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Federal Audit Oversight Authority FAOA

Activity Report 2012



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P.O. Box 6023
3001 Berne

Phone +41 31 560 22 22

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Federal Audit Oversight Authority FAOA

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Foreword

The Federal Audit Oversight Authority (FAOA) began its operational activities on 1 September 2007. After five years there is, however, still no sign of routine. The environment in which the FAOA operates is changing rapidly. On the one side, the national audit oversight environment is changing. For example, on 15 June 2012 the Federal Council decided, in principle, to merge the previously separate audit firm oversight functions within the financial markets area and bundle them together with the FAOA in a two-step approach. As a result of this decision, as early as 1 September 2012 the oversight of financial statement audits for listed banks, insurance companies and collective investment companies was transferred from FINMA to the FAOA.

At the international level change is also noticeable. Here there are numerous regulatory initiatives that will change the face of audit in the future. The FAOA considered these initiatives during the year under review. The audit reform of the European Commission is of particular note.

The remit of the FAOA is to ensure the quality of statutory audit services. This is done on the one side through the licensing system and on the other through the oversight of the 21 state-regulated audit firms. The activities of the FAOA have led to noticeable quality improvements over the last five years. Even so, in many cases the professional scepticism of the auditor remains insufficient. This manifests itself in recurring audit deficiencies. The professional scepticism of the auditor will therefore remain a point of focus for the FAOA. Audit firms are also challenged though, as they must develop an internal framework that fosters such professional scepticism.

A further threat to audit quality – particularly at public companies – arises from fee pressure. Already last year, the FAOA warned of the long-term consequences of the price fall. This situation and the risks it brings have not changed since then. An important step towards rectifying this problem would be the realisation that an audit is not a service exchangeable at will, and for which only price is important. The audit of an entity in a high risk, dynamic and increasingly complex economic environment is demanding. In such an environment an audit of the necessary quality cannot be assumed to be guaranteed.

The above statements demonstrate that challenges remain for the FAOA. The FAOA will face up to these challenges. The above-mentioned bundling of oversight authority over audit firms under the FAOA is an important step towards strengthening audit oversight as a whole. Alongside this, the relevance of the audit as a whole has to be increased. The FAOA believes that the above-mentioned regulatory initiatives at an international level could contribute to this enhanced relevance.

Numerous new projects, such as the assumption of FINMA responsibilities and the establishment of a new IT infrastructure, have placed strong demands on our staff. We would like to thank them for their great commitment.

Berne, 21 January 2013



Thomas Rufer
Chairman of the Board of Directors



Frank-Oliver Schneider
Chief Executive Officer

Key activities 2012

International cooperation

After the Statement of Protocol with the PCAOB and the Memorandum of Understanding with the German audit oversight authority (GAOC) in 2011, two further cooperation agreements could be completed with the financial markets oversight authority of the Netherlands (Authority for the Financial Markets, AFM) and with the French audit oversight authority (French High Council for Statutory Auditors, H3C) in the year under review. Both the new agreements with the Netherlands and France are based on a decision of the EU Commission, under which the oversight authorities of EU member countries were given the green light to negotiate with the Swiss oversight authority, this being recognised as equivalent. The agreed principle of home country oversight brings considerable relief to internationally-active Swiss audit firms.

With respect to the USA, two further joint inspections were performed with the American audit oversight authority (PCAOB). The relationship between the two authorities continued to develop positively. Long term, the FAOA is striving for PCAOB reliance on the work of the Swiss oversight authority to be as far-reaching as possible. Cooperation with the PCAOB will be further intensified to this end. The FAOA and PCAOB report separately. No PCAOB reports concerning the joint inspections in Switzerland have been published to date.

Although the relevant statutory provision is yet to be enacted (Art. 8 AOA), it is apparent that some differentiation is needed as regards the extra-territorial scope of Swiss audit oversight. Investor protection and the correspondingly effective oversight of foreign audit firms need to be brought into a well-balanced relationship with the competitiveness of the Swiss capital markets. On 20 December 2012 the Federal Council submitted its proposals for the amendment of Art. 8 AOA for consultation.

Oversight of state-regulated audit firms

Since 1 September 2012 the FAOA inspects statutory audit services at listed banks, insurance companies and collective investment companies. Appropriate specialists were recruited in good time, such that the first file reviews at banks and insurance companies could already be performed in the year under review. The FAOA takes its new responsibility

seriously and thus takes account of internationally recognised oversight standards. For example, particular aspects of the audits of the two largest Swiss banks will be inspected annually. This is because they are ranked as global systemically important financial institutions¹.

Alongside the three largest Swiss audit firms, which are inspected annually, an additional ten inspections were carried out at other state-regulated audit firms. In its inspections the FAOA regularly identifies similar findings. These recurring findings were subject to international comparison as part of an IFIAR survey. The survey shows that many Swiss findings can also be seen in many other IFIAR member countries. Thus it is sensible to tackle these recurring findings not only at the national level but also internationally. At the international level, contacts between IFIAR members and the representatives of the six globally-active audit networks stand to the fore. The IFIAR members believe that the global audit firms should make greater efforts. Recurring deficiencies in the areas of professional scepticism, group audits, revenue recognition and the engagement quality review (EQCR) should be rectified. This would also include detailed root cause analysis as to why the same findings always recur.

Audit firms performing ordinary audits are subject to the external quality control of the FAOA only if they audit public companies or have voluntarily placed themselves under oversight. In view of the complexity of the ordinary audit, as well as the new thresholds, this is no longer appropriate and leads to competitive distortion. On 20 December 2012 the Federal Council submitted its proposals for the relevant amendment of the law for consultation. The draft law envisages that all audit firms performing ordinary audits would, in future, be subject to state oversight by the FAOA. The proposed oversight would, however, be carried out in a differentiated way. Due to the lower risk and public interest involved, audit firms that do not audit any public companies would not be inspected every three years but generally only every five.

¹ The «Global Systemically Important Financial Institutions» (G-SIFIs) are 29 financial institutions that the representatives of the G20 rank as systemically important. See also, in particular, the «Policy Measures to Address Systemically Important Financial Institutions» of the Financial Stability Boards (FSB) of 4.11.2011, in which stronger oversight of G-SIFIs is demanded (www.financialstabilityboard.org).

Licensing

In contrast to the licensing of individuals, the licensing of audit firms is limited to five years. In 2013 the FAOA will renew the first audit firm licences from 2008. In this connection, the focus in the year under review was on the creation of necessary processes and the development of a modernised IT platform. Through the optimal use of information and communication technology, the FAOA aims to achieve time and cost savings for licence applicants and itself. Business dealings with the FAOA should be conducted electronically as far as possible (E-Government).

Court decisions

In the year under review the practices of the FAOA were judged in two decisions (prior year one) of the Federal Supreme Court and nine (prior year 16) of the Federal Administrative Court. As the court decisions of prior years had provided clarification on the application of the AOA, particularly in the licensing area, this year all but one of the decisions of the FAOA were confirmed.

Whistle-blowing

In the year under review the FAOA received 35 third party notifications (prior year 10 notifications) of possible breaches of law or professional law. The increased number of notifications led in almost all cases to FAOA fact-finding. In individual cases the fact-finding involved the inspection of working papers relating to non-public companies. As a result of this fact-finding, various breaches were found and punished – particularly relating to audits carried out without the necessary licence and breaches of independence requirements.

«Long term, the FAOA is striving for PCAOB reliance on the work of the Swiss oversight authority to be as far-reaching as possible. Cooperation with the PCAOB will be further intensified to this end.»

1 Oversight

1.1 Introduction

The FAOA currently oversees 21 state-regulated audit firms² that are allowed to audit public companies. The ten largest Swiss audit firms audit a total of 23,648 audit engagements (see Figure 1). It is to be noted thereby that the oversight of statutory audit services by the FAOA extends to begin with to the approximately 490 public companies³. The quality of audit services for non-public companies is examined only on an exception basis (e.g. upon receipt of third party information).

Figure 1:

Number of audit engagements of the ten largest Swiss audit firms, ranked according to the total number of audit engagements⁴

Audit firm	Registered office	Number of public companies audited	Total number of audit engagements
PricewaterhouseCoopers AG (PwC)	Zurich	192	6,926
BDO AG	Zurich	28	4,631
Ernst & Young AG	Basel	110	4,256
KPMG AG	Zurich	103	3,470
Deloitte AG	Zurich	23	1,117
OBT AG	St. Gallen	3	1,050
Fiduciaire FIDAG SA	Martigny	1	722
Provida Wirtschaftsprüfung ⁵	St. Gallen	0	662
Fidinter SA ⁶	Lausanne	0	426
T & R AG	Gümligen	1	388
Total		461	23,648

The Swiss public company audit market continues to be dominated by the three audit firms; PwC, Ernst & Young and KPMG («Big 3»). Measured against the total number of audited public companies, the share of the «Big 3» amounts to around 88% (prior year 85%).

The most important constituent of FAOA oversight is the inspection, which, for the most part, is carried out at the premises of the state-regulated audit firm. FAOA inspections are planned and executed using a risk-based approach and on the basis of a multi-year plan. The nature and scope of inspection procedures are individually tailored according to the risks and complexity of the audit firm and the inspected engagements. The inspection of state-regulated audit firms includes both formal and substantive aspects. Within the scope of the firm review procedures are

² See Appendix 4 for a complete list of state-regulated audit firms.

³ According to entry in the FAOA register (includes significant subsidiary companies and issuers of listed bonds).

⁴ Source of audit engagement numbers: Website «www.wer-revidiert-wen.ch» of Credita AG, Baar, Switzerland (status as in August 2012)/Source of public company data: FAOA register as at 30.11.2012.

⁵ Provida Wirtschaftsprüfung is voluntarily under FAOA statutory oversight.

⁶ Fidinter S.A. Lausanne is not state-regulated.

performed to check that licensing conditions have been met and that there is a suitable and functioning internal quality assurance system. During the file reviews the quality of audit services is inspected on a sample basis⁷. The general approach of the FAOA is described in its Oversight Concept⁸.

1.2 Statistics on the number of inspections and findings (2008–2012)

The number of FAOA firm review findings has reduced over the last few years. However, the quality assurance tools available are not always used consistently.

As regards file reviews, the FAOA has noted improvements in audit documentation. In relation to substantive findings, however, no clear trend of audit quality improvement can be seen. Differences in audit quality are attributable to the individual-related elements of auditing in particular. This also explains individual differences in file review results within the same state-regulated audit firm. The composition of the audit team plays a very important role in audit quality.

Figure 2:

Overview of FAOA inspections and Comment Form findings

Category	Big 3 ⁹		Other ¹⁰		Total	
	01.04.2008 – 31.12.2012 ¹¹	of which in 2012	01.04.2008 – 31.12.2012	of which in 2012	01.04.2008 – 31.12.2012	of which in 2012
Number of inspections	16	3	34	10	50	13
Firm review Comment Form findings	56	8	192	31	248	39
File review Comment Form findings	229	19	245	32	474	51
Number of files inspected ¹²	62	9	33	9	95	18

⁷ Cf. FAOA Activity Report 2011, section 1.4.1.

⁸ See www.revisionsaufsichtsbehörde.ch (Documentation/Oversight Concept).

⁹ Ernst & Young AG, KPMG AG und PricewaterhouseCoopers AG.

¹⁰ 18 state-regulated audit firms as per Appendix 4.

¹¹ The FAOA began its inspection activities on 1.4.2008.

¹² In each file review the FAOA selects the working papers relating to the audit of the consolidated financial statements (including holding company) and the audit of a significant subsidiary.

In its findings the FAOA distinguishes between Comment Form and Other Reportable Findings. On the one side, this differentiation is made to improve the efficiency of the inspection process. On the other, it ensures that focus is placed upon the most important deficiencies when further developing the quality assurance system. The Comment Form includes important findings that are detailed within the inspection report to the state-regulated audit firm. The written Other Reportable Findings are not included within the inspection report but are to be considered by the audit firm in further developing its quality assurance system.

Specific remedial measures are agreed for each Comment Form finding, the implementation of these being checked by the FAOA. The FAOA differentiates between firm and engagement-related measures. Firm-related measures are aimed at the firm-wide improvement of the quality assurance system. Engagement-related measures require specific actions at the engagement level (e.g. changes to the engagement team, involvement of specialists). If audit evidence is insufficient measures are requested to obtain evidence or documentation retrospectively. If the FAOA deems the quality of the audit to be unsatisfactory it requires this to have a significant impact on the compensation of the auditor-in-charge and, if appropriate, the EQCR.

1.3 Inspections 2012

1.3.1 General

The FAOA performed 13 inspections in 2012. By the end of 2013 the FAOA will have completed the second inspection cycle, all state-regulated audit firms being subject to an FAOA inspection at least once every three years¹³. The «Big 3» already had their fifth inspection in 2012, as each of these three firms audit over 50 public companies¹⁴.

1.3.2 IFIAR survey

In an internationally-linked economy with globally-active public companies and audit firms, it is important that the firm and file review findings of the FAOA are compared, on an anonymous basis, with those of other oversight authorities. Such an international view is also necessary because the audit of a large public

company involves the work of numerous component auditors from different countries and audit firms.

On 18 December 2012 the International Forum of Independent Audit Regulators (IFIAR)¹⁵ published the results of a widely-based survey¹⁶. The survey was completed by 44 IFIAR member countries, its aim being to identify, on an anonymous basis, common findings at the six largest global audit firms¹⁷. The survey focused particularly on file review findings at public companies and systemically important financial institutions¹⁸. It should become the basis for the discussion and, if possible, coordination of measures to improve audit quality at a global level.

A comparison of FAOA file review findings with those of other oversight authorities shows that findings are made in identical areas:

- Professional scepticism of the auditor
- Group audit
- Role and responsibilities of the engagement quality control reviewer
- Audit of revenue recognition

The IFIAR member countries believe that global audit networks and local audit firms need to make greater coordinated efforts to eliminate the recurring deficiencies in the above-mentioned areas permanently. The oversight authorities involved find that measures have been implemented by audit firms in the audit methodology update, staff training, engagement quality review and internal monitoring areas. Irrespective of these measures, however, it is necessary for the audit firm leadership to foster a culture of quality and hold it in high regard.

¹³ Cf. Art. 16 para. 1 AOA.

¹⁴ Cf. FAOA Circular 1/2010, margin note 8.

¹⁵ Cf. section 2.5.

¹⁶ The results of the IFIAR survey were published within the report «2012 summary report of inspection findings» on 18.12.2012, as available on the following website: [https://www.ifiar.org/IFIAR/media/Documents/General/IFIAR-2012-Summary-Report-of-Members-Inspection-Findings-18-Dec-12-\(2\).pdf](https://www.ifiar.org/IFIAR/media/Documents/General/IFIAR-2012-Summary-Report-of-Members-Inspection-Findings-18-Dec-12-(2).pdf).

¹⁷ BDO, Deloitte, Ernst & Young, Grant Thornton, KPMG und PwC.

¹⁸ Cf. www.financialstabilityboard.org concerning the definition of «Systemically Important Financial Institutions (SIFIs)» and «Global Systemically Important Financial Institutions (G-SIFIs)», which were the subject of the survey.

1.3.3 Firm Review Findings

As regards the audit of public companies, the IFIAR survey further shows the following areas to have the most findings:

- Audit of estimates (ISA 540)
- Audit of internal controls
- Participation of engagement quality control reviewer

In the context of the audit of financial reporting by important financial institutions, additional findings resulted in the areas of financial assets and securities' valuation, as well as loan write-downs.

Professional scepticism is a fundamental basic attitude of the auditor that has a decisive influence on every audit procedure and therefore also on audit quality. Professional scepticism is an attitude that includes a questioning mind, being alert to conditions which may indicate possible misstatements and a critical assessment of audit evidence¹⁹. Lack of professional scepticism is seen by the oversight authorities – and also the FAOA – as the main cause of file review findings in many cases. A major challenge will be to identify appropriate measures to foster the necessary professional scepticism of the auditor.

As a possible measure towards improving quality many oversight authorities recommend a transparent communication of file review findings. The FAOA believes the disclosure of findings to the Audit Committee of the relevant public company to be an important way to encourage audit quality²⁰.

In its firm review inspection procedures the FAOA focuses primarily on assessing the effectiveness of the quality assurance system. The existence of comprehensive handbooks, directives and systems does not necessarily guarantee adherence to regulatory requirements. Staff must be familiar with the available quality assurance tools. Additionally, firm leadership must communicate the use and importance of these tools and lead by example in everyday professional life.

The 13 inspections in 2012 resulted in 39 firm review findings. Below are details of the most important of these:

¹⁹ Cf. ISA 200.13(l).

²⁰ Cf. section 1.10.

1.3.3.1 Ethical principles and independence

Compliance with independence requirements, without compromise or limitation, is a fundamental prerequisite for an effective audit²¹. Given the importance of auditor independence, the FAOA performs comprehensive inspection procedures in this area in each case.

a. Acceptance of additional services engagements at audit clients

In the year under review the FAOA had many findings, at both large and small audit firms, relating to the process for accepting additional services engagements at audit clients. Additional services were provided to audit clients without identifying possible threats to independence. In these cases safeguards were not adequately assessed, documented and implemented. The nature and scope of the proposed additional services was often not documented in the working papers. In some cases the additional services were also provided before being approved by the auditor-in-charge. In these cases a major risk exists that the acceptance of additional services engagements may breach independence requirements.

The FAOA expects the processes for accepting additional services engagements at audit clients to be applied more consistently and for breaches to be discouraged through disciplinary measures. Audit firms must also ensure that the employees within each business area that accepts and provides additional services are adequately instructed as to the available processes and independence requirements.

b. Leadership and decision-making function

In the year under review the FAOA ruled against five members of staff from a state-regulated audit firm regarding breaches of independence requirements. In three cases the FAOA issued a reprimand. In the other two cases the licence was withdrawn for a period of two years. An appeal was made to the Federal Administrative Court with respect to each of the licence withdrawals. Both appellants were, at different times, auditor-in-charge of companies whose Boards included a Director of the appellants' audit firm. In addition, one of the appellants had taken a loan from the above-mentioned Board member. The other did not possess the necessary special licence from FINMA.

1.3.3.2 Human resources

The FAOA checks that state-regulated audit firms comply with the training regulations of the Swiss Institute of Certified Accountants. In some cases the required training hours were not reached. Further, it was found that training was not provided in subjects relevant to the functions of the staff members. If staff members perform the audit of financial statements prepared under international accounting standards then these standards should be taught appropriately.

Audit firms must further ensure that performance reviews are performed for partners and staff of all grades. As in prior years, the FAOA found that quality-relevant goals are still insufficiently taken account of²². The sale of additional services to audit clients is often taken account of positively, although international independence rules explicitly forbid this²³.

1.3.3.3 Compliance with Swiss law

a. Licensing of auditor-in-charge

The auditor-in-charge must hold an FAOA licence²⁴ and shall take overall responsibility for each audit engagement to which he or she is assigned²⁵. It is important here that responsibility is not only assumed formally but also effectively. At audited companies regarded as important by the global audit networks, the allocation of responsibilities within the engagement leadership is not always clear.

²¹ Cf. section 3.8.

²² Cf. FAOA Activity Report 2011, section 1.4.3.3.

²³ Cf. Code of Ethics for Professional Accountants (CoE) of the International Ethics Standards Board of Accountants (IESBA), section 290.228.

²⁴ Cf. Art. 6 para. 1 indent c AOA and para. 29 AOO.

²⁵ Cf. ISA 220.8.

b. Listed companies with principal operating activities abroad

Some Swiss-listed companies have their main operations abroad. To the extent that the group's administrative functions are abroad in such cases, a substantial proportion of the group audit is also often performed abroad. However, the overall responsibility for the audit of the statutory consolidated financial statements still remains with the Swiss auditor. In such cases a clear division of responsibilities is required as to the audit and quality assurance. The audit client is to be informed as to who has overall responsibility for the audit. It is also to be determined how it will be ensured that supervisory and working paper review procedures for work performed abroad will be timely, sufficient and documented.

c. Liability insurance

State-regulated audit firms must have sufficient insurance for their liability risks²⁶. At several state-regulated audit firms the insured sum covered not only the licence-holder but also other companies within the same group. In addition, the insured sum did not only cover liabilities arising from public company audits. In these cases the FAOA required the insurance contracts to be amended to comply with statutory requirements.

1.3.4 File Review Findings

18 file reviews were conducted by the FAOA in 2012. These reviews resulted in a total of 51 findings.

In conducting each of its file reviews the FAOA selects the audit working papers relating to public companies. Where an audit firm voluntarily elects to be under FAOA oversight, non-public companies are also inspected²⁷. Public companies are those companies that have shares listed on a stock exchange, that have outstanding bonds, or that are classified as significant subsidiaries²⁸. In response to various questions, the term «stock exchange» was clarified in an FAQ in October 2012²⁹. It was explained, in particular, that companies registered in Switzerland whose shares are included in the «Entry Standard» of the Frankfurt Stock Exchange or in the «AIM» of the London Stock Exchange represent public companies. As such, these companies must be audited by a state-regulated audit firm³⁰.

The first-time inspection of the working papers of bank and insurance company audits produced similar findings to those from financial statement audits in other industries³¹. Many findings relate to group audits (ISA 600) and the audit of estimates (ISA 540). In its file reviews of banking engagements the FAOA also had findings relating to the audit of internal controls. The use of insufficient sample sizes and the audit of inappropriate controls result in errors in the scoping of substantive testing. This can lead to a failure to detect material misstatements in financial reporting.

1.4 Proceedings and preliminary fact-finding

In addition to routine inspections, the FAOA also conducts event-driven preliminary fact-finding and proceedings at state-regulated audit firms. In so doing, the FAOA considers, in particular, plausible information from third parties (e.g. media, whistle-blowers).

In 2012 the FAOA received eight notifications from third parties that related to state-regulated audit firms, the majority of which having been received anonymously through the FAOA website³².

Since the inspection activities of the FAOA began in 2008, 21 proceedings³³ have been conducted as part of the oversight of state-regulated audit firms:

– Six proceedings were against audit firms. In three cases the FAOA had identified breaches of independence requirements. In two cases measures agreed with the FAOA after its first inspection were not implemented or not implemented on a timely basis. In one case the statutory reporting obligation³⁴ was not met.

²⁶ Cf. Art. 9 indent c AOA and Art. 11 AOO.

²⁷ Cf. Art. 33 AOO.

²⁸ Cf. Art 727 para. 1 section 1 CO.

²⁹ Cf. FAQ on the definition of public companies of 9.10.2012.

³⁰ Cf. Art. 7 para. 1 AOA.

³¹ Cf. IFIAR survey findings (section 1.3.2 above) and FAOA Activity Report 2011, section 1.4.4.

³² Cf. www.revisionsaufsichtsbehörde.ch («Hinweise Dritter auf all-fällige Missstände»).

³³ These proceedings include already completed and on-going proceedings.

³⁴ Cf. Art. 14 para. 2 AOA.

- 15 proceedings were against individuals with an FAOA licence. Nine cases involved breaches of independence requirements. In six cases the FAOA found that the auditor-in-charge had not exercised proper duty of care.

In the instances found involving the failure to exercise proper duty of care the FAOA objected, in particular, to the following elements:

a. Leadership responsibility relating to audit quality

The auditor-in-charge shall assume responsibility for overall quality³⁵. He or she must be satisfied that the audit team possesses the necessary competence and capabilities³⁶. In addition, he or she must assume responsibility for the direction and supervision of the audit engagement³⁷. In cases where the FAOA found significant breaches of auditing or accounting standards this leadership responsibility had not been observed, or not sufficiently so. The FAOA particularly expects the involvement of the auditor-in-charge as regards significant risks.

b. Competence and capabilities

An audit firm may only accept an engagement if it has the necessary competence³⁸. This ensures that the engagement will be conducted in accordance with relevant standards.

During its file reviews the FAOA found breaches of basic accounting and auditing standards (e.g. substantial deficiencies in the treatment of deferred tax, failure to attend inventory counts, lack of IT audit procedures). The nature and scope of these breaches indicated to the FAOA that the audit team was insufficiently competent to fulfil the responsibilities assigned to it. This risk exists particularly at smaller audit firms, who perform few audits involving specific accounting or auditing standards. In these cases the critical mass necessary to develop and retain competence and capabilities is not reached.

³⁵ Cf. ISA 220.8.

³⁶ Cf. ISA 220.14.

³⁷ Cf. ISA 220.15.

³⁸ Cf. ISQC 1.26.

1.5 Audit Quality Measures

Every year the FAOA collects from the largest audit firms audit quality measures relating to various areas relevant to ISQC 1³⁹. These allow for trend analysis, as well as comparison between the individual audit firms. In addition, the audit quality measures enable the timely identification of possible negative influences on audit quality.

Figure 3:

Audit quality measures relating to the audit function of the five largest state-regulated audit firms, with prior year comparison⁴⁰

Audit quality measure	2010		2011		2012	
	from	to	from	to	from	to
Average annual revenue per audit partner (CHF mio.)	1.5	4.0	1.4	4.0	1.4	4.1
Average number of chargeable hours per partner	699	1,060	761	1,007	786	1,000
Ratio of additional fees to audit fees	0.1	0.7	0.1	0.5	0.1	0.6
Number of staff per audit partner	7.5	11.4	8	11.5	7.6	11.9
Staff turnover in %	15	27	16	23	16	28
Non-local reviewer participation within internal monitoring in %	11	100	0	100	3	100
Average number of EQCR hours per public company audit	4	16	9	20	7	22

The most important observations from the analysis of this key data are as follows (see Figure 3):

- In 2012 the **average annual revenue per audit partner** changed very little compared to prior years. A reduction in audit fees generally increases the risk that financial goals will be placed above those relating to quality. Furthermore, the year on year comparison shows, as in prior years, no positive correlation between the **average chargeable hours per partner** and the revenue per partner. Average revenue depends particularly on the number of staff per partner and the client structure of the firm.

³⁹ In part, the calculation of the audit quality measures was made using unaudited data. In individual cases simplifications or assumptions had to be made. The informative value and comparability of these measures is therefore limited and no responsibility is taken for their accuracy.

⁴⁰ The FAOA collected 12 audit quality measures relating to the individual elements of ISQC 1. They were collected from the five largest state-regulated audit firms. It should be noted that some firms also amended their prior year calculation basis to account for known errors.

- The ratio of **additional fees to audit fees** at public companies did not change in comparison with last year at the lower level and increased slightly at the higher level. For the FAOA the ratio of additional fees to audit fees represents an important risk factor in the independence area⁴¹.
- The **staff to partner ratio** decreased slightly at the lower level. With a high staff to partner ratio the risk exists that a partner cannot adequately fulfil his or her responsibilities as auditor-in-charge. This ratio is relatively low by international standards.
- Compared to the prior year **staff turnover** changed only marginally at four firms. At one firm staff turnover increased significantly (28 %) due to extraordinary measures. Adjusting the performance indicators for these extraordinary measures the highest turnover in 2012 was around 22 %. High staff turnover can threaten staff continuity on audit engagements. This in turn can have a negative impact on audit quality.
- The **composition of quality control review teams** for the purpose of ensuring objectivity varies considerably. Greater participation by non-local reviewers⁴² is normally beneficial since it generally increases the objectivity of the internal quality control review. According to the FAOA, there is a tendency for there to be a greater number of, and more substantial, quality control review findings where non-local reviewer participation is greater. At two firms the participation of non-local reviewers was 100 %.
- The **average number of EQCR⁴³ hours per public company** has hardly changed over the last years. The FAOA views the relatively low number of hours critically as important quality assurance duties are assigned to the EQCR. Precisely given the recurring engagement control review deficiencies found, an increase in EQCR participation is to be striven for⁴⁴.

1.6 Cooperation with other Swiss regulatory authorities and stock exchanges

To avoid duplication the FAOA coordinates its oversight activities with the other oversight authorities established under special law and with the stock exchanges⁴⁵.

In the year under review no joint inspections were performed with FINMA. However, given the respective oversight activities of the FAOA and FINMA, as well as the assumption of particular FINMA oversight responsibilities by the FAOA⁴⁶, a regular exchange took place.

The SIX Exchange Regulation (SER) is responsible for ensuring that companies listed on the SIX Swiss Exchange comply with accounting standards. The FAOA and SER coordinate their activities to avoid duplication. The FAOA assesses the audit activities of audit firms. The SER, on the other hand, assesses issuers' compliance with their responsibilities under the listing regulations.

In the year under review the FAOA received three notifications from the SER. In each case these led to preliminary fact-finding to assess the role of the auditor. The focus of the fact-finding in each case is upon compliance with legal and professional audit requirements, and not upon a re-assessment of compliance with accounting standards.

Should the FAOA find possible material breaches of accounting standards it notifies SER or the BX Berne eXchange. In the year under review one such notification was made to the BX Berne eXchange.

⁴¹ Cf. section 1.8.1 (Provision of additional services).

⁴² Non-local reviewers are partners or staff from foreign network member firms.

⁴³ The Engagement Quality Control Reviewer (EQCR) is the individual responsible for the engagement quality review (ISQC 1.35).

⁴⁴ Cf. section 1.3.2.

⁴⁵ Cf. Art. 22 and 23 AOA.

⁴⁶ Cf. section 1.7.

1.7 Assumption of particular FINMA responsibilities

On 15 June 2012 the Federal Council decided, in principle, to consolidate the previously separate oversight of financial and regulatory audits. In a first step, the oversight of the financial statement audits of listed banks, insurance companies and collective investment companies was transferred to the FAOA. No changes in the law were required for this. The transfer of the other responsibilities will follow in a second step, as soon as the Federal Assembly enacts the necessary changes to the law. This phased approach should ensure a smooth transfer. The Federal Council instructed the Federal Department of Justice and Police FDJP to prepare a Message of the Federal Council on the amendment of the Audit Oversight Act (AOA) and the Financial Market Supervision Act (FMSA). This is expected to be sent to the Federal Assembly in the first half of 2013.

The aim of the transfer of authority is to strengthen the system of financial markets oversight in Switzerland through a concentration of power. The consolidation of audit oversight authority within one authority will eliminate the weak points of the previous division. In the future, only the FAOA will be responsible for the oversight of audit firms. Staff resources and technical expertise will be bundled, thereby further professionalising oversight over the audit industry. At the same time, FINMA will gain independence in its dealings with audit firms, which will improve the interchange between the audit firms and FINMA over problems at financial institutions under oversight. Furthermore, duplication can be eliminated and efficiency gains for audit firms can be achieved. For the areas affected this means the following:

Licensing:

The FAOA assumes sole responsibility for licensing and, for the first time, adjudicates on the licensing of audit firms and auditors-in-charge who require a special law licence in the financial markets area.

Oversight:

The FAOA is solely responsible for the oversight of audit firms in the financial and regulatory audit areas. This applies to banks, securities traders, insurers, central mortgage bond institutions, collective investment companies, asset managers of collective investment companies, pension funds, and financial intermediaries under the direct oversight of FINMA.

Together with the authority to exercise oversight, responsibility for sanctioning audit firms and auditors-in-charge will be transferred to the FAOA.

Auditing standards:

FINMA will continue to determine the inspection topics and standards for the regulatory audit of financial institutions, while the FAOA is responsible for recognising the standards applying to the financial audit.

International administrative assistance:

The FAOA is responsible for international administrative assistance in the audit oversight area. A uniform, clear and efficient process can thereby be established vis-à-vis foreign oversight authorities. Requests made to the FAOA for administrative assistance may certainly not be used to obtain information and documentation from financial institutions that cannot be obtained through FINMA.

1.8 Analyses

1.8.1 EU proposals (audit reform)

Having evaluated responses to its Green Paper, the European Commission published its proposals for improving the audit market on 30 November 2011. Specifically, the Commission submitted separate proposals for a new Regulation on the audit of public-interest entities and for a Directive to amend the existing eighth EU-Directive.

Individual aspects of the new proposals are addressed below⁴⁷.

Auditor rotation

The European Commission proposes that the auditors of public interest entities should be required to stand down from the audit engagement after a period of six years (so-called external rotation). A cooling-off period of four years would then apply before the audit firm could again work on the engagement. The rotation period would increase to nine years in the case of a joint audit. In exceptional cases it would be possible to extend the engagement period for a joint audit by two, respectively three, years.

As a rule, where an entity is audited by the same auditor for a long period of time a relationship of trust develops between the audited entity and the audit firm, or rather their representatives, which can impair independence. There is a danger that this trust can, in fact or at least appearance, impair the independence and objectivity of the auditor. However, both the audited entity and the audit firm have a basic interest in maintaining their business relationship for as long as possible. This is because a first-time audit generates one-off costs for both sides. The alignment of interest between audited entity and auditor towards having as long a business relationship as possible can threaten independence.

The rotation of the audit firm after a certain number of years on an engagement is therefore generally a suitable way to strengthen independence. It is true that various studies on this subject have shown that mandatory rotation of the audit firm does not necessarily improve quality and independence or, as the case may be, that a longer term of engagement possibly has positive effects. However, it cannot be denied that an engagement term of many decades undoubtedly impairs independence, at least in appearance. In place of a fixed rule other approaches should also be considered: It would be possible, for instance, to require the appointment of an Audit

Committee to deal with audit issues at the level of the auditor. This could be given the responsibility, by way of an audit charter for example, of putting the audit out to tender within a period of nine to twelve years. Thus, flexibility could be maintained on the one hand while making the entity aware of the issue on the other.

Mandatory audit tendering

The European Commission proposes that public interest entities should be required to adopt an open and transparent tendering process when selecting a new auditor. The Audit Committee of the entity should thereby be closely involved in the selection process. The proposal foresees, amongst other things, that the Audit Committee of the administrative or supervisory body of the audited entity should recommend the appointment of an audit firm and also justify their recommendation. The recommendation must include a minimum of two proposals for the audit engagement. The selection criteria are also specified in detail.

The strengthening of the role of the Audit Committee that goes along with this proposal is to be welcomed. Audit Committees represent an important instrument in ensuring adequate control, respectively supervision, of financial reporting. In Switzerland the FAOA supports efforts to define and strengthen the role of the Audit Committee mandatorily. Whether the individual proposals of the European Commission are suitable for Switzerland is to be examined. On the whole, however, the general direction on this point appears to be right.

⁴⁷ A comprehensive analysis of the EU Commission's proposals of 30.11.2011 can be found in Schneider/Widmer: «Unabhängigkeit der Revisionsstelle: Ausgewählte Aspekte des Grünbuchs der EU», in: Finanz- und Rechnungswesen Jahrbuch 2013.

Provision of additional services

The European Commission proposes a mandatory differentiation between audit-related and non-audit services and defines both terms. Audit firms auditing public interest entities should no longer be permitted to provide non-audit services to the audited entity or its affiliates. In addition, large audit firms should separate their audit and non-audit services in order to eliminate the danger of conflicts of interest. Still further-reaching limitations are foreseen for audit firms for whom large public interest entities contribute more than a third of total audit fee income and who belong to a network whose members in the European Union have combined fee income of over EUR 1,500 million.

The parallel advisory activities of an auditor are not problematical per se, at least in terms of independence in fact. Advisory services to audit clients are therefore generally permissible in Switzerland. However, the economic independence of the auditor can be called into question if the ratio between advisory fees and audit fees becomes too high. Since the award of additional services is often linked to the audit engagement there can be an excessive interest in continuing the audit relationship, and the advisory services connected with it. Auditor independence can thereby be threatened. In Switzerland, the acceptance of an engagement which would lead to economic dependence is incompatible with independence. According to FAOA Circular 1/2010, a significant risk of impaired independence exists if the relationship between audit fees and additional fees exceeds a ratio of 1:3 in two consecutive years. Given current developments and discussions on independence, a reduction in this ratio is foreseeable.

In Switzerland the general prohibition of parallel services is certainly not in focus, only their limitation to a smaller amount. The effects of such a limitation in Switzerland would generally be small, at least in terms of SMI companies. As an FAOA analysis of audit fees and fees for other services for the year 2011 shows, at no SMI company do auditor fees from parallel services exceed 30% of audit fees. The majority of SMI companies (13 companies) purchase additional services from their auditors that amount to even less than 10% of audit fees. In this area the larger Swiss companies therefore already appear to have recognised that an independent audit is pos-

sible only if the auditor does not have to consider further lucrative engagements in reaching his or her audit opinion.

The proposals of the European Commission towards reforming the audit market go significantly less far than was expected based on the Green Paper. Some of the central aims, such as auditor rotation and the prohibition or, as the case may be, significant limitation of parallel services will remain contentious. It is currently unclear how the EU Parliament, or rather the member states, will react to the proposals. However, if one looks at the development of independence and audit quality requirements and the corresponding regulation over the last years, respectively decades, a strengthening of the current provisions appears likely. Overall, the improvements should not be seen as a threat, but far more as a chance to increase audit relevance.

1.8.2 Other international initiatives

The financial crisis led to a worldwide questioning of the value and relevance of the audit. Since then, regulators and standard setters in many countries have examined the need for changes in regulation intensively. The aim of the large number of regulatory initiatives is to close the expectation gap between the current role of the audit and the public perception of it. At the international level initiatives to increase the value and relevance of the audit exist in the following areas:

- Improvement, respectively development, of the auditor's reporting model;
- Strengthening the role of the Audit Committee;
- Enhancing the independence, objectivity and professional scepticism of the auditor;
- Increasing audit transparency;
- Alternatives to the market concentration of the Big 4.

1.9 Standard-setting

Over the last few years accounting and auditing standards have been revised and developed further. The updating of methodologies and continuous staff training is of central importance to audit firms. To guarantee these, audit firms must have internal processes and sufficient resources to monitor developments and make the necessary changes on a timely basis. For its part, the FAOA views the further development of international and national auditing standards as an important element in improving audit quality and monitors such developments actively. The FAOA is a member of an international working group that fosters periodic exchanges over the international process for determining audit standards⁴⁸.

1.9.1 Swiss auditing standards

With a view to further developing national auditing standards, the Swiss Institute of Certified Accountants undertook a consultation concerning the Swiss Auditing Standards (SAS), 2013 edition. The revised SAS apply to the audit of statutory and consolidated financial statements for financial periods ending on or after 15 December 2013. The 2013 edition of the SAS replaces that of 2010. As before, the SAS must be used for the ordinary audit of statutory and consolidated financial statements. The FAOA submitted its comments on the draft in October 2012⁴⁹. The FAOA welcomes the incorporation of the Clarified ISA and the quality assurance standard ISQC1 within the SAS.

Through the new Swiss quality assurance standard 1 (QS 1), new requirements have been set regarding the quality assurance systems of a firm. Of the 21 state-regulated audit firms as at the end of 2012, nine still have quality assurance systems based on SAS 220. Here the FAOA will accordingly assess whether the revised SAS and QS1 have been implemented appropriately as part of its inspections.

1.9.2 International auditing standards

With the implementation of the Clarified ISAs, substantial changes took effect during the audit of the 2010 statutory and consolidated financial statements⁵⁰. Jointly with other European audit oversight authorities, the FAOA submitted a comment letter to the IAASB in October 2012 in this regard⁵¹. The

comment letter highlighted individual weak points in the extant ISAs.

In 2012 the FAOA also submitted comments on various other IAASB and IESBA proposals⁵². The following should be highlighted:

- The IAASB presented an invitation to comment with regard to improving auditor reporting in the future. This was commented on within a consolidated comment letter from the European audit oversight authorities⁵³. The FAOA supports the efforts of the IAASB to improve the transparency of auditor reporting. Through it, the reader of the report should be able to obtain a better understanding of the audit process and the significant risks of the audited entity.
- Already last year, the FAOA provided a comment letter on the revision of the standard covering cooperation between the external and internal auditor (ISA 610)⁵⁴. In line with other oversight authorities, the FAOA is critical of the concept of direct assistance by the internal audit function. As, in revising the internal audit standard, questions also arose as to the definition of the audit team and the scope of independence requirements, a comment letter was submitted to the IESBA in June 2012 relating to the definition of the engagement team⁵⁵.

⁴⁸ Cf. section 2.5. The FAOA is a member of the IFIAR Standard Coordination Working Group (SCWG).

⁴⁹ See www.revisionsaufsichtsbehörde.ch («Dokumentation/Stellungnahmen der RAB/RAB reicht der Treuhand-Kammer Stellungnahme zur Vernehmlassung der PS ein» of 8.10.2012).

⁵⁰ Cf. FAOA Activity Report 2011 Section 1.10.1a.

⁵¹ See www.revisionsaufsichtsbehörde.ch («Dokumentation/Stellungnahmen der RAB/Stellungnahme zur Implementation der 'Clarified ISAs' an das IAASB» of 17.10.2012).

⁵² See www.revisionsaufsichtsbehörde.ch («Dokumentation/Stellungnahmen der RAB»).

⁵³ See www.revisionsaufsichtsbehörde.ch («Dokumentation/Stellungnahmen der RAB/Stellungnahme zur Berichterstattung der Revisionsstelle an das IAASB» of 23.10.2012).

⁵⁴ Cf. FAOA Activity Report 2011, section 1.10.1c.

⁵⁵ See www.revisionsaufsichtsbehörde.ch («Dokumentation/Stellungnahmen der RAB/Stellungnahme zur Definition des Prüfungsteams an das IESBA und IAASB» of 1.6.2012).





1.10 Forwarding of reports to the Audit Committee

The Board of Directors has an important, non-transferable duty with respect to the design of the accounting function, financial control and the preparation of the annual report⁵⁶. The Audit Committee is responsible for reaching an independent opinion on the external audit. The Audit Committee must form a picture of the effectiveness of the external audit, as well as assessing the performance, independence and fees of the auditor⁵⁷.

Alongside continual improvement in audit firm practices, further accompanying measures are needed to improve audit quality. Strengthening the role of the Audit Committee, in particular, is one of these⁵⁸. The active and responsible discharge of its duties by the Audit Committee has substantial effects on audit quality.

The FAOA therefore believes it important and necessary that affected public companies know the results of the file reviews conducted on their audit engagements. This supports the Audit Committees in their duty to evaluate and continually check the work of the auditor. The wish of the FAOA is, moreover, in line with the needs of other regulators and is being discussed within the scope of international initiatives towards further developing audit quality. Due to its official secrecy obligation the FAOA is not allowed to forward information itself. Therefore, it is recommended that the auditor forward the relevant information to the Audit Committee⁵⁹.

- Auditor responsibilities with respect to fraud (ISA 240);
- Audit of accounting estimates, including estimated fair values and their disclosure in the notes to the financial statements (ISA 540);
- Special considerations relating to group audits, including the work of the component auditor (ISA 600);
- Audit of risk areas, for which substantive testing alone cannot provide sufficient appropriate audit evidence (e.g. bulk transactions at banks and insurance companies; ISA 315.30);
- Assessment of the work of the engagement quality control reviewer (EQCR);
- Assessment of professional scepticism.

In each file review further points of focus arise from analyses of the specific circumstances and relate to the application of auditing or accounting standards. Since the FAOA does not perform «an audit of the audit», only certain points of focus are selected in each case.

⁵⁶ Cf. Art. 716a para. 1 section 3 and 6 CO.

⁵⁷ Cf. «swiss code of best practice for corporate governance» of the *economiesuisse*, section 23 f.

⁵⁸ Cf. FAOA Activity Report 2011, section 1.9.2.

⁵⁹ Cf. FAQ «Offenlegung der Inspektionsergebnisse der RAB gegenüber geprüften Publikumsgesellschaften» of 5.7.2012.

1.11 Points of focus for 2013 inspections

Within the scope of its regular inspections in 2013 the FAOA will set the following points of focus:

- Assessment of processes to ensure the implementation of Swiss Auditing Standards (SAS), 2013 edition;
- Compliance with independence requirements in connection with additional services;

2 International

2.1 Introduction

Given the increasing integration of the capital markets and the international audit networks, international cooperation is one of the main responsibilities of every audit oversight authority. This cooperation represents an important pre-condition for improving audit quality, increasing public confidence in audit reports and, lastly, for increasing investor confidence in the capital markets. In this regard, a trend from bilateral instruments of cooperation to multi-lateral forms of cooperation can be observed⁶⁰.

For the above reasons the FAOA intensified its international activities in 2012. Given the listing of Swiss entities on foreign exchanges and the inclusion of foreign entities on Swiss exchanges, various EU member countries, as well as the USA, are amongst the most important partners of the FAOA⁶¹. With the coming enactment of Article 8 AOA, however, the oversight authorities of further countries will also play a role⁶². The FAOA is therefore active in international organisations and committees⁶³ and makes timely contact with potential partner authorities. Finally, the translation of the FAOA regulations into English should serve to provide a better understanding of the Swiss oversight system abroad⁶⁴.

2.2 Relations with the European Union

2.2.1 Equivalence of the Swiss oversight system

Since the EU recognised the equivalence of the Swiss oversight system in January 2011, the oversight authorities of EU member countries have been free to complete agreements with Switzerland on specific cooperation. In October 2011 the first Memorandum of Understanding could be completed with the German Audit Oversight Commission (GAOC). In 2012 the FAOA has negotiated with various national oversight bodies from the EU and EEA. Negotiations with the oversight authorities of France and the Netherlands could be concluded successfully. Negotiations with other oversight authorities are continuing and will be completed in 2013.

2.2.2 Memorandum of Understanding with the Netherlands

In November 2011 the FAOA completed a Memorandum of Understanding with the Dutch Authority for the Financial Markets (AFM) on cooperation in the oversight of audit firms. The Memorandum does not have the force of a state treaty as it does not contain legally enforceable obligations.

Cooperation between national oversight authorities is very important in the oversight of global audit networks. At the same time, unnecessary duplication for audit firms is to be avoided. For this reason the FAOA and the AFM respect the oversight of audit firms within their home territories and waive their own oversight of those firms. This so-called «principle of home oversight» gives considerable relief to Swiss audit firms; cross-border inspections, such as those required by the PCAOB, are mutually waived. In addition, the registration process for audit firms from the respective countries is made as easy as possible.

⁶⁰ Cf. section 2.2.4.

⁶¹ Cf. section 2.2.2 f. and 2.3.1.

⁶² Cf. section 2.6.

⁶³ Cf. section 2.3.3, 2.4 and 2.5.

⁶⁴ Free download under www.revisionsaufsichtsbehörde.ch («Dokumentation»).

2.2.3 Memorandum of Understanding with France

At the end of 2012 the audit oversight authorities of France (H3C) and Switzerland (FAOA) also completed a Memorandum of Understanding (MoU) for the oversight of audit firms according to the principle of home oversight. France is thereby the third European Union (EU) member country with whom Switzerland has agreed such cooperation.

As with the other agreements with EU oversight authorities, and taking into account that audit networks are globally active, the MoU will help to improve audit quality, strengthen public trust in audit reports and improve the trust of investors in the financial markets. The FAOA and the H3C recognise the necessity of mutual cooperation, which is shaped by trust in the oversight activities of both countries. Accordingly, both authorities waive cross-border inspections and limit the information required for licensing auditors (individuals and legal entities) in their respective countries to that required for identification. This brings considerable relief to Swiss audit firms.

2.2.4 EAIG und Colleges of Supervisors

The FAOA has taken part in the meetings of the European Audit Inspection Group (EAIG)⁶⁵ since 2011. In addition, the FAOA hosted the EAIG meeting of November 2012, attended by over 40 representatives from the audit oversight authorities of the EU area. The EAIG analysed, amongst other things, anonymous findings from the inspections of member audit oversight authorities and executed a root cause analysis of the identified deficiencies. The results form the basis of follow-up meetings with representatives of the International Auditing and Assurance Standards Board (IAASB) and the International Ethics Standards Board of Accountants (IESBA). The FAOA, together with other EAIG members, also prepared and submitted a written comment on the regulatory proposals of the IAASB and IESBA⁶⁶.

In 2007 the national firms of KPMG in Germany, Great Britain and Switzerland joined to form KPMG Europe LLP (KPMG ELLP). KPMG ELLP is registered in London and has its head office in Frankfurt am Main. The firm provides no audit services. The aim of the combination is the more effective provision of services and the improved enforcement of uniform quality and independence standards in the regional

network. Hence, quality assurance processes are increasingly structured and monitored at the European level, though still implemented at a national level. Ernst & Young also strengthened their network structure at the European level with the foundation of Ernst & Young Europe Co LLP (EY ELLP).

Given the above-mentioned regionalisation of quality-relevant structures, the oversight authorities within the EU area decided to coordinate their cooperation as regards KPMG ELLP and EY ELLP within so-called Colleges of Supervisors. In a first step, interviews were held with the leadership of each ELLP. In a second step, experiences arising from the implementation of quality assurance processes within the individual countries are being exchanged. The FAOA supports this development and takes an active part in the Colleges. Only through multi-lateral cooperation will it be possible to achieve an effective and as uniform as possible oversight of international audit networks across national borders.

2.2.5 Registration of Swiss audit firms⁶⁷

Since the transitional period ended at the end of July 2010, the registration process for foreign audit firms has been approached very differently in the EU member countries. Certain EU member countries continue to waive the requirement for (also only minimal) registration. Other countries now conduct a registration process, as if the foreign audit firm had its registered office in the respective EU member country⁶⁸.

⁶⁵ Cf. FAOA Activity Report 2011, section 1.8.

⁶⁶ Cf. section 1.9.2.

⁶⁷ See Appendix 5 for an overview of Swiss audit firm registrations in the EU.

⁶⁸ Cf. FAOA Activity Report 2011, section 2.2.3.

Mutual recognition in the licensing area leads to discussion in the course of negotiating each Memorandum of Understanding⁶⁹. This is because neither the relevant EU Directive, nor the decisions of the EU Commission based on this Directive, require EU member countries to recognise third country licensing and oversight systems completely and to waive the exercise of national authority. While the laws of some EU member countries allow the waiver of registration requirements for Swiss audit firms, those of other countries do not. This situation is unsatisfactory from a Swiss point of view since it can lead to unwelcome duplication in the registration of Swiss audit firms. Where national regulations make mutual recognition impossible, a «best efforts» clause is agreed, under which the registration process is reduced to a minimum and duplication avoided.

2.3 Cooperation with the USA

2.3.1 Statement of Protocol and joint inspections

In 2011 the FAOA and FINMA agreed a Statement of Protocol (SoP) with the PCAOB for cooperation in the oversight of audit firms⁷⁰. Amongst other things, the SoP forms the basis for joint inspections at Swiss audit firms. As a direct result of this agreement with the PCAOB, Swiss audit firms were removed from the PCAOB's so-called «grey list»⁷¹.

After having already inspected two Swiss audit firms in 2011, accompanied by the FAOA and FINMA, the PCAOB inspected two further audit firms in 2012. Though involving considerable effort, the inspections to date have been completed without major problems for either the respective authorities or the audit firms. Procedures could be improved in 2012, based on the experiences of 2011. Under the current SoP one final inspection is planned for 2013. New negotiations will also be held in 2013, as the current SoP expires in April 2014.

2.3.2 Reliance

As mentioned, the SoP with the PCAOB expires in April 2014⁷². The question of PCAOB reliance on the work of the Swiss oversight authorities will be the central topic of the renegotiations. The PCAOB has already published a number of criteria that it wishes

to use in considering the nature and extent of reliance (adequacy and integrity, independence, financing, as well as transparency and services rendered)⁷³. The PCAOB will decide on a case by case basis if, and to what extent, reliance will be placed («sliding scale»). Partial reliance in the firm review area appears possible based on an evaluation of prior joint inspections. By contrast, the PCAOB has to date never placed reliance on a foreign oversight authority in the file review area.

Long-term, the FAOA is seeking the most far-reaching PCAOB reliance on the work of the Swiss oversight authorities possible. To achieve this aim, the FAOA intensified its cooperation with the PCAOB in 2012. On the one hand, coordination was increased in the firm review area during the joint inspections. On the other, the FAOA provided the PCAOB with a deep insight into its methodology and inspection processes. In 2013 the cooperation between the FAOA and the PCAOB will take a further step forward, in that they will inspect one audit engagement together. PCAOB feedback on the quality of the FAOA's oversight system is positive. According to the PCAOB, however, it does not currently have the legal foundation that would allow it to delegate the whole of its oversight activities to foreign authorities. The PCAOB's margin of discretion in the renegotiation of the SoP will be correspondingly limited.

⁶⁹ Cf. section 2.2.1.

⁷⁰ Cf. FAOA Activity Report 2011, section 1.4.2 and 2.3.

⁷¹ On 31.7.2009 the PCAOB published a grey list containing the names of those audit firms that could not be inspected by the due date. Since then the list has been updated every six months.

⁷² Cf. section 2.3.1.

⁷³ Cf. PCAOB Rule 4012, Inspections for Foreign Registered Public Accounting Firms.

2.3.3 PCAOB Regulatory Institute

In November 2012 representatives from the audit oversight and other authorities of 37 countries, including Switzerland, took part in the sixth PCAOB Regulatory Institute in Washington, D.C. The aim of the three-day conference was to provide an overview of current oversight systems and inspection techniques, to discuss questions of mutual interest and to foster an exchange of experiences. Furthermore, the conference allowed the FAOA to make contact with oversight authorities that are not yet members of IFIAR⁷⁴. As in 2011, the FAOA was invited to join a panel and, in particular, to present its oversight and inspection process and insights into its joint inspections with the PCAOB.

2.4 Relationship with other countries and organisations

In July 2012 Japan published criteria for establishing the equivalence of foreign audit oversight authorities and enacted specific provisions on the oversight of foreign-registered audit firms⁷⁵. In this connection, an update was made to the assessment of the Swiss oversight system begun in 2009⁷⁶. Earlier discussions regarding possible cooperation continued in 2012 but with no concrete results.

In December 2012 the FAOA welcomed representatives from the oversight authorities of Latvia, Poland, Slovenia and the Czech Republic and, over two days, provided them with an insight into the organisation and processes of the FAOA. The training was provided at the request of the World Bank within the framework of the Financial Reporting Technical Assistance Programme (FRTAP) for new EU member countries. The FRTAP is financed by the Swiss Enlargement Contribution, with which Switzerland takes an active part in reducing economic and social disparities within the enlarged European Union.

2.5 International Forum of Independent Audit Regulators

Founded in 2006, the International Forum of Independent Audit Regulators (IFIAR) had 44 members at the end of the year under review. The current President and Vice President are from the British Financial Reporting Council (FRC) and the American PCAOB respectively. The Chief Executive Officer of the FAOA acts as Treasurer. In 2012 IFIAR held plenary meetings in Busan (South Korea) and London, an Inspection Workshop in Abu Dhabi, and a first-time International Cooperation Workshop in London.

Within the scope of the regular exchange of ideas with representatives of the «Big 6», respectively the Global Public Policy Committee (GPPC), experiences were shared as regards recurring inspection findings. Particularly in the following areas, IFIAR members found potential for improvement:

- Professional scepticism of the auditor
- Group audit
- Revenue recognition
- Engagement quality control review
- Audit of internal control system
- Audit of estimates
- Consideration of quality in partners' compensation
- Auditor independence
- Using the work of an expert
- Application of Clarified ISAs

⁷⁴ Cf. section 2.5.

⁷⁵ JFSA and CPAAOB Guidance for Assessing the Equivalency of Audit and Public Oversight System of Foreign Jurisdictions (Download under <http://www.fsa.go.jp/en/news/2012/20120710-1.html>).

⁷⁶ Cf. FAOA Activity Report 2009, section 4.4.

Further important topics of the IFIAR Plenary Meetings were exchanges of ideas with investor representatives, as well as developments in the auditing standards area and the related regular dialogue with the IAASB and IESBA.

IFIAR remains an important platform for the FAOA, allowing contact with other oversight authorities and the opportunity to discuss different oversight strategies and their implementation in an international context. The FAOA involved itself in IFIAR debates at various levels in 2012:

- As a member of the International Cooperation Working Group (ICWG), the FAOA assisted in the organisation of a half-day workshop on the question of international cooperation and brought Swiss experiences to the panels «Overview of experiences with sharing audit inspection reports with other regulators and accessing audit workpapers in other jurisdictions, including limitations on, and barriers to, sharing of information between regulators», and «Regional supervisory colleges».
- The FAOA is also a member of the Standard Coordination Working Group (SCWG). The aim of this working group is to exchange ideas on current international standard-setting and to communicate to the IAASB and IESBA the experiences oversight authorities have had concerning the implementation of, and compliance with, current standards. In 2012 the SCWG addressed the following focus areas:
 - Improving the Auditor's Report;
 - ISA 720 «the auditor's responsibilities relating to other information in documents containing audited financial statements»;
 - ISA Implementation Project;
 - Auditor Rotation;
 - IAASB Audit Quality Project;
 - IESBA – «Breach of a Requirement of the Code»;
 - IESBA Strategy and Work Plan;
 - IESBA – «Proposed changes to the Code of Ethics for Professional Accountants addressing conflicts of interest»;
 - IESBA – «Proposed changes to the Code of Ethics Definition of Engagement Team»;
 - IESBA – «Illegal Acts»;
 - Professional Scepticism; as well as
 - Preparation for meetings between IFIAR and the Chairman of the IAASB.

– The Inspection Workshop dealt, amongst other things, with regulatory challenges concerning audit effectiveness, auditor independence and the effects of fee pressure on audit quality. Current audit-related topics from the various IFIAR working groups were analysed and discussed within numerous inter-active workshops, some chaired by the FAOA. The participant group is confined particularly to inspectors with direct audit firm oversight experience. It is therefore possible to have discussions at a high technical level, which serves the FAOA in developing and refining its inspection activities. The next Inspection Workshop will be organised by the FAOA and held in Switzerland in 2013.

2.6 Extra-territorial scope of the AOA

In line with comparable regulations in the USA, the member states of the EU and other countries, the Audit Oversight Act (AOA) displays certain extra-territorial properties. Accordingly, the auditors of foreign companies who draw directly or indirectly on the Swiss capital market also require a licence as a state-regulated audit firm. The scope of audit oversight at home (Art. 727 para. 1 section 1 CO) is thereby reproduced internationally. Article 8 AOA forms the basis of this extra-territorial scope and is currently not yet in force.

The extra-territorial scope of the AOA results in the auditor of an international group being subject to the audit oversight of several countries. To avoid duplication, the legislator decided to waive FAOA licensing and oversight requirements with respect to foreign audit firms in two cases:

- First, where a foreign audit firm is subject to oversight by a foreign audit oversight authority recognised by the Federal Council (Art. 8, para. 2 AOA).
- Secondly, where outstanding bonds are guaranteed by a company whose auditor is subject to Swiss audit oversight or oversight by a foreign oversight authority recognised by Switzerland (Art. 8 para. 3 AOA)⁷⁷.

⁷⁷ Bonds are often issued by issuers domiciled «off-shore» but guaranteed by a parent company domiciled «on-shore». Investors are not disadvantaged as the bonds are fully guaranteed by the parent company and thereby subject to audit oversight: Federal Council Message of 23.6.2004 on the amendment of the Swiss Civil Code (audit requirement under corporate law), as well as the Federal Law on the licensing and oversight of auditors, BBl 2004 4068.

If the auditor of an international group does not fall under the above exceptions that auditor must be licensed and subject to oversight in Switzerland. Failing this, the SIX Exchange Regulation (SER) de-lists the relevant securities, respectively sanctions the issuer (Art. 8 para. 3^{bis} SEA in conjunction with Art. 13 of the listing regulations).

As already mentioned, Article 8 AOA is yet to be enacted. From practical experience gathered over the last five years it is apparent that the oversight systems of the respective countries are very heterogeneous and that the oversight authorities of various countries probably cannot be recognised by Switzerland: In certain countries there is either no oversight authority or there are serious doubts as to whether the existing authority can be recognised. It is to be assumed, therefore, that more foreign audit firms will fail to meet exception conditions (Art. 8 para. 2 and 3 AOA) and consequently fall under the direct oversight of the FAOA than was originally anticipated by the legislator. The exercise of oversight authority abroad may certainly come up against political, legal and practical difficulties. Being licensed as a state-regulated audit firm and being inspected abroad by the FAOA will involve certain costs for the foreign audit firm, and indirectly also for the listing of shares and bonds in Switzerland. This can have consequences for the attractiveness of the Swiss capital market. On the other hand, Swiss capital market investors also have the right to expect an audit that meets international standards if the company in which they invest is registered abroad.

The interests of investor protection, the exercise of effective and efficient oversight and the competitiveness of the Swiss capital market are therefore, to a certain extent, in conflict with one another. These interests must be accommodated through a differentiated approach to state oversight.

After considering various options at the legal ordinance level, and after consultation with the Federal Department of Justice, it was decided that a partial amendment of the law would provide a more expedient way of achieving a sound arrangement with respect to the extra-territorial scope of the AOA. The planned partial amendment to Article 8 AOA is likely to include the following:

- Abolishment of oversight over audit firms auditing significant subsidiaries of foreign-registered public companies;
- Clarification that issuers of non-listed bonds are not required to appoint a state-regulated auditor;
- Licensing as a state-regulated audit firm also upon meeting equivalent foreign licensing conditions;
- Introduction of a provisional licensing procedure for foreign-registered audit firms;
- Option of limiting the oversight of foreign audit firms to file reviews, i.e. for those audit engagements relevant to the Swiss capital market.

As mentioned, the amendment of Article 8 AOA is being managed by the Federal Department of Justice. The amendment will be made within the framework of another legislative project, which concerns the modernisation of the commercial register. The relevant draft law was submitted for consultation on 19 December 2012, the consultation ending on 31 March 2013.

3 Licensing

3.1 Introduction

In the year under review the FAOA recorded a total of 507 new licences. As in prior years, an increase in the number of applications was noted after the completion of each examination entitling an FAOA licence.

In the licensing area the focus lay, however, on preparatory work for the forthcoming renewal of audit firm licences.

3.2 Statistics

3.2.1 Licences

Figure 4:

Licensed individuals and audit firms as at 31 December 2012⁷⁸

Type of licence	Auditor	Audit expert	Total at 31.12.2012	Total at 31.12.2011
Individuals	2,271	5,737	8,008	7,696
Sole proprietorships	385	463	848	854
Audit firms	900	1,866	2,766	2,707
State-regulated audit firms ⁷⁹	–	21	21	21
Total licences	3,556	8,087	11,643	11,278

In the year under review 25 applications were rejected. 12 applicants withdrew their applications. Seven applications were not proceeded with on the grounds of incomplete documentation. In addition, 23 licence withdrawals were imposed and six reprimands issued.

At the end of the year under review three individuals and eight audit firms still held provisional licences. The majority of these cases involve on-going appeal proceedings at the Federal Administrative Court or Federal Supreme Court and can, therefore, only be resolved or at least taken further upon a court decision. Another part relates to applications from individuals with foreign qualifications, the evaluation of which is time consuming (cf. section 3.7). By contrast, the two state-regulated audit firms holding provisional licences last year could be licensed definitively. Therefore, all state-regulated audit firms now hold definitive licences.

⁷⁸ All numbers refer to legally binding completed proceedings. Pending appeals are not included. The determining factor is therefore the status of the licensing process as per the end of 2012.

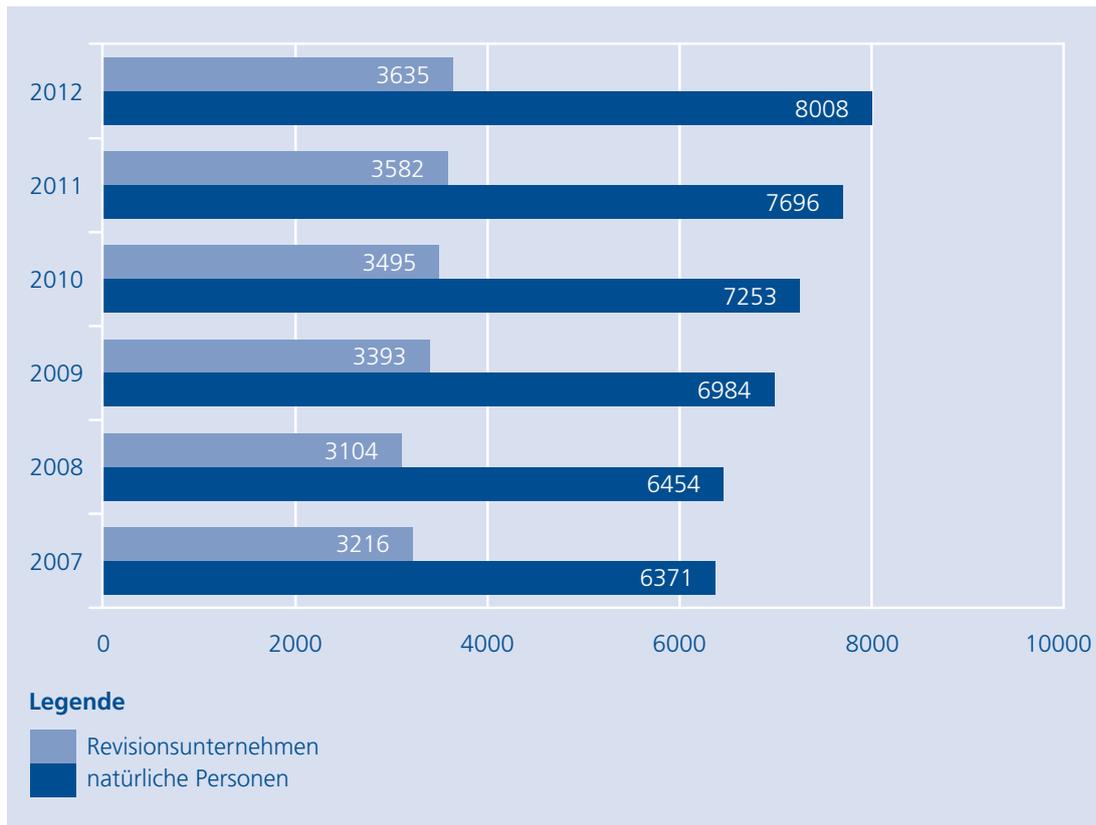
⁷⁹ Cf. Appendix 4.

3.2.2 Development of licences

Since the FAOA began its operating activities on 1 September 2007, the number of licences held by individuals and audit firms has developed as follows:

Figure 5:

Status as at 31 December 2012



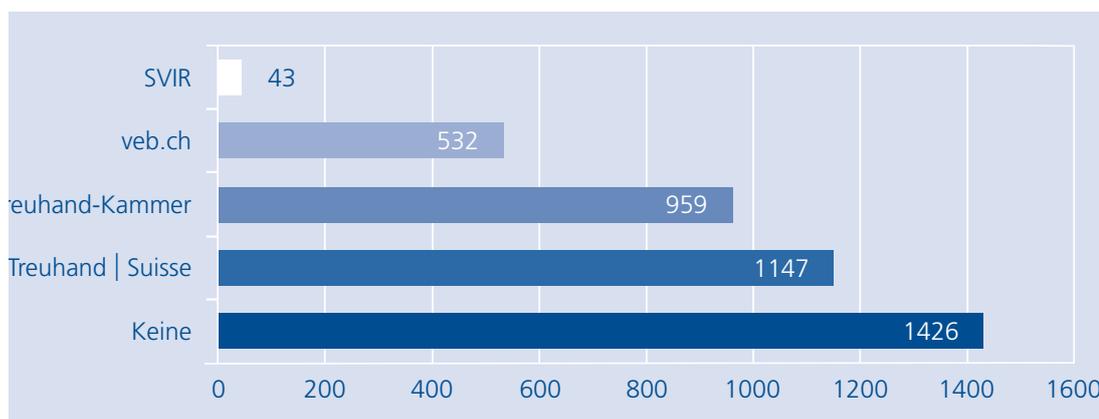
3.2.3 Memberships of professional associations

Licensed audit firms entered their respective professional association memberships on-line. The membership can be seen in the public FAOA register. Many audit firms have dual memberships. It is to be noted that a relatively large number of audit firms (1,426) do not belong to a professional association and are therefore not subject to the monitoring of an association with respect to compliance with training requirements.

The self-declarations provide the following statistics:

Figure 6:

Status as at 31 December 2012



3.3 Amendment of legal foundations

The new licensing system⁸⁰ is also linked to an amendment of the legal foundations within the Auditor Oversight Ordinance (AOO) and Circular 1/2007.

The Federal Council enacted the relevant amendment to the AOO with effect from 1 December 2012⁸¹. In particular, the requirements relating to internal quality assurance were thereby amended. Audit firms are legally required to ensure the quality of their work through a system of internal measures⁸². Following the significant increase in the thresholds separating the less rigorous limited audit (so-called «KMU-audit») from the ordinary audit⁸³, the question as to the importance of quality assurance has to be answered in a differentiated way.

It is no longer justifiable to make concessions on internal quality assurance for audit engagements above the threshold in view of their size and complexity, as well as the economic significance of the respective audited entities. Given this, all audit firms performing ordinary audits must have a quality assurance system meeting professional standards by 15 December 2013. The deadline coincides with the enactment of the relevant updated professional regulations⁸⁴ of the Association of Swiss Certified Public Accountants.

⁸⁰ Cf. section 3.6.

⁸¹ Cf. «Amtliche Sammlung des Bundesrechts», Nr. 47 of 20.11.2012, page 6071 f.

⁸² Cf. Art 6 para. 1 indent d AOA.

⁸³ Instead of the thresholds of CHF 10 million balance sheet total, CHF 20 million sales and 50 full-time employees averaged over the year, as from 1 January 2012 the new criteria of CHF 20 million balance sheet total, CHF 40 million sales and 250 full-time employees averaged over the year apply.

⁸⁴ Cf. section 1.9.

Audit firms having only one licensed professional and performing only limited audits remain exempt from an obligation towards quality assurance until 1 September 2016. The legislator must, in the meantime, decide whether to establish the legal basis for a peer-review system or rather abolish the audit obligation for entities subject to limited audit. A corresponding submission is included in the above-mentioned consultation of 19 December 2012, which runs until 31 March 2013.

Various other amendments provide mainly for clarity, efficiency and flexibility in the application of the law. Thus, for example, Art. 21a AOO now describes the cases in which licence transfer is possible. Further, the new Art. 22a AOO governs the process for correcting an entry to the register where this does not, or no longer continues to, reflect the facts or the legal position, and the individual or audit firm has not made the correction or reported it.

FAOA Circular 1/2007 was amended to take account of the amendments to both the Audit Oversight Ordinance and the licensing system⁸⁵ and was enacted by the Board of Directors of the FAOA on 1 December 2012.

3.4 Transparency in the register of auditors regarding quality assurance

A further amendment to the Audit Oversight Ordinance coming into force on 1 December 2012, concerns the public register of the FAOA. In the future, the market should decide whether it attaches importance to an internal, respectively external, quality assurance system. The entry made by licensed audit firms has been extended accordingly and now includes details as to the standards under which the internal quality assurance system is operated, as well as the nature of external quality assurance. If no quality assurance system is implemented, an appropriate reference also appears. Any interested party can therefore obtain information as to how the audit firm ensures the quality of its work.

3.5 Licence renewal

3.5.1 General

The Audit Oversight Act (AOA) stipulates that audit firms are licensed for a period of five years (Art. 3 para. 2 AOA). The granted licence expires automatically at the end of these five years. For this reason timely action should be taken towards renewal before the end of the expiry period. By way of a service, the audit firms concerned will be informed by the FAOA around six months before licence expiry. The active participation of audit firms is particularly important in ensuring the efficient and timely handling of the renewal application. To raise the timely awareness of firms in this regard, the FAOA has given various presentations across Switzerland, and published an article in the professional journals «Schweizer Treuhänder» and «Trex»⁸⁶.

The FAOA granted the first definitive audit firm licences at the beginning of 2008. Therefore these expire at the beginning of 2013. The FAOA already informed the first of the firms before the end of 2012. In the course of the renewal process, audit firms seeking renewal are asked to enter the necessary details on-line, within the web-based licensing system, and to send the required documentation. To avoid unnecessary expense the FAOA asks for an appropriate notification from firms not wishing to renew their licences, and thereby not wishing to provide statutory audit services in the future. In this case the licence expires automatically at the end of the five year period. Where the licence is renewed early, the new five year period begins at the end of the previous licence period.

⁸⁵ Cf. section 3.6.

⁸⁶ Cf. Schneider/Derada, *Erneuerung der Zulassung von Revision-
sunternehmen – Erfüllung der gesetzlichen Anforderungen als
oberstes Ziel*, in: *Der Schweizer Treuhänder* 2011, 790 f. (German
version), 794 f. (French version), and *TREX, Der Treuhänder-
experte*, 5/11, 284 f. (German version), 288 f. (French version).

Figure 7:

Expiry of definitive audit firm licences (excluding state-regulated audit firms), status as at 31 December 2012

Expiry date	Auditor licence	Audit expert licence	Total
2013	132	352	484
2014	699	1307	2006
2015	304	482	786
2016	95	119	214
2017	53	63	116

The statutory licensing requirements for audit firms are set out in Article 6 AOA and apply irrespective of whether a first-time or renewed licence is concerned. The licensing conditions are divided between individual-related requirements (indents a–c) on the one side and organisational requirements for the audit firm (indent d) on the other.

In general, the depth of the application check is risk-based. A risk-based approach allows the work of the FAOA to be targeted, effective and efficient. As a rule, an ordinary audit is considerably more complex than a limited audit. The volume of professional standards and the related risk of error are significantly higher for an ordinary audit. Public interest in ordinary audits is also greater since the economic consequences of audit failures at companies over the thresholds are more significant. The risk-based approach of the FAOA generally leads to the details of auditors who perform ordinary audits being checked more thoroughly.

3.5.2 Individual-related requirements

Quota checks⁸⁷ are generally systems-based, using the data contained within the web-based FAOA-licensing system. The FAOA aims to test compliance with quotas in detail on a sample basis. In the most likely rare cases where there is a suspicion that the law has been circumvented the FAOA can carry out additional investigations. In this context, it is conceivable that an audit firm may employ licensed individuals on a pro-forma basis in order to feign compliance with quotas.

3.5.3 Organisational requirements

The crux of the licence renewal is the verification of compliance with quality assurance system requirements. Such a system aims to continually improve audit quality and thus minimise (liability) risk. The FAOA will verify the information supplied with respect to the quality assurance system and request additional information and documentation should ambiguities or contradictions be noted. The areas of independence, training and internal monitoring will be closely examined.

3.6 New licensing system

The web-based licensing system of the FAOA was implemented under time pressure in 2007. Although the FAOA managed the flood of licence applications efficiently, numerous minor changes have been made since then. Due to this and collected past experience, the FAOA decided to update its licensing portal with the coming renewal of audit firm licences. The new system is expected to go live before mid-2013.

The new system includes the following changes:

- All external and internal FAOA services will be offered, taken up and executed through processes within the FAOA-portal. The portal will be constructed in a customer-friendly, simple and clear way.
- Document submission – from the licence applicant to the FAOA and vice versa – will be through an up-/download mechanism, which can automatically track and keep a history of when, and at what time, a document was up/downloaded.

- The user guide will be integrated directly within the log-in process, such that relevant information appears on the respective input page.

- The system will be constructed such that entries generally need only be made once. For example, if the licence applicant has to submit additional documentation (evidence of professional practice), existing details (surname, first name etc.) will be integrated directly within the relevant form (so-called intelligent pdf) when it is opened.

- Further, an interface to the UID-Register⁸⁸ will be created, through which all of the information within the UID register that is required by the FAOA will be imported directly to the relevant input pages.

- The individual or audit firm has constant access to the status of their application and the contact details of the FAOA employee responsible.

A further significant change concerns information as to the function of individuals employed by the audit firm. Until now function links were entered in the on-line entries of individuals. These links were not always updated on a timely basis, particularly with respect to leavers. The firm had neither the access to such links nor the capability to update them. As mentioned in section 3.5.2, an audit firm must meet certain requirements relating to individuals. It can only adhere to these requirements if it has the necessary information and authority. For this reason, in the new system the firm itself, and not the individual, will input function links. Existing links will be migrated to the new system, such that the audit firm will need only to update or add to the details, if applicable. The new system provides real added value to both customers and FAOA employees.

⁸⁷ See Art. 6 para. 1 indents a–c. AOA.

⁸⁸ Specific company identification number (UID); Cf. www.uid.admin.ch.

Affected audit firms will be requested to supply necessary information and documentation around half a year prior to licence expiry. Since the first licence renewals are due in March 2013 and the new system is only expected to go live in the Spring of 2013, it is probable that the first licence renewals will be processed and checked on the old system. Information which is not available in the old system (namely, questions on quality assurance and information on individuals employed by the firm, including function) will be requested as documents. All data and documents in the old system will be correctly transferred to the new system. Hence, no additional efforts will be required on the part of the firms concerned.

3.7 Individuals with a foreign education

The assessment of licence applications from individuals with a foreign education is, and will remain, highly time consuming⁸⁹. The assessment of the equivalence of a foreign qualification to a relevant Swiss qualification and the investigation as to whether the country from which the qualification originates offers (substantial) reciprocity are difficult.

The FAOA decides whether a foreign educational course is comparable to a Swiss one according to administrative discretion. However, this discretion relates solely to the question of whether the foreign education is equivalent to one of the Swiss qualifications shown within the definitive legal catalogue of Art. 4 para. 2 AOA. The list of recognised qualifications is therefore definitive in international terms.

The principle of reciprocity is a general basic principle of international law that allows a country to make its behaviour dependent on the behaviour of another country, where the other country behaves towards it in the same way in the same situation⁹⁰. The reciprocity requirement aims to ensure that those holding Swiss educational qualifications have the possibility to establish themselves abroad. In contrast to the other licensing conditions of the AOA, the requirement for reciprocity therefore has an economic rather than trade regulation character. In this connection, the ruling of the Federal Supreme Court that the USA does not offer reciprocity to Switzerland as regards the licensing of audit experts is notable⁹¹.

In the year under review the FAOA was able to license individuals with qualifications from additional countries. The list of equivalent foreign educational qualifications is at Appendix 6.

⁸⁹ Foreign licence applicants who hold a foreign educational qualification equivalent to a recognised Swiss qualification (Cf. in addition Art. 4 para. 2 indents a to c AOA), have appropriate professional experience and can demonstrate the necessary knowledge of Swiss law, satisfy the educational and professional experience conditions, in so far as this is provided for in a state treaty with the country of origin or the country of origin grants reciprocity (Art. 4 para. 2 indent d AOA).

⁹⁰ Cf. FSC Decision 109 Ib 168, E. 5.

⁹¹ Cf. FSC Decision 2C_895/2011 of 10.4.2012, E. 2.2, as well as section 4.2 below.

3.8 Auditor independence

3.8.1 General

Auditor independence is one of the core corporate governance principles, serving both investor protection and the protection of the public interest, minority shareholders and creditors. Independence is therefore a central concern of audit oversight and of professional and statutory law⁹².

According to the law, the auditor must be independent and must form his or her audit opinion objectively (Art. 728 para. 1 and Art. 729 para. 1 CO). Independence must not be impaired either in fact or appearance. Breaches of independence in appearance are to be judged according to the same criteria as breaches of independence in fact⁹³. Compliance with independence requirements within the framework of ordinary and limited audits is manifestly relevant to compliance with licensing conditions, the good reputation of the auditor, respectively audit expert, and for the assurance of proper audit services.

The same auditor independence requirements apply to limited and ordinary audits. For limited audits, however, the legislator does make exceptions with respect to accounting assistance, the provision of other services (Art. 729 para. 2 CO)⁹⁴ and partner rotation (Art. 730a para. 2 CO).

In the year under review, as in prior years⁹⁵, the FAOA found repeated breaches of independence⁹⁶. Given the importance of independence to the profession, the FAOA will again pay particular attention to compliance with independence requirements in 2013.

3.8.2 Accounting assistance and the limited audit

Where the same audit firm provides accounting assistance and performs a limited audit independence is under particular threat. Audit firms that offer so-called dual mandates⁹⁷ must therefore select the safeguards necessary to guarantee a reliable audit at all times.

In July 2011 the FAOA published an FAQ⁹⁸ presenting the most important principles to be followed when conducting dual mandates. According to this, it is permissible to provide accounting assistance when performing limited audits, provided that the audit firm takes the appropriate organisational and staffing measures to ensure a reliable audit. Besides this, the audit firm must ensure that it only assists in the preparation of the financial statements and that the Board of the audited entity remains responsible for all critical matters of approach.

This subject was also further debated in 2012. During the course of various presentations and seminars, the FAOA thus explained the principles to be followed in conducting dual mandates, presented various case studies and described possible practical approaches. From the discussions at these events it can be concluded that staff segregation presents few difficulties in practice. With respect to organisational segregation, however, the question is often how the audit firm can ensure that the individual providing accounting assistance has no managerial authority over the individual performing the limited audit. Reference is made in this regard to the profession which, during 2012, presented a practical approach to the problem in the form of a set of specimen regulations⁹⁹. The question of whether staff and organisational segregation has to be assured at the engagement or company level has also led to discussions.

⁹² FAC Decision No. B-5065/2011 of 3.5.2012, E. 3.5.

⁹³ FSC Decision No. 2C_9272807 of 8.5.2012, E. 3.2.2; FAC Decision No. B-739/2011 of 6.9.2012, E. 3.3.4.

⁹⁴ Cf. FAQ on «Unabhängigkeit der Revisionsstelle bei der eingeschränkten Revision» of 18.7.2011 and FAOA Activity Report 2011, page 40.

⁹⁵ Cf. FAOA Activity Report 2011, pages 39 f.

⁹⁶ Cf. also in addition section 4.2.

⁹⁷ Accounting assistance and limited audit provided by the same audit firm or, as the case may be, the same group of firms.

⁹⁸ Cf. FAQ on «Unabhängigkeit der Revisionsstelle bei der eingeschränkten Revision» of 18.7.2011.

⁹⁹ Cf. «Reglement für die organisatorische Trennung von Revision und Buchführung und das Erbringen von anderen Dienstleistungen of the Schweizerischen Instituts für die eingeschränkte Revision (Treuhand I Suisse)».

In a further FAQ¹⁰⁰, the FAOA stated that independence requirements also apply to companies under the same management as the company under audit or the auditor (Art. 728 para. 6 CO). Accounting assistance in the course of an ordinary audit is therefore incompatible with auditor independence in all cases. This stipulation applies not only to the ultimate holding company but also to every other entity that is under the same management as the ultimate holding company or the auditor. Accordingly, it is incompatible with independence requirements for the auditor to provide accounting services to a subsidiary of an entity subject to ordinary audit by that auditor. This applies irrespective of whether the subsidiary is considered a significant or non-significant component from a Group audit perspective, or whether the component would require only a limited audit, or no audit at all (opting-out), on a stand-alone basis.

Within the scope of its oversight activity the FAOA had findings at two state-regulated audit firms that related to accounting assistance and the performance of a limited audit. In one case, the FAOA found that in providing accounting assistance the audit firm had gone beyond a permissible level and had prepared significant parts of the financial statements itself. Besides this, the audited entity had not been adequately informed as to the risks associated with dual mandates. In the other case, the FAOA criticised the fact that the internal regulations of the audit firm concerned did not explain the principles

relating to the provision of accounting assistance appropriately. Finally, the FAOA withdrew the licence of an individual, based on third party information, because that individual had failed to report an obvious case of over-indebtedness and had not ensured sufficient organisational segregation in the course of conducting dual mandates.

In the course of the licence renewal process, starting in 2013, the FAOA will ask audit firms for information as to whether they conduct dual mandates and, if applicable, what safeguards they have put in place. Based on this information, the FAOA will assess whether the requirements relating to accounting assistance and the limited audit have been adequately taken account of in the quality assurance system of the firm¹⁰¹.

¹⁰⁰ Cf. FAQ on «Erbringung von Revisionsdienstleistungen und Mitwirkung bei der Buchführung im Konzernverhältnis» of 6.6.2012.

¹⁰¹ Cf. also in addition section 3.5.3.



4 Court rulings

4.1 Introduction

In 2012 the federal courts (Federal Administrative Court [FAC] and Federal Supreme Court [FSC]) most particularly addressed cases in which good reputation did not exist or was no longer given. Seven decisions were reached in this area and all confirm FAOA practice. Four cases related to lack of auditor independence, two related to audit reports that were issued without the required licence and one related to a lack of financial stability.

Further, the FAC ruled on the required knowledge of Swiss law and, in two decisions, on the application of the hardship clause. Finally, the FSC confirmed and clarified its adjudication on the reciprocity conditions applying to licence applicants with a foreign education.

In the following section 4.2 only the most important deliberations of the federal courts on the interpretation of licensing conditions are commented upon. A full list of the decisions issued, with particular information on the subject matter covered, is in section 4.3.

4.2 Important court decisions

According to the FAC, an auditor breaches independence requirements if he audits, for more than ten years, the financial statements of an entity that he works for and in which his wife is the only member of the Board of Directors. Such breaches called good reputation into question even though proper conditions were restored through opting-out, following the enactment of the new audit law. In such a case the FAOA may refuse to grant a licence and reconsider this decision, at the earliest, two years after the date upon which the decision became legally enforceable¹⁰².

The FAC came to the same conclusion in the case of an applicant who had worked under sub-contract for an entity whose financial statements she had audited for many years. She subsequently relinquished the audit of the entity but took a seat on its Board of Directors whilst the entity was audited by an individual who supervised her. With the decision referred to¹⁰³, the FAC clarified that economic dependence can arise not only from audit engagements but also from other circumstances. Although the size of permissible fees is only defined for state-regulated audit firms (10 per cent, cf. in addition

Art. 11 para.1 indent a AOA), it can also be used for other audit firms (in the present case an average of 13.2 per cent). In addition, the relief provided with respect to independence in the case of limited audits was limited to accounting assistance and suitable measures to avoid self-audit (Art. 729 para. 2 CO), as well as the absence of a limitation for the auditor-in-charge (Art. 730a para. 2 CO). Except for these two exceptions, the term independence is applied in equal measure, without regard to the type of audit performed (ordinary or limited)^{104,105}. The size of the audited entity is not relevant and there is no reason to qualify the effect on good reputation solely because the detected breach of independence was in appearance only. Finally, the FAC underlined that good reputation could only be assessed on a specific case and a comparison with cases decided upon earlier was consequently only of marginal relevance¹⁰⁶.

The FAC then confirmed the refusal of the FAOA to grant a licence to an applicant against whom payment enforcement orders for over CHF 4 million had been issued, including threatened bankruptcy proceedings for over CHF 220,000 and the attachment of assets for debts of over CHF 228,000. It noted that the lack of financial stability and the prospect of bankruptcy raised doubts as to the ability of the applicant to provide sustained audit services. In addition, the FAC considered that debts of such magnitude, compared to the financial assets of the applicant, may make the possibility apparent to third parties that the auditor will accept as many engagements as possible and not perform these engagements with the care and seriousness that could be expected of him¹⁰⁷. The court agreed with the view of the FAOA that any future licence could only first be granted four years after the decision had become legally enforceable, and provided that the financial situation of the applicant had improved by then¹⁰⁸.

¹⁰² FAC Decision No. B-5065/2011 of 3.5.2012, E. 4.

¹⁰³ FAC Decision No. B-739/2011 of 6.9.2012, E. 3.3.1.

¹⁰⁴ FAC Decision No. B-739/2011 of 6.9.2012, E. 3.2.3.

¹⁰⁵ FSC Decision No. 2C_927/2011 of 8.5.2012, E. 3.5.1.

¹⁰⁶ FAC Decision No. B-739/2011 of 6.9.2012, E. 3.3.4.

¹⁰⁷ FAC Decision No. B-8823/2010 of 13.6.2012, E. 5.4.2.

¹⁰⁸ FAC Decision No. B-8823/2010 of 13.6.2012, E. 5.6.

The FAC further took the view that a one year licence withdrawal was reasonable in the case of an individual with simultaneous decision-making roles within an audit firm and an audited entity, even if that individual had not prepared the audit report personally. This constellation is obviously not compatible with independence. According to Art. 728 para. 3 CO, this also applies to an applicant in his capacity as a member of the Board of Directors or Executive Board¹⁰⁹. The court further clarified that the law did not permit exceptions with respect to the simultaneous exercise of a decision-making role within the audited entity and the auditor of that entity, even if a particular structure was chosen or if the relevant individuals were briefed on the matter¹¹⁰.

The FAC also confirmed a one year licence withdrawal in the case of a licensed individual who had audited the financial statements of an employer foundation, the audit of which requires an audit expert licence. The court remarked in this regard that the provision of Art. 40 para. 1 indent a AOA¹¹¹ covered not only an audit without any licence but also an audit in which the relevant individual holds a licence but not the one required by law. This applies particularly to the case in which an auditor performs an audit which is reserved for audit experts. In addition, the court clarified that in such cases auditors must track the development of legal provisions applying to their profession; a recent change in the law cannot excuse the committed breach. The arguments of the licensed individual that legal conformity had been restored and that the employer foundation had continued to place its trust in him are, on the other hand, not important¹¹².

Finally, the FSC had to deal with the question of reciprocity in terms of Art. 4. para. 2 indent d AOA¹¹³ and came to the conclusion that the USA did not offer reciprocity to Swiss auditors and also that no relevant state treaty existed. It added that the hardship clause (cf. Art. 43 para. 6 AOA and Art. 50 AOO) was not relevant in this case as these provisions applied only to professional experience¹¹⁴.

¹⁰⁹ FAC Decision No. B-853/2011 of 27.7.2012, E. 4.3.1.

¹¹⁰ FAC Decision No. B-853/2011 of 27.7.2012, E. 4.3.2.

¹¹¹ Under this provision, those providing an audit service without the appropriate licence, or in spite of a prohibition against performing their work, are subject to a custodial sentence of up to three years or a fine.

¹¹² FAC Decision No. B-1723/2011 of 24.10.2012, E. 4.3 and 5.2.

¹¹³ According to this provision, individuals satisfy the educational and professional experience conditions if they hold one of the equivalent foreign educational qualifications listed under indents a, b or c of Art. 4 para. 2 AOA, have appropriate professional experience and can demonstrate the necessary knowledge of Swiss law, in so far as this is provided for in a state treaty with the country of origin or the country of origin grants reciprocity.

¹¹⁴ FSC Decision No. 2C_895/2011 of 10.4.2012, E. 2.2 and 2.3.

4.3 Complete list of court decisions

As mentioned under section 4.1 above, it is useful to list the decisions of the federal courts with respect to the interpretation of licensing conditions. The decisions issued in 2012 appear in chronological order, with a short note on the subject matter dealt with and the conclusions of the court.

- FAC Decision No. B-1872/2011 of 27 February 2012: In relation to the examination concerning necessary knowledge of Swiss law, it is not discriminatory for the «Akademie der Treuhand-Kammer AG» to hold non-mandatory preparatory courses in English only. Dismissal of appeal by the FAC.
- FAC Decision No. B-6714/2010 of 13 March 2012: Application of hardship clause. Approval of appeal by the FAC and granting of audit expert licence.
- FSC Decision No. 2C_895/2011 of 10 April 2012: Lack of reciprocity on the part of the USA. Hardship clause not applicable as issue relates to education. Dismissal of appeal by the FSC.
- FAC Decision No. B-5065/2011 of 3 May 2012: Breach of independence requirements (audit of an entity whose sole Board Director is the wife of the auditor). Rejection of licence application. Dismissal of appeal by the FAC.
- FSC Decision No. 2C_927/2011 of 8 May 2012: Breach of independence requirements (direct and indirect interest in the audited entity, close relationship with a member of the Board of Directors and significant shareholder of the audited entity). Three year licence withdrawal. Dismissal of appeal by the FSC.
- FAC Decision No. B-8823/2010 of 13 June 2012: Financial instability and audit by an unlicensed audit firm. Rejection of licence application. Dismissal of appeal by the FAC.
- FAC Decision No. B-5113/2011 of 28 June 2012: Audit by unlicensed auditor. Rejection of licence application. Dismissal of appeal.
- FAC Decision No. B-853/2011 of 27 July 2012: Breach of independence requirements (simultaneous decision-making position within audit firm and audited entity). One year licence withdrawal. Dismissal of appeal.
- FAC Decision No. B-739/2011 of 6 September 2012: Breach of independence requirements (economic independence, close relationship). Rejection of licence application. Dismissal of appeal by the FAC.
- FAC Decision No. B-1723/2011 of 24 October 2012: Audit of an employer foundation by an auditor and not an audit expert as required. One year licence withdrawal. Dismissal of appeal by the FAC.
- FAC Decision No. B-5830/2011 of 31 December 2012: Insufficient professional experience for the granting of an audit expert licence. Anti-money laundering audits not equivalent to the audit of financial statements. Conditions for application of hardship clause not met. Licence as auditor. Dismissal of appeal by the FAC.

Appendices

1 Organisation of the FAOA

Legal form	Public-law institution with separate legal identity	
Relation with the government administration	Independent unit within the decentralised government administration, organisationally attached to the Federal Department of Justice and Police (FDJP)	
Registered office	Berne	
Representative bodies of the FAOA	Board of Directors	Thomas Rufer (Chairman) , Graduate in Business Administration and Swiss Certified Accountant
		Sabine Kilgus (Vice-Chairman) , PD Dr., lawyer
		Renato Fassbind , Dr., US CPA
		Conrad Meyer , Prof., Dr.
		Daniel Oyon , Prof., Dr. Further information is available on the website of the FAOA
	Executive Board	Frank Schneider , Chief Executive Officer and Head of Oversight, Swiss Certified Accountant
		Reto Sanwald , Head of Legal & International, Dr. iur., attorney
Sébastien Derada , Head of Licensing & Support		
Auditor	Swiss Federal Audit Office (SFAO)	
Number of staff	26 employees, representing 20 full-time equivalents (position 31.12.2012). At the end of the prior year 25 employees, representing 18.4 full-time equivalents, were employed by the FAOA.	
Funding	The FAOA is financed entirely from the fees and oversight charges levied on licensed individuals and audit firms under oversight. No taxpayers' money is used. The FAOA maintains its own accounts outside the Federal budget.	
Legal function	To ensure the proper provision and quality of audit services.	
Responsibilities	Appraisal of licence applications, oversight of the auditors of public companies, accomplishment of international administrative assistance in the audit oversight area.	
Independence/Oversight	The FAOA performs its oversight activities independently but is subject to the oversight of the Federal Council. It reports annually to the Federal Council and the Federal Assembly on its activities.	

2 Index of abbreviations

AFM	Authority for the Financial Markets
AOA	Audit Oversight Act of 16 December 2005 (SR 221.302)
AOO	Audit Oversight Ordinance of 22 August 2007 (SR 221.302.3)
BBI	Federal Law Gazette
CO	Swiss Civil Code of 30 March 1911 (SR 220)
EAIG	European Audit Inspection Group
EQCR	Engagement Quality Control Reviewer
EU	European Union
FAC	Federal Administrative Court
FCC	Federal Casino Commission
FDJP	Federal Department of Justice and Police
FINMA	Federal Financial Market Supervisory Authority
FOPH	Federal Office of Public Health
FRC	Financial Reporting Council
FRTAP	Financial Reporting Technical Assistance Programme
FSB	Financial Stability Boards
FSC	Federal Supreme Court
FSIO	Federal Social Insurance Office
GAOC	German Auditor Oversight Commission
G-SIFIs	Global Systemically Important Financial Institutions
H3C	French High Council for Statutory Auditors
IAASB	International Auditing and Assurance Standards Board
ICWG	International Cooperation Working Group
IESBA	International Ethics Standards Board for Accountants
IFIAR	International Forum of Independent Audit Regulators
ISA	International Standards on Auditing
ISQC	International Standard on Quality Control

OAK BV	Supervisory Commission for Occupational Pension Schemes
PCAOB	Public Company Accounting Oversight Board
SAS	Swiss Auditing Standards of the Swiss Institute of Certified Accountants
SCWG	Standard Coordination Working Group
SEA	Stock Exchange Act of 24 March 1995 (SR 954.1)
SEC	U.S. Securities and Exchange Commission
SER	SIX Exchange Regulation
SIFIs	Systemically Important Financial Institutions
SoP	Statement of Protocol
SR	Classified Compilation of Federal Legislation

3 Special-law licences

A special-law licence, deriving from a main licence granted under the AOA, must be obtained for activities in the following areas (status: 31.12.2012):

Audit in the field of	Main licence under the AOA: Audit firm	Main licence under the AOA: Lead auditor	Special-law regulatory authority	Additional requirements
Banks ¹¹⁵	State-regulated audit firm	Audit expert	FINMA	Art. 26 FMSA ¹¹⁶ , Art. 3 FMAO ¹¹⁷
Securities traders ¹¹⁸	State-regulated audit firm	Audit expert	FINMA	Art. 26 FMSA, Art. 3 FMAO
Collective investment companies ¹¹⁹	State-regulated audit firm ¹²⁰	Audit expert	FINMA	Art. 26 FMSA, Art. 3 FMAO
Insurers ¹²¹	State-regulated audit firm	Audit expert	FINMA	Art. 26 FMSA, Art. 3 FMAO
Anti-money laundering ¹²²	Auditor	Auditor	FINMA	Art. 19b AMLA ¹²³
Central mortgage bond institutions ¹²⁴	State-regulated audit firm	Audit expert	FINMA	Art. 26 FMSA, Art. 3 FMAO
Pensions companies ¹²⁵	Audit expert ¹²⁶	Audit expert	(OAK BV) ¹²⁷	–
Health insurance companies ¹²⁸	Audit expert	Audit expert	(FOPH)	–
Casinos ¹²⁹	Audit expert	Audit expert	FCC	Art. 75 CO ¹³⁰

¹¹⁵ Banking Act of 8 November 1934 (BA; SR 952.0).

¹¹⁶ Financial Market Supervision Act of 22 June 2007 (FMSA; SR 956.1).

¹¹⁷ Financial Market Auditing Ordinance of 15 October 2008 (FMAO; SR 956.161).

¹¹⁸ Stock Exchange Act of 24 March 1995 (SEA; SR 954.1).

¹¹⁹ Collective Investment Schemes Act of 23 June 2006 (CISA; SR 951.31).

¹²⁰ There are, however, two exceptions: First, audit firms that audit asset managers and representatives of foreign collective investment companies need to be licensed as audit experts. The lead auditor also requires a licence as an audit expert (Cf. Art. 5 FMAO). Secondly, audit firms who have to prove that they meet the conditions of Art. 2, para. 3 of the CISA with respect to investment companies need to be licensed as auditors (Cf. Art. 6 FMAO).

¹²¹ Insurance Supervision Act of 17 December 2004 (ISA; SR 961.01).

¹²² Anti-Money Laundering Act of 10 October 1997 (AMLA; SR 955.0).

¹²³ Applies only to the audit of financial intermediaries that are directly subject to FINMA oversight. Self-regulating organisations may define differing conditions for audit firm licensing with respect to their members.

¹²⁴ Mortgage Bond Act of 25 June 1930 (MBA; SR 211.423.4).

¹²⁵ Federal Act of 25 June 1982 relating to Occupational, Survivors' and Disability Pensions (OPA; SR 831.40).

¹²⁶ There is, however, one exception: Only audit firms that are licensed as state-regulated audit firms can act as auditors of investment foundations (Art. 9 of the Ordinance of 22 June 2011 relating to investment foundations, ASV; SR 831.403.2).

¹²⁷ Oberaufsichtskommission Berufliche Vorsorge (Supervisory Commission for Occupational Pension Schemes).

¹²⁸ Federal Act of 18 March 1994 relating to Health Insurance (HIA; SR 832.10) and the Ordinance of 27 June 1995 relating to Health Insurance (HIO; SR 832.102).

¹²⁹ Casino Act of 18 December 1998 (CA; SR 935.52).

¹³⁰ Casino Ordinance of 24 September 2004 (CO; SR 935.521).

4 List of state-regulated audit firms

Status: 31 December 2012

Fully licensed

500003	PricewaterhouseCoopers AG	Zürich
500012	T & R AG	Gümligen
500038	Bankrevisions- und Treuhand AG	Zürich
500149	OBT AG	St. Gallen
500241	Mazars Coresa	Genève
500420	Deloitte AG	Zürich
500436	Refidar Moore Stephens	Glattbrugg
500498	PKF Wirtschaftsprüfung AG	Zürich
500505	Treuhand- und Revisionsges. Mattig-Suter	Schwyz
500646	Ernst & Young AG	Basel
500705	BDO AG	Zürich
500762	Balmer-Etienne AG	Luzern
500770	Intercontrol AG	Zürich
500959	BDO Visura International AG	Zürich
501091	Provida Wirtschaftsprüfung AG	St. Gallen
501382	Berney & Associés SA	Genève
501403	KPMG AG	Zürich
501470	Ferax Treuhand AG	Zürich
501570	Fiduciaire FIDAG SA	Martigny
501839	Grant Thornton AG	Zürich
502658	Treureva AG	Zürich

5 Registration of Swiss audit firms in the EU ¹³¹

Status: 31 December 2012

Country	Registered Swiss audit firm
Germany (German Audit Oversight Commission, GAOC)	As a result of the MoU between Germany and Switzerland there is no obligation to register in Germany.
Great Britain (Professional Oversight Board, FRC)	Deloitte AG, Ernst & Young AG, KPMG AG, PwC AG (4)
Finland (The Auditing Board of the Central Chamber of Commerce of Finland)	Ernst & Young AG (1)
France (French High Council for Statutory Auditors)	Ernst & Young AG, KPMG AG, PwC AG (3)
Ireland (Irish Auditing & Accounting Supervisory Authority)	Ernst & Young AG, KPMG AG, PwC AG (3)
Italy (CONSOB)	Ernst & Young AG, KPMG AG, PwC AG (3)
Liechtenstein (Financial Market Authority, FMA)	Ernst & Young AG, KPMG AG, PwC AG (3)
Luxembourg (Commission de Surveillance du Secteur Financier)	Deloitte AG, Ernst & Young AG, KPMG AG, PwC AG (4)
Netherlands (Netherlands Authority for the Financial Markets)	Ernst & Young AG (1)
Spain (Accounting and Auditing Institute ICAC)	PwC AG (1)
Sweden (Swedish Supervisory Board of Public Accountants)	Ernst & Young AG, KPMG AG, PwC AG (3)

¹³¹ Source: Reports submitted to the FAOA by the audit firms concerned. It should be remembered that it is a requirement to report registrations with foreign oversight authorities to the FAOA (Margin note 22 indent c section 1 of Circular 1/2010 of 31 March 2010 on reporting by state-regulated audit firms to the FAOA). No distinction has been drawn between provisional and definitive registration. The authority of the Swiss audit firms to provide statutory audit services in these countries is decisive.

6 List of equivalent foreign educational qualifications

Status: 31 December 2012

Country	Equivalent foreign educational qualifications
Germany	Bestellungsurkunde Wirtschaftsprüfer
France	Diplôme d'études supérieures comptables et financières und Diplôme d'expertise comptable
Great Britain	Chartered/Certified Accountant Memberships bei: ICAEW, ICAS, ICAI, ACCA, AIA
Ireland	Chartered/Certified Accountant Memberships bei: ICAEW, ICAS, ICAI, ACCA, ICPAI, IIPA + Audit permission
Italy	Dottore commercialista (Ragioniere e perito commerciale; Laurea/Dottore in economia e commercio; Dottore in economia aziendale; Dottore in economia delle istituzioni e dei mercati finanziari; Laurea in economia e professione)
India	Chartered Accountant
Netherlands	Registeraccountant
Norway	Studiet i revisjon (registered auditor, state authorised auditor)
Austria	Bestellungsurkunde Wirtschaftsprüfer
Philippines	Certified Public Accountant (CPA)
Sweden	Approved/Authorised public accountant
Turkey	Certified Public Accountant

7 Financial statements of the FAOA

Balance sheet

(in CHF)

	Note	31.12.2012	31.12.2011
Cash at bank and in hand	5	4,618,090	5,943,113
Receivables	6	183,084	176,192
Work-in-progress	7	290,000	314,000
Prepayments	8	24,666	70,288
Current assets		5,115,840	6,503,593
Tangible fixed assets	9	403,310	307,807
Intangible fixed assets	10	311,276	63,036
Investments	11	93,887	71,236
Non-current assets		808,472	442,079
Total assets		5,924,312	6,945,672
Short-term liabilities relating to services		165,585	116,698
Liabilities to state-regulated audit firms	12	54,193	723,440
Social security liabilities		67,541	19,903
Short-term provisions	13	205,000	157,500
Accruals	14	310,913	273,591
Accrued licensing fees	16	369,800	615,060
Current liabilities		1,173,032	1,906,192
Accrued licensing fees	16	251,280	539,480
Non-current liabilities		251,280	539,480
Reserves	17	4,500,000	4,500,000
Capital and reserves		4,500,000	4,500,000
Total liabilities		5,924,312	6,945,672

Income statement

(in CHF)

	Note	01.01.2012 –31.12.2012	01.01.2011 –31.12.2011
Oversight charges	2.12	2,748,307	2,036,560
Inspection fees	2.12	1,231,064	1,202,203
Licensing fees	18, 2.12	521,200	585,200
Commission on internet payments	2.12	-31,525	-34,276
Reimbursement of licensing fees	2.12	-30,600	-41,600
Accrual of licensing fees	16	-81,600	-100,800
Release of accrued licensing fees from prior years	16	615,060	1,831,940
Other income		32,578	66,737
Net revenues		5,004,484	5,545,964
Personnel expense	19	-4,116,666	-3,781,867
Operating expense	15, 20	-762,324	-660,388
Depreciation	9, 10	-140,654	-147,773
Operating profit		-15,161	955,936
Financial income		15,399	55,283
Financial expense		-238	-326
Financial result		15,161	54,957
Transfer to reserves (net)	17	–	-1,010,893
Profit/loss		–	–

Cash flow statement

(in CHF)

	Note	01.01.2012 –31.12.2012	01.01.2011 –31.12.2011
Transfer to reserves	17	–	1,010,893
Depreciation of fixed assets	9, 10	140,654	147,773
Release of licensing fees (long-term)	16	-288,200	-513,960
Increase/decrease in debtors	6	-6,893	2,712
Increase/decrease in work-in-progress	7	24,000	-158,643
Increase/decrease in prepayments	8	45,622	-4,331
Increase/decrease in liabilities		-620,360	765,653
Increase/decrease in social security liabilities		47,640	–
Increase/decrease in short-term provisions	13	47,500	-42,520
Increase/decrease in accruals	14	37,322	35,277
Increase/decrease in accrued licensing fees (short-term)	16	-245,260	-1,217,180
Net cash flows from operating activities		-817,974	25,674
Acquisition of tangible fixed assets	9	-180,768	-78,235
Acquisition of intangible fixed assets	10	-303,629	-20,481
Acquisition of investments	11	-22,653	-146
Net cash flows from investing activities		-507,049	-98,862
Change in cash and cash in hand		-1,325,023	-73,188
Cash and cash in hand at the start of the year	5	5,943,113	6,016,301
Cash and cash in hand at year end	5	4,618,090	5,943,113

Change in capital and reserves

(in CHF)

	01.01.2012 –31.12.2012	01.01.2011 –31.12.2011
Opening balance as of 1.1.	4,500,000	3,489,107
Transfer to reserves	0	1,010,893
Balance as of 31.12.	4,500,000	4,500,000

Notes to the 2012 financial statements

1 Operating activities

The Federal Audit Oversight Authority (FAOA) has its registered office at Bundesgasse 18 in Berne. It serves as a licensing body and administers a public register of the individuals and firms who provide audit services as defined by the Audit Oversight Act (AOA). Further, it oversees audit firms who provide audit services to public companies.

The FAOA was founded on 1 November 2006 and began its operating activities on 1 September 2007. The FAOA is a public-law institution and a separate legal entity. The FAOA conducts its activities independently, organises itself, and finances itself entirely from the fees paid by service users and the charges paid by state-regulated audit firms. The FAOA is autonomous in its organisation and management and maintains its own accounts.

Its function is regulated by the Audit Oversight Act of 16 December 2005 (AOA; SR 221.302). The aim of the Audit Oversight Act is to ensure the proper provision and quality of audit services.

On 15 June 2012 the Federal Council decided, in principle, to merge the previously separate audit firm oversight functions within the financial markets area and bundle them together with the FAOA in a two-step approach. As a result of this decision, as early as 1 September 2012 the oversight of financial statement audits for listed banks, insurance companies and collective investment companies was transferred from FINMA to the FAOA.

As at 31 December 2012 the FAOA employed 26 employees, representing 20 full-time equivalents. At the end of the prior year 25 employees, representing 18.4 full-time equivalents, were employed by the FAOA.

2 Accounting policies

2.1 Introduction

These financial statements of the FAOA are prepared in accordance with the requirements of the International Public Sector Accounting Standards (IPSAS), subject to Article 662a–663b of the Swiss Civil Code (according to Art. 35 para. 2 AOA).

These financial statements were approved by the Board of Directors on 25 February 2013. The attached statements are the entity financial statements for the financial year comprising calendar year 2012

with a balance sheet date of 31 December 2012 (including comparatives). The reporting currency is Swiss Francs (CHF).

Unless otherwise stated, assets and liabilities are valued at historical cost, which normally represents nominal value. Revenues and expenses are booked in the period in which they accrue.

The amounts stated in the financial statements are rounded to the nearest Swiss Franc and can therefore include immaterial rounding differences.

2.2 Cash and cash in hand

Cash and cash in hand comprises of petty cash, current accounts at financial institutions and an investment account at the Federal Finance Administration (FFA). Under Art. 36 para. 1 AOA the FAOA is obliged to deposit excess funds with the Federal Administration.

The amounts are stated at nominal values.

2.3 Receivables relating to services

Receivables are stated at nominal values after allowance for possible impairments.

2.4 Work-in-progress

Work-in-progress relating to inspections is valued using the applicable daily rates per Art. 39 para. 2 AOO.

2.5 Tangible fixed assets

Tangible fixed assets are accounted for at cost less accumulated depreciation. Depreciation is calculated on a linear basis over the expected useful life of the asset.

Asset category	Useful life (years)
Furniture and furnishings	10
Office equipment, IT equipment (hardware)	3
Fixtures and fittings	10

The residual value, useful life and method of depreciation of a tangible fixed asset is checked at each balance sheet date and amended if appropriate.

Where the book value of a tangible fixed asset exceeds the recoverable amount of that asset the difference is booked to the income statement as an impairment charge.

Tangible fixed assets disposed of are written-off at book value. Revenues arising upon the disposal of tangible fixed assets are disclosed separately in the income statement.

2.6 Intangible fixed assets

Intangible fixed assets are accounted for at purchase or production cost, less required write-downs. Depreciation is calculated on a linear basis over the expected useful life of the asset.

Asset category	Useful life (years)
Licensing register software	5
Other software	3

The residual value, useful life and method of depreciation of an intangible fixed asset is checked at each balance sheet date and amended if appropriate.

Where the book value of an intangible fixed asset exceeds the recoverable amount of that asset the difference is booked to the income statement as an impairment charge.

Self-generated goodwill cannot be capitalised.

2.7 Investments

Investments are accounted for at market value.

2.8 Taxes

The FAOA is exempt from all federal, cantonal and municipal taxes.

2.9 Provisions

Provisions include, in particular, short-term liabilities relating to personnel expense.

2.10 Leasing

Operating leases which cannot be terminated within one year are disclosed in the notes to the financial statements.

2.11 Capital and reserves

The FAOA accumulates reserves necessary for the exercise of its oversight activities, up to a maximum of an annual budget (Art. 35 para. 3 AOA). The accumulation of the reserve takes place over a period of 5 years and is periodically adjusted for changes in the annual budget. The FAOA received no donated capital upon foundation.

2.12 Revenues (fees and oversight charges)

The FAOA charges fees for its rulings, inspections and services and levies a charge upon state-regulated audit firms to cover any costs not covered by such fees. The fees and charges are set out in section five of the Audit Oversight Ordinance (AOO).

Fee income for the licensing of audit firms is accrued over a period of 5 years. Fee income for the licensing of individuals is taken directly to income. Fee reimbursements are charged directly to income.

Oversight charges are booked to income upon invoicing.

2.13 Financial result

The financial result comprises of interest income and interest expense. Interest is booked on an accrual basis. The FAOA holds no derivative financial instruments and does not use hedging.

3 Information regarding risk assessment (Art. 663b CO)

3.1 Information regarding risk assessment

The Executive Board is responsible for the internal control system and for the risk assessment related to this. The Executive Board performed and documented a risk assessment on 17 December 2012. This resulted in no adjustment to the insurance coverage previously determined with an external advisor. The internal control system of the FAOA is amended to take account of the risk assessment as appropriate.

The following financial risk is relevant to the FAOA:

3.2 Credit risk

The revenues of the FAOA are generated by charges and fees on those providing audit services. Reminders are sent in the case of late payment. Legal action is taken if appropriate.

4 Estimation uncertainty

The preparation of the financial statements according to generally accepted accounting standards requires the use of estimates and assumptions. These affect the stated amounts of assets and liabilities and the disclosure of contingent assets and liabilities as at the balance sheet date, as well as the stated amounts of income and expense. Although the Executive Board makes these estimates to the best of their knowledge, having due regard for current events and possible future FAOA measures, actual results could differ from the amounts estimated.

Explanatory information on individual financial statement items

5 Cash and cash in hand

(in CHF)

	2012	2011
Cash in hand	383	260
PostFinance accounts	449,439	89,397
Investment account at Federal Finance Administration FFA	4,168,268	5,853,456
Total cash and cash in hand	4,618,090	5,943,113

6 Receivables

	2012	2011
Licence fee receivables	126,570	103,038
Yellowpay receivables	50,962	72,939
Other receivables	5,552	215
Total receivables relating to services	183,084	176,192

No debts were written-off and no bad debt provisions were established in either the financial year 2012 or the prior year.

7 Work-in-progress

	2012	2011
Work-in-progress	290,000	314,000
Total work-in-progress	290,000	314,000

Work-in-progress comprises of inspection fees yet to be invoiced.

8 Prepayments

	2012	2011
Prepayments	24,666	70,288
Total prepayments	24,666	70,288

Prepayments represent payments made in advance for expenses of the following year.

9 Tangible Fixed assets

(in CHF)

	Furniture and furnishings	Office equipment, IT equipment (hardware)	Fixtures and fittings	Total 2012	Total 2011
Acquisition costs					
Opening balance	298,379	76,221	149,173	523,773	487,985
Acquisitions	60,588	5,969	114,211	180,768	78,235
Disposals	-1,795	-4,217	–	-6,012	-42,447
Closing balance	357,172	77,973	263,384	698,529	523,773
Accumulated depreciation					
Opening balance	-128,392	-35,579	-51,955	-215,966	-188,260
Acquisitions	-36,615	-22,312	-26,388	-85,265	-70,153
Disposals	1,795	4,217	–	6,012	42,447
Closing balance	-163,212	-53,674	-78,333	-295,219	-215,966
Net book value	193,960	24,299	185,051	403,310	307,807

At the balance sheet date there was no indication that tangible fixed assets were impaired.

There are currently no tangible fixed assets that are restricted, subject to rights of disposal or pledged.

The increase of CHF 114,211 in the acquisition cost of fixtures and fittings is attributable to the renovation of ceilings in the offices at Bundesgasse 18 in Bern. The increase of CHF 60,588 in the acquisition cost of furniture and furnishings is mainly attributable to additional furniture for the new offices at Hufgasse 11 in Zurich.

The fire insurance value of tangible fixed assets at 31 December 2012 was CHF 400,000 (prior year CHF 400,000). It is planned to increase the insurance cover to CHF 550,000 in 2013.

10 Intangible fixed assets

(in CHF)

	Software register and administration	Other software	Total 2012	Total 2011
Acquisition costs				
Opening balance	343,741	100,926	444,667	437,559
Acquisitions	302,400	1,229	303,629	20,482
Disposals	–	–	–	-13,374
Closing balance	646,141	102,155	748,296	444,667
Accumulated depreciation				
Opening balance	-294,359	-87,272	-381,631	-317,385
Acquisitions	-49,381	-6,008	-55,389	-77,620
Disposals	–	–	–	13,374
Closing balance	-343,740	-93,280	-437,020	-381,631
Net book value	302,401	8,875	311,276	63,036

At the balance sheet date there was no indication that intangible fixed assets were impaired.

There are currently no intangible fixed assets that are restricted, subject to rights of disposal or pledged.

The increase of CHF 302,400 in the acquisition cost of software register and administration is attributable to payments with respect to the modernisation of the IT environment. The new IT environment (software) is expected to go live in the first half of 2013. Depreciation of the new software will begin upon it going live.

11 Investments

In connection with the rent of offices the FAOA has two tenant deposit accounts in the total amount of CHF 93,887.

12 Liabilities to state-regulated audit firms

The FAOA levies an annual oversight charge upon state-regulated audit firms (see section 2.12). An on account amount is charged at the beginning of the year. Unused on account amounts are refunded to the state-regulated audit firms in the following year. The amount of CHF 54,193 (prior year CHF 723,440) will be credited to the state-regulated audit firms in 2013.

13 Short-term provisions

(in CHF)

	2012	2011
Personnel expense liabilities	197,000	150,000
Provision for third party compensation	8,000	7,500
Total short-term provisions	205,000	157,500

Holiday, accrued flexible working hours and overtime entitlements are calculated and accrued as at 31 December based on individual employment terms.

A provision for compensation was established in connection with FAOA rulings subject to third party appeal (in particular, licence application rejections).

14 Accruals

	2012	2011
Various accruals	310,913	273,591
Total accruals	310,913	273,591

Accruals include, in particular, accruals in relation to personnel expense and accruals for the cost of the Activity Report 2012.

15 Operating leases

	2012	2011
Minimum payments within one year	10,740	10,740
Minimum payments in years 2 to 6	42,960	52,805

Operating leases comprise of a contract with Triumph-Adler for multi-purpose equipment. The current contract has a total term of 6 years (1.1.2012 – 1.1.2018).

The FAOA has not entered into any finance leases.

16 Accrued licensing fees

	2012	2011
Accrued licensing fees (short-term)	369,800	615,060
Accrued licensing fees (long-term)	251,280	539,480
	621,080	1,154,540

Fee income from the licensing of audit firms, as well as individuals (2007 to 2010), was accrued over a period of 5 years.

17 Reserves

(in CHF)

	2012	2011
Reserves	4,500,000	4,500,000
Total reserves	4,500,000	4,500,000

According to Art. 35 para. 3 AOA, the FAOA may accumulate a reserve for the exercise of its oversight activities, up to a maximum amount of an annual budget.

18 Licensing fees

	2012	2011
Licensing fees individuals	419,200	456,200
Licensing fees audit firms	102,000	129,000
Total licensing fees	521,200	585,200

19 Personnel expense

	2012	2011
Staff compensation and Board member fees	3,018,094	2,881,960
Employer contributions	685,055	565,074
Other personnel expense	263,668	253,258
Third party personnel costs	149,849	81,575
Total personnel expense	4,116,666	3,781,867

Employer contributions comprise payments relating to national insurance (state pension, invalidity, income compensation) occupational pension schemes, work-related accident insurance and daily sickness allowance insurance. A contribution of CHF 25,000 (prior year CHF 25,000) made to the employer contribution reserve of the FAOA pension fund is included above.

In the reporting year third party personnel costs include, in particular, external translation service charges, as well as expenses incurred in connection with the modernisation of the IT environment.

The increase in personnel expense is, in particular, related to the assumption of additional responsibilities from FINMA as from 1 September 2012 (Note 1).

20 Operating expense

(in CHF)

	2012	2011
Accommodation	189,242	177,040
Minor capital expenditure, fixed asset maintenance and leasing	14,783	18,087
Administrative expense	108,414	88,573
IT expense	227,989	199,575
Other operating expense	221,896	177,113
Total operating expense	762,324	660,388

The increase in operating expense is attributable to the taking up of additional offices in Zurich, as well as higher expenses related to the more expansive Activity Report (including publication of the financial statements in three languages).

21 Contingencies

At the balance sheet date there were no contingent liabilities and, in particular, no pending or threatened claims for damages.

22 Related party transactions

22.1 Definition of «related parties»

Related parties can be entities or individuals who can influence the FAOA or can be influenced by the FAOA. At the FAOA the following groups are defined as related:

- The Federal Administration, within the meaning of Art. 6 Government and Administration Ordinance (RVOV)
- Swisscom, Post, Swiss Federal Railways
- Members of the Board of Directors
- Members of Management, respectively the Executive Board

All transactions with related individuals and entities were entered into on the basis of normal customer, respectively supplier, relationships and strictly on arm's length terms.

22.2 Particular relationship with the Federal Administration

The Federal Audit Oversight Authority, a public-law institution with separate legal identity, is organisationally attached to the Federal Administration. As such, the Federal Administration can influence the FAOA in many ways:

- The AOA is a federal law. The AOA and other regulations are enacted by the Federal Council.
- The Federal Council elects the Board of Directors, appoints the Chairman and Vice-Chairman, determines compensation and approves the selection of the Chief Executive Officer.
- As auditor of the FAOA, the Swiss Federal Audit Office audits the oversight authority in accordance with the Federal Auditing Act.
- The Federal Audit Oversight Authority is required to invest excess funds with the Federal Administration at market interest rates (Art. 36 para. 1 AOA).

If required for liquidity reasons, the Federal Administration grants the FAOA loans at market interest rates (Art. 36 para. 2 AOA). The FAOA is exempt from all federal, cantonal and municipal taxes (Art. 37 AOA).

22.3 Remuneration of the Board of Directors and Management

(In CHF thousands)

	2012	2011
Board of Directors		
Fees of Chairman	75	110
Fees of Vice-Chairman	38	75
Fees of other members	52	90
Social security contributions ¹	0	0
Total compensation of the members of the Board of Directors	165	275
Chief Executive Officer and Executive Board		
Salary of Chief Executive Officer	250	247
Other benefits of Chief Executive Officer ²	37	32
Salaries of other members	323	326
Other benefits of other members	43	32
Social security contributions ³	107	107
Total compensation of the members of the Executive Board	760	744

In the reporting year individual, performance-related salary increases were effected. No general inflation adjustment was made.

¹ All social security contributions (employer and employee) are borne by the members of the Board of Directors.

² Includes additional taxable benefits such as bonuses and non-mandatory child allowances.

³ Comprises pension/invalidity/income compensation insurance contribution, unemployment insurance contribution, work-related/non-work-related accident insurance contribution, occupational pension savings contribution and risk premium.

23 Events after the balance sheet date

No events have occurred since the balance sheet date of 31 December 2012 that impact the informational value of the 2012 financial statements.





Report of the statutory auditor on the limited statutory examination

to the Board of Directors of the Federal Audit Oversight Authority in Bern

As statutory auditor according to art. 32 of the Auditor Oversight Act (SR 221.302), we have examined the financial statements (balance sheet, income statement, cash flow statement, statement of changes in equity, and notes) of the Federal Audit Oversight Authority for the year ended 31 December 2012.

These financial statements are the responsibility of the Management. Our responsibility is to perform a limited statutory examination on these financial statements. The Swiss Federal Audit Office is independent according to the Swiss Federal Audit Office Act (SR 614.0).

We conducted our examination in accordance with the Swiss Standard on the Limited Statutory Examination. This standard requires that we plan and perform a limited statutory examination to identify material misstatements in the financial statements. A limited statutory examination consists primarily of inquiries of company personnel and analytical procedures as well as detailed tests of company documents as considered necessary in the circumstances. However, the testing of operational processes and the internal control system, as well as inquiries and further testing procedures to detect fraud or other legal violations, are not within the scope of this examination.

Based on our limited statutory examination, nothing has come to our attention that causes us to believe that the financial statements do not comply with Swiss laws and regulations.

Bern, 4 March 2013

SWISS FEDERAL AUDIT OFFICE

Walter Risler
 Licensed Audit Expert

Paul Ackermann
 Licensed Audit Expert

Original text German

