

In addition, the IFIAR decided that its first meeting in 2009 would be held in Switzerland. The meeting takes place in Basel from April 27–29, 2009.

5 Court rulings

5.1 Introduction

By the end of 2008 the FAOA had received 10,909 license applications (see Sub-section 2.2 above). In the assessment of these applications a number of legal questions arose concerning the licensing conditions of Article 4 et seq. of the Audit Oversight Act. In connection with the first appeal proceedings against negative decisions by the FAOA, the Federal Administrative Court (hereinafter referred as the «FAC»), and in one case the Federal Supreme Court (hereinafter referred as the «FSC»), had an opportunity to express their opinion on specific licensing conditions – educational qualifications, professional experience and impeccable reputation – and on the FAOA's licensing practice.

The following summary provides an overview of the most important legal questions on which the two courts handed down rulings on educational qualifications (Sub-section 5.2), professional experience (Sub-section 5.3), reputation (Sub-section 5.4), procedural issues (Sub-section 5.5) and infringements of fundamental rights asserted (Sub-section 5.6)²⁷.

5.2 Educational qualifications

The list of educational qualifications required for licensing as an auditor or audit expert is now final (cf. list in Art. 4, para. 2 of the Audit Oversight Act). The FAC has backed this stance in a number of cases concerning applicants whose educational qualifications included a federal banking expert degree [eidg. dipl. Bankfachmann]²⁸, a university degree in political sciences²⁹, an education in business studies³⁰ or training as a private trustee without a Federal Certificate of Competence³¹. The Court states that the lawmakers deliberately included only a limited number of educational qualifications in the Act; these were educational courses which, as far as appropriate practical experience was concerned, would offer an assurance of high-quality audit services. The reverse conclusion to be drawn from this was that the educational qualification courses not listed in the Act had been deemed by the lawmakers to be inadequate³².

²⁷ For more on this, see also article by Reto Sanwald/Manus Widmer, Bundesverwaltungsgericht stützt Zulassungspraxis der RAB [Federal Administrative Court backs FAOA's authorization process], Grundsatzurteile zum Revisionsaufsichtsgesetz [Leading decisions on the Audit Oversight Act], in: Der Schweizer Treuhänder 2008, pp. 758 et seq.

²⁸ Decision No. B-1940/2008/kua of the FAC of June 10, 2008.

²⁹ Decision No. B-3393/2008 of the FAC of September 24, 2008.

³⁰ Decision No. B-2807/2008 of the FAC of August 19, 2008.

³¹ Decision No. B-2486/2008 of the FAC of October 7, 2008.

³² Decision No. B-1940/2008/kua of the FAC of June 10, 2008, recital 2.2.3.



Because of the lawmakers' clear directives, the FAOA has no power to authorize individuals with any educational qualifications other than those specified in the Act. As a general principle, the only exception is for individuals whose qualifications were obtained through educational courses under previous legislation that equate to one of the courses listed in the Act (so-called «grandfathered qualifications»). These include in particular those who had passed their first-year («propaedeutic») accounting expert [Bücherexperte] exams in 1974–1986, first-year tax expert exams in 1982–1986 and the Swiss Trustee Association trustee exam in 1981, 1982 and 1984. Under the Regulation relating to the Professional Examination for Trustees with Federal Certificate of Competence of December 1, 1983, these individuals may acquire the Federal Certificate of Competence for Trustees without having to take the examination again. Applicants who acquired such qualifications in any other year were denied this opportunity. The professional associations concerned and the Federal Office for Professional Education and Technology (OPET) could not (or could no longer) justify this different treatment. The FAC therefore ruled that there was no objective reason why individuals who had

passed their first-year accounting expert exam in other years should not be able to profit from this special Regulation³³. Effectively, individuals who passed their first-year accounting expert exams in 1958–1986 met the Audit Oversight Act's educational qualifications licensing conditions.

On the other hand, there is in any case no question of granting authorization license on the basis of the so-called «hardship clause» of Article 43, paragraph 6 of the Audit Oversight Act to an individual who does not have a recognized educational qualification. In addition, the possibility envisaged by the Act that the Federal Council may recognize other educational qualifications as being equivalent (cf. Art. 4, para. 3 of the Audit Oversight Act) relates only to educational qualifications that did not exist at the time the Audit Oversight Act was enacted³⁴.

³³ Decisions of the FAC No. B-3805/2008/scl of December 4, 2008, No. B-1499/2008/scl of December 15, 2008 and No. B-1237/2008/scl of December 22, 2008; these cases related to individuals who had passed their first-year (propaedeutic) accounting expert [Bücherexperte] exams in 1966 and 1970.

³⁴ Decision No. B-1940/2008/kua of the FAC of June 10, 2008, recital 2.4.



5.3 Practical experience

The lawmakers set different practical experience requirements for each type of license: Individuals applying for a license as an auditor must be able to give evidence of at least one year's practical experience under the supervision of a practitioner within the meaning of the Act (cf. Art. 5 of the Audit Oversight Act)³⁵. For admission as an audit expert, on the other hand, depending on their professional qualifications, applicants have to be able to give evidence of practical experience of up to twelve years, of which at least two-thirds must have been acquired under supervision (cf. Art. 4, paras. 2 and 4 of the Audit Oversight Act). In both cases the practical experience must have been acquired predominantly in the fields of accounting and auditing.

The FAC had to rule on the case of one applicant who claimed many years spent teaching accounting and business law as practical experience (see also Sub-section 2.5 above). The Court maintained that working as a teacher could not be deemed eligible as practical experience within the meaning of the Act. It stated that it was evident from the meaning and purpose of the statutory provisions relating to professional experience that the practical experience in the fields of accounting and auditing must stem at least to a large extent from the performance of such engagements and that practical activity in both fields was a necessary condition and one which needed to be substantiated³⁶. The FSC did not find in favour of the appeal against this decision since it considered any such appeal as non-admissible (cf. Art. 83, indent (t) of the Federal Supreme Court Act; SR 173.110). It did, however, hint that the appeal would have had no prospect of success anyway: teaching was no substitute for practical experience. In the light of the liberal drafting of the Act, which made it possible for individuals with broadly diversified educational qualifications to be granted admission, the practical experience requirements assumed that much greater importance³⁷.

In another decision, the FAC ruled on the FAOA's practice regarding admission as an auditor in application of the hardship clause (Art. 43, para. 6 of the Audit Oversight Act)³⁸. The practice whereby individuals can make up for one year's supervised practical experience with twelve years' unsupervised practical experience was judged to be too mechanical. The FAOA must not rely merely on the length of the practical experience but must also take into account other factors relevant to the particular case.

Nevertheless, applicants must still have many years' practical experience at September 1, 2007 (i.e. the date on which the Audit Oversight Act came into force), the majority of which was acquired in the fields of accounting and auditing and without any significant interruptions.

5.4 Reputation

An impeccable reputation is an essential condition for the admission of both audit experts and auditors. The impeccable reputation requirement is set out in Article 4 of the Audit Oversight Ordinance, which states that an applicant shall be admitted if that person has an impeccable reputation and if no other personal circumstances suggest that they do not offer every assurance of being able to perform proper audits. The items warranting particular attention here include criminal convictions and the existence of certificates of unpaid debt in bankruptcy.

Despite the greater clarity introduced by Article 4, the assurance requirement still remains an indeterminate legal concept, which has to be clearly defined in each specific case. The lawmakers did, however, follow the example of the standard criterion employed in financial market legislation, namely, «every assurance of proper business conduct». For the interpretation of this concept, it is therefore appropriate for the FAOA to take as its yardstick the practice relating to the equivalent provisions in the financial market field. The FAC has endorsed the position taken by the FAOA³⁹.

³⁵ For this purpose practitioners are deemed to be individuals licensed to act as audit experts or individuals licensed to act as auditors and foreign practitioners with comparable qualifications. During a two-year transitional period from September 1, 2007 lower requirements apply for qualification as a supervising practitioner (cf. Art. 43, paras. 4 and 5 of the Audit Oversight Act).

³⁶ Decision No. B-390/2008/kua of the FAC of April 30, 2008.

³⁷ Ruling No. 2C-438/2008 of the FSC of October 16, 2008, recital 3.

³⁸ Decision No. 5196/2008 of the FAC of December 11, 2008.

³⁹ Decision No. B-2440/2008 of the FAC of July 16, 2008, recitals 4.2.3 and 4.2.4, with further remarks on the development of a reputation examination pursuant to the Audit Oversight Act.

In one specific instance the court had to rule on an applicant who had for many years not been complying at all with his statutory obligations under Article 53 of the Occupational Pensions Act (OPA) [Berufliche Vorsorgegesetz – BVG]⁴⁰ as auditor of a pension scheme. The applicant had failed to conduct any audit of the accounts and had thereby failed in particular to identify that no accounts had been prepared at all for many years. Furthermore, he had breached his statutory obligations to provide the foundation supervisory authority with information on numerous occasions by failing to supply the information requested. In the course of criminal proceedings, the FSC subsequently followed the rulings of the courts of lower instance by finding the applicant guilty of gross violations of his statutory obligations as auditor under the OPA. Such misconduct is likely to tarnish the professional reputation and good name of an auditor and raise considerable doubts about his ability to conduct his business in a credible manner and to comply with the associated obligations. The FAOA's refusal to accept the license application was therefore considered by the FAC to be lawful⁴¹.

5.5 Procedural issues

By way of an interim decision, the FAC also issued an opinion on the question of the suspensory effect of an appeal against a negative admission decision by the FAOA⁴². In its opinion, as a basic principle, an appeal against a rejection of an application has no suspensory effect. This is in line with both theory and practice, according to which an appeal against a negative decision which does not change the existing legal position cannot be recognized as having suspensory effect⁴³.

In the aforementioned decision, the FAC also examined whether provisional admission should be prescribed in the context of a precautionary measure (cf. Art. 56 of the Administrative Proceedings Act [Verwaltungsverfahrensgesetz – VwVG]⁴⁴ but, after carefully weighing up the interests involved, decided that it should not. It came to the conclusion that the public interest of being protected against non-qualified audit work outweighed the interest of the employer – which already had provisional admission as an audit firm from the FAOA – in the admission of its employee and applicant. The lack of a provisional license did not prevent the applicant from continuing to work for his employer, even if he was not allowed to sign audit reports as lead auditor.

5.6 Fundamental rights

Several of the appeals against decisions by the FAOA to refuse to grant licenses were based on alleged infringements of fundamental rights. The most frequently asserted was an infringement of economic freedom (Art. 27 of the Federal Constitution [Bundesverfassung]; SR 101). Objections were also often raised against alleged violations of the precept of equality of treatment (Art. 8 of the Constitution), the prohibition on arbitrariness or the right to protection of vested rights (Art. 9 of the Constitution). Occasionally, the appropriateness of the refusal to grant authorization license was also questioned.

The FAC ruled that such objections were in principle admissible but in each case referred the appellant to the constitutional application precept, according to which Federal Acts and international law shall prevail for the Federal Constitutional Court and the other law-applying authorities (cf. Art. 190 of the Constitution)⁴⁵. Accordingly, Federal Acts should in principle be applied even if they might run counter to the Constitution. The aforementioned objections regarding the infringement of fundamental rights were, however, always rejected by the FAC on grounds of content. It stated that while the requirement for approval to pursue a profession in auditing was a serious infringement of economic freedom, such an infringement was permissible if it was based, as in the present case, on a formal statutory basis such as the Audit Oversight Act and was also appropriate⁴⁶.

⁴⁰ Federal Act of June 25, 1982 relating to Occupational, Survivors' and Disability Pensions.

⁴¹ Decision No. B-2440/2008 of the FAC of July 16, 2008, recital 4.3.1.

⁴² Interim decision No. B-2807/2008/baj/rip/scl of the FAC of May 26, 2008 (not published).

⁴³ Cf. HÄFELIN/MÜLLER/UHLMANN, *Allgemeines Verwaltungsrecht* [General Administrative Law], 5th edition, Zurich 2006, Marginals 1799 et seq.

⁴⁴ Federal Act of December 20, 1968 relating to Administrative Proceedings (SR 172.021).

⁴⁵ Cf. For instance, Decision No. B-1940/2008/kua of the FAC of June 10, 2008, recital 3.1; with further reference to relevant court rulings and literature.

⁴⁶ Decision No. B-2440/2008 of the FAC of July 16, 2008 recital 6.

In another decision the FAC held that the definitive statutory list of recognized educational qualifications (cf. Art. 4, para. 2 of the Audit Oversight Act) was not unconstitutional non-equality of treatment. The refusal to admit individuals who did not have a statutorily recognized educational qualification was based, rather, on objective and reasonable grounds, and non-equality was based on substantial actual differences⁴⁷.

⁴⁷ Decision No. B-1940/2008/kua of the FAC of June 10, 2008, recital 3.2.



Appendices

1 Abbreviations (where used in English)

CRO	Commercial Register Ordinance; SR 221.411
FCC	Federal Constitutional Court / Federal Casino Commission
EGAOB	European Group of Auditors' Oversight Bodies
EQCR	Engagement Quality Control Reviewer
FAC	Federal Administrative Court
FCC	Federal Constitutional Court
FCRO	Federal Commercial Registry Office
FDJP	Federal Department of Justice and Police
FINMA	Financial Market Supervisory Authority
FOH	Federal Office of Housing
FOPH	Federal Office of Public Health
FOPI	Federal Office of Privat Insurance
FSIO	Federal Social Insurance Office
GAAP	U.S. Generally Accepted Accounting Principles
GAAS	U.S. Generally Accepted Auditing Standards
IAASB	International Auditing and Assurance Standards Board
IASB	International Accounting Standards Board
IFIAR	International Forum of Independent Audit Regulators
IFRS	International Financial Reporting Standards
ISA	International Standards on Auditing
ISQC	International Standards on Quality Control
OPET	Federal Office for Professional Education and Technology
PCAOB	Public Company Accounting Oversight Board
SFBC	Swiss Federal Banking Commission
SEC	U.S. Securities and Exchange Commission
SIX	SIX Swiss Exchange
SME	Small and medium-sized enterprise

2 Key Financial Data

Income Statement

	2008	2006/2007
Oversight Authority charges	3'010'000	–
Inspection fees	1'073'000	–
Admission fees	1'336'800	9'076'100
Commissions for payments via internet	-73'703	-390'114
Reimbursement of admission fees	-279'350	-42'150
Unbilled admission fees 2008	-1'061'440	-4'970'720
Release of unbilled admission fees 2007	1'242'680	–
Other income	12'900	–
Net revenues	5'260'887	3'673'116
Personnel expenses	-3'330'249	-2'020'289
Operating expenses	-710'643	-698'008
Depreciation	-142'422	-76'499
Operating result	1'077'573	878'320
Financial income	112'647	708
Financial expense	–	-29'028
Financial expense	112'647	-28'320
Set up of reserves	-1'190'220	-850'000
Profit / Loss	–	–

Compensation of the Board of Directors and Management

	2008	2007
Board of Directors		
Fee, Chairman of the Board of Directors	110	110
Fee, Vice Chairman of the Board of Directors	75	75
Fee, other Members of the Board of Directors	90	90
Social Security Contributions ⁴⁸	16	17
Total fees paid to the Board of Directors	291	292
Director and Executive Board		
Salary, Director	240	230
Other benefits, Director	25	14
Salary, other Members of the Executive Board	358	226
Other benefits to other Members of the Executive Board	12	14
Social Security Contributions ⁴⁹	104 ⁵⁰	57
Total compensation paid to management	739	541

⁴⁸ The social security contributions that were paid during 2006/07 were reimbursed as it was ascertained that the Board members were not liable to social security contributions.

⁴⁹ Includes AHV/IV/EO-contributions, BU/NBU-contribution, BVG saving contribution and risk premium.

⁵⁰ In 2008 members of management were employed for the first time for a complete year. On July 1, 2008 the occupational pension scheme changed from a defined benefit to a defined contribution scheme, which necessitated a different calculation basis.

3 Special-law authorizations

A special-law license, deriving from a basic license granted under the Audit Oversight Act, must be obtained for activities in the following areas (position as of January 1, 2009):

Audits in the field of	Basic license under the Audit Oversight Act: Audit firms	Basic license under the Audit Oversight Act: lead auditors	Special-law regulatory authority	Additional requirements
Banks ⁵¹	State-regulated audit firm	Audit expert	FINMA ⁵²	Art. 26 FMSA ⁵³ Art. 3 FMAO ⁵⁴
Securities traders ⁵⁵	State-regulated audit firm	Audit expert	FINMA	Art. 26 FMSA Art. 3 FMAO
Collective investments ⁵⁶	State-regulated audit firm ⁵⁷	Audit expert	FINMA	Art. 26 FMSA Art. 3 FMAO
Insurers ⁵⁸	State-regulated audit firm	Audit expert	FINMA	Art. 26 FMSA Art. 3 FMAO
Anti-money laundering ⁵⁹	Auditor	Auditor	FINMA	Art. 19b AMLA ⁶⁰
Central mortgage bond institutions ⁶¹	State-regulated audit firm	Audit expert	FINMA	Art. 26 FMSA Art. 3 FMAO
Pensions companies ⁶²	Audit expert ⁶³	Audit expert	(FSIO ⁶⁴)	–
Health Insurances ⁶⁵	Audit expert	Audit expert	(FOPH ⁶⁶)	–
Casinos ⁶⁷	Audit expert	Audit expert	FCC ⁶⁸	Art. 75 CO ⁶⁹

⁵¹ Banking Act of November 8, 1934 [Bankgesetz; SR 952.0].

⁵² Federal Financial Market Supervisory Authority (FINMA), which commences operations on January 1, 2009 and unifies the Federal Banking Commission, the Federal Office of Private Insurance and the Anti-Money Laundering Control Authority.

⁵³ Financial Market Supervision Act (FMSA) of June 22, 2007 [Finanzmarktaufsichtsgesetz – FINMAG; SR 956.1].

⁵⁴ Financial Market Auditing Ordinance (FMAO) of October 15, 2008 [Finanzmarktprüfverordnung – FINMA-PV; SR 956.161].

⁵⁵ Swiss Stock Exchange Act (EA) of March 24, 1995 [Börsen und Effektenhandelsgesetz – BEHG; SR 954.1].

⁵⁶ Collective Investment Schemes Act (CISA) of June 23, 2006 [Kollektivanlagengesetz – KAG; SR 951.31].

⁵⁷ There are, however, two exceptions: Firstly, audit firms that audit asset managers and representatives of foreign collective investment companies need licenses as audit experts. The lead auditor also requires authorization license as an audit expert (cf. Art. 5 of the FMAO). Secondly, audit firms that have to prove that they fulfil the conditions of Art. 2, para. 3 of CISA for investment companies need a license as auditors (cf. Art. 6 of FMAO).

⁵⁸ Insurance Supervision Act (ISA) of December 17, 2004 [Versicherungsaufsichtsgesetz – VAG; SR 961.01].

⁵⁹ Anti-Money Laundering Act (AMLA) of October 10, 1997 [Geldwäschereigesetz – GwG; SR 955.0].

⁶⁰ Applies only to the auditing of financial intermediaries who are directly subject to supervision by the FMSA. Self-regulatory organizations may define differing conditions for the admission of audit firms for their membership.

⁶¹ Mortgage Bond Act of June 25, 1930 [Pfandbriefgesetz – PFG; SR 211.423.4].

⁶² Federal Act of June 25, 1982 relating to Occupational, Survivors' and Disability Pensions (OPA) [Berufliche Vorsorgegesetz – BVG; SR 831.40].

⁶³ There is, however, one exception: only audit firms that have state-regulated audit firm admission status can act as auditors for investment foundations (Art. 33, para. 3 of the Ordinance of April 18, 1984 relating to Occupational, Survivors' and Disability Pensions (OPO) [Berufliche Vorsorgeverordnung – BVV2; SR 831.441.1].

⁶⁴ Federal Social Insurance Office (FSIO) [Bundesamt für Sozialversicherungen].

⁶⁵ Federal Act of March 18, 1994 relating to Health Insurance [Krankenversicherungsgesetz – KVG; SR 832.10].

⁶⁶ Federal Office of Public Health [Bundesamt für Gesundheit].

⁶⁷ Casino Act of December 18, 1998 [Spielbankgesetz – SBG; SR 935.52].

⁶⁸ Federal Casino Commission [Eidg. Spielbankenkommission].

⁶⁹ Casino Ordinance of September 24, 2004 [Spielbankverordnung – SBV; SR 935.521].

