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A practical guide to the new Swiss financial reporting law

Tools, tips for implementation and best practices

January 2015

A paper produced by PwC (not only) for people responsible for financial reporting and auditing

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Foreword

Dear reader

The new Swiss financial reporting law entered into force on 1 January 2013. The entities concerned must implement the new provisions for annual accounts from the 2015 financial year onwards, and for consolidated accounts from the 2016 financial year. They can also choose to apply the provisions earlier on a voluntary basis.

We want to make it as easy as possible for you to implement the new Swiss financial reporting law. PwC has therefore drawn up an illustrative financial statement and converted it into Microsoft Excel. This tool aims to ensure that your annual accounts comply with the requirements of the new financial reporting law.

Last but not least, our tool will save you time and money, because we are making it available to you free of charge. We would also be happy to arrange a no-obligation appointment with our experts to answer your questions about the new financial reporting law and to discuss the associated impact on other areas (e.g. internal planning and controlling).

You can order the software by completing the attached reply card or download it online at www.pwc.ch/smecontrolling.

We trust that you will find this paper interesting and wish you every success implementing the new financial reporting law.

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Leader Management & Controlling
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Contents

1. An overview of the new Swiss financial reporting law[1]

1.1 What was the goal of the revision of the accounting legislation?

Like the old legislation, the aim of the new law is to ensure that an entity presents accounts that enable third parties to form a reliable judgement of its economic position.

The aims of the revision were as follows:

- To harmonise the rules laid down in the Code of Obligations for all legal forms under private law
- To differentiate between entities according to their size
- To introduce clear, understandable terms and rules on the structure of accounts and valuation
- To increase transparency
- To strengthen the rights of minority shareholders
- To ensure more meaningful and informative consolidated reporting
- To create a tax neutral solution

1.2 Who is affected by the new rules?

The general duty to keep accounts and file financial reports applies to sole proprietorships and partnerships (general partnerships and partnerships limited by shares) that have achieved sales revenue of at least CHF 500,000 in the last financial year, as well as to all legal entities (companies limited by shares, limited liability companies, partnerships limited by shares, cooperatives, and associations and foundations). For all these, the law uses the term "entities" regardless of the legal form of the entity in question (Art. 957 Code of Obligations [CO]). Small entities (sole proprietorships and partnerships with sales revenue of less than CHF 500,000, associations and foundations that do not have to be entered in the commercial register, and foundations exempt from the audit requirement) are only subject to reduced accounting requirements.

[1] This chapter examines selected changes to Swiss financial reporting law and does not claim to be exhaustive. For a detailed description of the new financial reporting law, please see the PwC paper "The new Swiss financial reporting law. An overview of the most important changes, plus the revised wording of the law", and the legal texts set out in it.

1.3 What requirements do all entities have to comply with?

The following minimum requirements apply to all entities:

	Accounting (Art. 957 CO)	Financial reporting (Art. 958 CO)[1]
Purpose	• Basis for financial reporting • Record transactions and circumstances required to present entity's economic position	Present economic position of the entity so that third parties can reliably assess it
Assumption		• Going concern • Accrual
Principles	• Transactions recorded completely, truthfully and systematically • Documentary proof • Appropriate given form and size of entity • Clarity • Verifiability (Art. 957a CO)	• Clear and understandable (Art. 958c CO) • Complete • Reliable • Include essential information • Prudent • Same rules applied in presentation and valuation • No offsetting
General rules	• Compliance with recognised accounting principles • Duty to keep accounts • Retention	• Compliance with recognised financial reporting principles • Requirement to provide evidence • Retention period • Approval • Signing off
Components	• Accounting records • Accounting vouchers • Inventories	• Annual accounts (balance sheet, profit and loss account, notes; for larger entities cash flow statement) • Consolidated accounts[1] (Art. 963 CO) • Annual report[2] (Art. 961c CO)
Forms of accounting	Written or electronic	In account or report form, with prior-year figures
Currency	In CHF or functional currency	In CHF or functional currency (plus values in CHF)
Language	In official Swiss language or English	In official Swiss language or English

[1] Reduced requirements for small entities
[2] If requested

The accounts are filed in the annual report. This contains the annual accounts. The annual report must be prepared within six months after the end of the financial year and submitted to the responsible governing body or the responsible persons for approval (Art. 958 CO).

Creditors who prove a legitimate interest must also be allowed to read the annual and consolidated accounts and the relevant audit reports (Art. 958e CO). The accounting records and audit reports must be retained for ten years. Special rules apply if records and reports are retained electronically or in a comparable manner (Art. 958f CO).

1.4 How do the requirements differ for entities of different sizes?

The law lays down different accounting and financial reporting requirements depending on the size and economic significance of the entity in question.

<table>
<tr><th></th><th colspan="5">Sole proprietorships, partnerships and legal entities ("undertakings")</th></tr>
<tr><th rowspan="4">Size thresholds</th><td rowspan="4">Sole proprietorships and partnerships with sales revenue below CHF 500,000
Associations and foundations not entered in commercial register (small undertakings)</td><td rowspan="4">Sole proprietorships and partnerships</td><td colspan="2">Legal entities</td><td rowspan="4">Listed companies, cooperatives with 2,000 members or more, large foundations</td></tr>
<tr><td colspan="2">Required to have ordinary audit?</td></tr>
<tr><td colspan="2">2 out of 3 criteria in 2 successive years: [3]
Balance sheet total: CHF 20 m;
Sales revenue: CHF 40 m;
Headcount: 250 full-time positions on annual average</td></tr>
<tr><td>Not met</td><td>Exceeded</td></tr>
<tr><th>Audit</th><td>No</td><td>No [1]</td><td>No audit or limited audit (Art. 729 CO)</td><td>Ordinary audit (Art. 727 CO)</td><td>Ordinary audit (Art. 727 CO)</td></tr>
<tr><th>Financial statements in accordance with CO</th><td>Simplified accounts of income, expenditure and asset position</td><td>Annual accounts
• Balance sheet
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• Balance sheet
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• Notes [2]</td><td colspan="2">Annual accounts
• Balance sheet
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+ additional information [4]
– further details in notes
– cash flow statement
– annual report</td></tr>
<tr><th>Financial statements in accordance with a recognised standard</th><td>On request of minority shareholders (Art. 962 para. 2 CO)</td><td>On request of minority shareholders</td><td>On request of minority shareholders</td><td>On request of minority shareholders</td><td>Mandatory (Art. 962 CO)</td></tr>
</table>

1 Partnerships are subject to a statutory audit if a personally liable partner demands financial statements in accordance with a recognised standard or if the company voluntarily prepares group financial statements in accordance with a recognised standard and has these audited. (Art. 962 para. 2 (3) in conjunction with Art. 962a para. 3 CO and Art. 962 para. 3 in conjunction with 963b para. 2 CO). Limited partners may demand that an audit be carried out by an expert (Art. 600 para. 3 CO).

2 Sole proprietorships and partnerships (but not legal entities) are not obliged to produce notes to their financial statements (Art. 959c para. 3 CO).

3 The following criteria apply to associations: balance sheet total of CHF 10 million; revenues of CHF 20 million and 50 full-time employees (Art. 69b para. 1 SCC). An association member with personal liability or an obligation to make additional contributions may demand a limited audit.

4 Companies that are part of a group are not obliged to provide this additional information unless qualified minorities demand this additional information (Art. 961d CO).

1.5 What additional financial reporting requirements apply to larger entities?

Larger entities are defined as those that are required by law to have an ordinary audit (as per Art. 727 CO). These entities must

- provide additional information in the notes to the annual accounts (on long-term interest-bearing liabilities and the fees paid to the auditor) (Art. 961a CO),
- prepare a cash flow statement (Art. 961b CO) and
- prepare a management report.

The management report should – as a supplement to the annual accounts – provide information on the conduct of a risk assessment, orders and assignments, research and development activities and extraordinary events. It should also include a statement about future prospects (Art. 961c CO) and indicate the annual average number of full-time positions (Art. 961c OR).

These additional requirements may be dispensed with if the entity is part of a group that prepares consolidated accounts in accordance with a recognised financial reporting standard, provided a qualified minority does not request this additional information (Art. 961d CO).

1.6 Who has to prepare consolidated accounts?

If a legal entity (an incorporated company, association or foundation) controls one or more entities that are required to file financial reports, in addition to annual accounts the entity must prepare consolidated accounts in the annual report for all the entities controlled.

Sole proprietorships and partnerships are exempt from the consolidation requirement.

A legal entity is deemed to control another entity if it:

- holds the majority of the voting rights in the highest management body
- has the right to appoint or remove the majority of the members of the supreme management or administrative body
- is able to exercise a controlling influence on the entity based on the articles of association, foundation deed or comparable instruments.

A legal entity is exempt from the requirement to prepare consolidated accounts if together with the controlled entity it has not exceeded two of the following thresholds in two successive financial years:

- Total assets of CHF 20 million
- Revenue of CHF 40 million
- An annual average of 250 full-time positions.

Sub-groups are also exempt from the consolidation requirement if the controlling entity's consolidated accounts have been prepared, audited and made available in accordance with regulations equivalent to the Swiss law (Art. 963a para. 1 ciph. 2 CO).

Associations, foundations and cooperatives (but not companies limited by shares or limited liability companies) may delegate the duty to prepare consolidated accounts to a controlled entity provided the controlled entity concerned brings all the other entities together under single management and actually exercises control.

Consolidated accounts must be prepared in any case where this is necessary to make the most reliable assessment of the economic position. Company members who represent at least 20% of the basic capital, 10% of the members of a cooperative, 10% of the members of an association or a foundation supervisory body, or a company member or an association member subject to personal liability or a duty to pay in further capital may also demand that consolidated accounts be prepared.

The requirement that companies limited by shares and limited liability companies have both the annual accounts and the consolidated accounts approved by the annual general meeting of shareholders or annual general meeting of members continues to apply (Art. 698 CO and Art. 804 CO).

1.7 What principles have to be followed when preparing consolidated accounts?

Listed companies (if required by the stock exchange), large cooperatives (with at least 2,000 members) and foundations required by law to undergo an ordinary audit must prepare financial statements in accordance with a recognised financial reporting standard (Swiss GAAP FER, IFRS, IFRS for SMEs, US GAAP or IPSAS) (Art. 963b CO).

The consolidated accounts of other entities are governed by recognised financial reporting principles. However, they need not apply any recognised financial reporting standards, meaning that they are to a large extent free to choose any consolidation and valuation rules they wish within the scope of recognised accounting principles. As under the old provisions governing companies limited by shares, they have to specify the rules used in the notes to the consolidated accounts (Art. 963b para. 3 CO).

However, in such cases company members who represent at least 20% of the basic capital, 10% of the members of a cooperative, 10% of the members of an association or a foundation supervisory body, or a company member or an association member subject to personal liability or a duty to pay in further capital may require that consolidated accounts nevertheless be prepared in accordance with a recognised financial reporting standard.

2. Practical tips for implementing the tool.

After concentrating on the theoretical requirements of the new financial reporting law in the previous chapter, we will now discuss how to implement it. PwC has designed a tool (referred to as the PwC tool) to make it easier for you to apply the new Swiss financial reporting law. It also aims to ensure that your annual accounts comply with the requirements of the new financial reporting law. Finally, our predefined template for annual financial statements will save you time and money!

In the following paragraphs, we will demonstrate the main functions of the PwC tool with the help of selected screenshots. We would be happy to arrange a personal appointment to explain how the PwC tool works in more detail and to answer any questions you may have about the new financial reporting law.

2.1 General information about the PwC tool

The PwC tool for the new Swiss financial reporting law is divided into different sections as follows (each on a separate MS Excel sheet):

1. General information
2. Cover sheet
3. Balance sheet
4. Profit and loss statement according to nature of expense or activity-based costing method
5. Cash flow statement
6. Notes
7. Appropriation of earnings
8. Sample management report and checklist

The different sections are interconnected. The advantage of this is that data only needs to be entered once and – where relevant – will be copied into the other sections (e.g. cash flow statement) automatically. The key functions are as follows:

Sections marked grey are input fields.

Sections marked white are fields that are calculated automatically on the basis of the data entered.

Text formatted in red shows whether or not the built-in controls have detected an error.

More detailed information can be found on the first sheet, "General information", in the PwC tool. Individual pages are formatted so that you can print out your annual accounts directly – all you need to do is add your logo.

2.2 What are the minimum requirements for my entity?

Before using the PwC tool, you should give serious thought to which provisions of the new law apply to your entity. As so many different exceptions exist, we advise you to discuss your situation with your auditor. We would be happy to help if you need any further information.

2.3 What is the minimum structure for the balance sheet?

The law now defines a number of key terms in the provisions governing the balance sheet:

Items must be recognised as *ASSETS* if, according to Art. 959 para. 1 CO,

- they may be disposed of due to past events
- a cash inflow is probable
- their value can be reliably estimated.

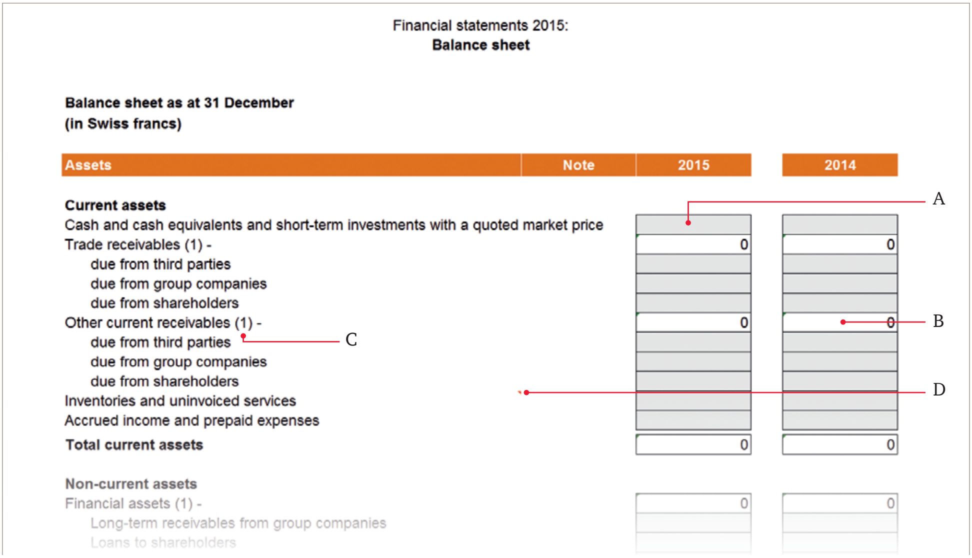
Liabilities must be recognised as *LIABILITY* if, according to Art. 959 para. 5 CO,

- they have been caused by past events
- a cash outflow is probable
- their value can be reliably estimated.

SHAREHOLDERS' EQUITY must be shown and structured in the required legal form (Art. 959 para. 7 CO).

This structure must be adapted if necessary to take account of the entity's business activity or to enable third parties to assess its asset or financing position. Receivables and liabilities vis-à-vis direct or indirect participants and management bodies and vis-à-vis entities in which there is a participation must be presented separately on the balance sheet or in the notes to the accounts. All items that will probably be realised or are expected to fall due for payment within one year of the balance sheet date or within the normal operating cycle must be entered on the balance sheet as current assets or current liabilities. Assets are shown on the basis of their degree of liquidity, and liabilities on the basis of their due date. The entity's own shares are no longer to be carried as assets, but are to be presented separately as a reduction in shareholders' equity. Interest-bearing liabilities (financial debts) are to be shown separately to make it easier to calculate and analyse key measures, such as EBIT.

Note:
The "Balance sheet" section of the PwC tool shows the balance sheet structure in accordance with the provisions of the CO mentioned above. Data is entered directly into the coloured cells. If any additional instructions need to be considered for specific items, appropriate comments have been inserted into the PwC tool (either directly as Excel comments or as footnotes at the bottom of the balance sheet).



Financial statements 2015:
Balance sheet

Balance sheet as at 31 December
(in Swiss francs)

Assets	Note	2015	2014
Current assets			
Cash and cash equivalents and short-term investments with a quoted market price			
Trade receivables (1) -		0	0
due from third parties			
due from group companies			
due from shareholders			
Other current receivables (1) -		0	0
due from third parties			
due from group companies			
due from shareholders			
Inventories and uninvoiced services			
Accrued income and prepaid expenses			
Total current assets		0	0
Non-current assets			
Financial assets (1) -		0	0
Long-term receivables from group companies			
Loans to shareholders			

A Input fields: Data for the current year and – if necessary – for previous years is entered here. Alternatively you can of course incorporate links to files from your previous systems.

B Calculation fields: These are generally (sub-)totals. However, some fields are calculated automatically on the basis of information from preceding sheets (e.g. change in inventories).

C Footnotes: On some sheets, additional observations can be found regarding certain items.

D Comments: Useful tips and information have been inserted as Excel comments for specific items.

2.4 How does the profit and loss account have to be structured?

The profit and loss account can be prepared according to the period-based (nature of expense) accounting method or the cost of sales (activity-based costing) method (Art. 959b CO). If the cost of sales method is used, the notes to the accounts must also show the staff costs and, as a single item, depreciation and valuation adjustments to fixed asset items.

In recognised financial reporting standards (e.g. IFRS, US GAAP), exceptional items are tolerated only very rarely or not at all – in an attempt to avoid controversial distinctions. Particularly in cases where there are incentives linked to the achievement of specific financial targets, entities will be more inclined to state an item of expenditure as exceptional. For the same reasons, in cases of doubt the tendency will be to state income as operational in nature. Swiss law does, however, allow extraordinary, non-recurring or prior-period costs and income. These items must be shown separately in the profit and loss account and explained in the notes (Art. 959c para. 2).

Note:
The PwC tool contains two sheets presenting the profit and loss statement, one with expenses classified by nature and one with expenses classified by function. As both methods result in an identical annual profit or loss, the data can be incorporated into the subsequent calculations irrespective of the method chosen.

Financial statements 2015:
P&L by nature of expense

XYZ Inc., Zurich

Profit and loss statement for the financial year/period ended 31 December (in Swiss francs)

P&L by nature of expense

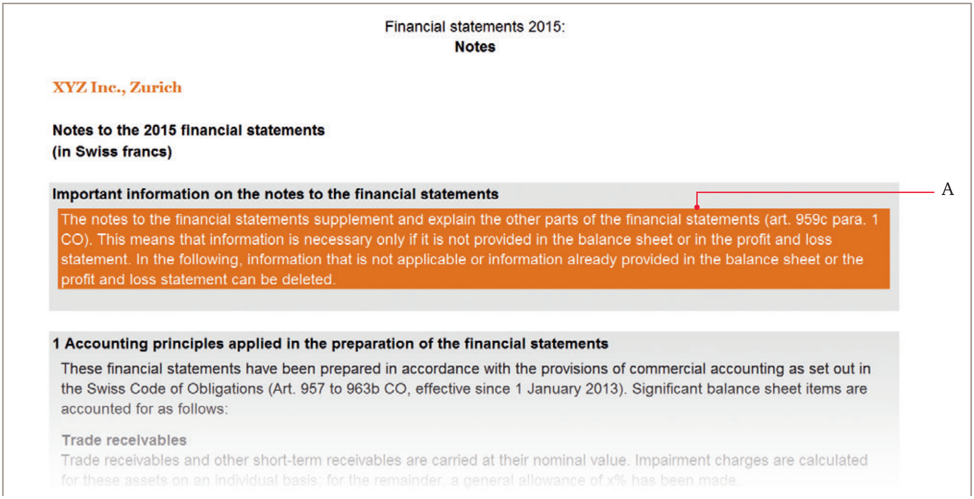
	Note	2015	2014
Net proceeds from sales of goods and services			
Changes in inventories of unfinished and finished goods and in uninvoiced services			
Cost of materials			
Staff costs			
Other operating expenses			
Depreciation and valuation adjustments to fixed assets			
Earnings before interest and taxes		0	0
Financial income			
Financial expenses			
Earnings before taxes		0	0
Non-operating income			
Non-operating expenses			
Extraordinary, non-recurring or prior-period income			
Extraordinary, non-recurring or prior-period expenses			

Note:
Built-in control calculations carried out automatically in the background in the PwC tool must be taken into account. The annual profit or loss shown in the profit and loss statement is therefore validated according to the corresponding balance sheet items as well as the amount stated under appropriation of profit.

2.5 What has to be disclosed in the notes?

All entities, with the exception of sole proprietorships and partnerships, must now present notes to supplement and explain the other parts of the annual accounts.

Note:
The PwC tool helps you to draw up legally compliant notes by proposing "building blocks" containing all the relevant information. Passages that require details specific to your entity are shown in red. Information that is not relevant to your entity or that has already been covered in the balance sheet or profit and loss statement can simply be deleted.



Financial statements 2015:
Notes

XYZ Inc., Zurich

Notes to the 2015 financial statements
(in Swiss francs)

Important information on the notes to the financial statements

The notes to the financial statements supplement and explain the other parts of the financial statements (art. 959c para. 1 CO). This means that information is necessary only if it is not provided in the balance sheet or in the profit and loss statement. In the following, information that is not applicable or information already provided in the balance sheet or the profit and loss statement can be deleted.

A

1 Accounting principles applied in the preparation of the financial statements

These financial statements have been prepared in accordance with the provisions of commercial accounting as set out in the Swiss Code of Obligations (Art. 957 to 963b CO, effective since 1 January 2013). Significant balance sheet items are accounted for as follows:

Trade receivables
Trade receivables and other short-term receivables are carried at their nominal value. Impairment charges are calculated for these assets on an individual basis; for the remainder, a general allowance of x% has been made.

A Editing information (should be deleted before printing)

2.6 What information is included in the annual report?

The management report presents the business performance and the economic position of the entity and, if applicable, of the corporate group at the end of the financial year from points of view not covered in the annual accounts (Art. 961c para. 1 CO). The management report therefore gives additional explanations about significant events that have occurred during the financial year.

Note:
As the management report is individually tailored to each entity, there is no standard template in the PwC tool. Instead, the PwC tool contains a checklist specifying the most important elements to be included in the management report. In addition to the general business performance, information must be provided on risk assessment, extraordinary events and future prospects, for example. The PwC tool also contains an example of a management report for a sample entity.

Financial statements 2015:
Management report checklist

XYZ Inc., Zurich

Management report on the financial year 2015

Important information on the management report (annual report)

The management report presents the business performance and the economic position of the entity and, if applicable, of the corporate group at the end of the financial year. This is a perspective not addressed by the financial statements (art. 961c para. 1 CO). In other words, the management report is an explanatory account of important events occurring during the financial year.

General development of business

Development of business
Economic situation
Full-time equivalents on annual average

In many cases it also makes sense to address the following points:

Information on the operating environment (market/industry, competition, business cycle, legislative environment and expectations for the future)
Information on the financial situation (sales, costs and capital structure)
Information on other significant components of the financial statements and their development
Information on offices and production facilities

Risk assessment (covering, for example, the following points):

Objectives, organisational set-up, role of risk management and risk management instruments used

2.7 How can consolidation be achieved efficiently?

If a legal entity (an incorporated company, association or foundation) controls one or more entities that are required to prepare financial statements, in addition to annual accounts the entity must prepare consolidated accounts in the annual report for all the entities controlled.

Drawing up consolidated accounts can be extremely expensive and time consuming depending on the complexity of the entity. As a result, software solutions are being used more and more frequently, even by small and medium-sized enterprises. The extent to which the associated investments result in the necessary added value depends on a variety of factors, e.g.

- The number of entities to be consolidated
- The currencies to be taken into account
- The number of consolidation procedures per year
- The applicable financial reporting standard
- The extent of additional information to be consolidated (e.g. additional management information, cash flow statement)
- The extent of intercompany relations
- The existing minorities or proportionally consolidated entities
- The number of corporate transactions or deferrals to consolidated companies

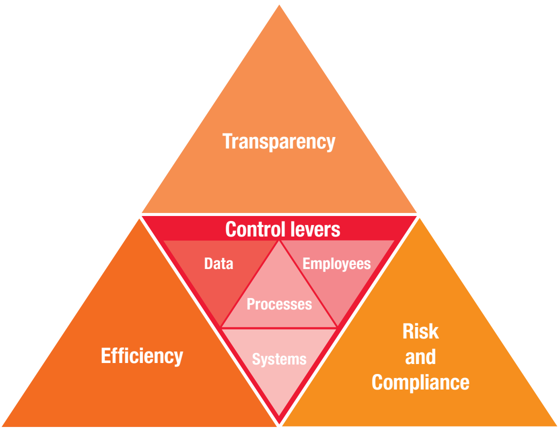
Note:
As a result of the complex nature of consolidated accounts, a consolidation function is not included in the free PwC tool by default. However, PwC offers a range of solutions in the field of consolidation – ranging from an Excel-based solution to consolidation software. Do not hesitate to contact us. We would be happy to offer you advice on the solution that would be the most cost-effective for you, with no obligation. We would of course be delighted to assist you in implementing a consolidation solution tailored to meet your needs.

3. What is the impact on internal planning and controlling?

The new financial reporting law in particular, and the Code of Obligations in general, do not give any explicit instructions regarding the structure of (internal) planning and controlling.

However, it is obvious that some statutory minimum requirements – for instance regarding the preparation of the management report (Art. 961c CO) – cannot be met by financial accounting alone. This particularly concerns forward looking indicators, such as research and development activities or risk and opportunity assessment in addition to non-financial key figures, such as the number of full-time positions or the number of orders and assignments received.

The Management Information System (MIS) describes all the management information given to the management and relevant employees on a regular basis. The main aim of the MIS is to achieve transparency within the entity as efficiently as possible. Suitable control mechanisms have to be implemented to ensure that information is consistently protected against unauthorised access.



Transparency: Organise and present information to give a specific insight into the management of the entity and to support decision-making.

Efficiency: Provide employees with relevant management information promptly, using efficient processes and organisational structures.

Risk and Compliance: Constantly monitoring the control levers to ensure that the right people take responsibility for information and have efficient access to coherent information.

Control levers: Make efficient, effective use of processes, employees, data and systems, in order to support the activities of the entity.

In practice, transparency – in plain terms – means that the MIS does not merely contain information and analyses about the company's business performance and results. Although it is important to be aware of the reasons for positive and negative past developments, it is equally important to be able to recognise, measure and assess the drivers for the future development of sales and results. These drivers are the only factors that can be influenced actively by management and by the board of directors.

As far as guaranteeing efficiency is concerned, it is essential for the MIS to focus on significant facts and contain prior comments and recommended actions for the relevant employees. Thanks to modern IT solutions, pages of figures can easily be converted into understandable, meaningful graphics. With the help of drill-down functionalities, additional details tailored to the target audience can be provided at the touch of a button. The manual preparation required by an entity can be greatly reduced, without restricting the information conveyed to the target audience.

All Management Information Systems are based on the needs of the decision-makers in the entity. These needs are usually defined in the corporate strategy – operationalised by a business plan. In other words, a functional MIS must give a clear idea of how much progress an entity has made towards implementing its strategy – in all the different areas in which it operates.

Your contacts

Our dedicated SME advisory team has already helped many customers with tasks ranging from defining the contents of an MIS to setting up a related cost and performance accounting system, not to mention implementing the technical system as part of a specially-designed software solution. Our team consists of experienced experts in the fields of reporting, controlling and financial accounting. With your help, we can put together the perfect team to suit your project requirements in terms of specialist know-how, scope of responsibility, and managerial and industrial experience. As well as providing specialist support, we would be happy to offer project management expertise or operational assistance in the event of staff shortages to meet your individual needs.

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