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Annual Report 2016

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Foreword

In the first year of its 2016–2019 strategy period, the FAOA has taken the initial steps toward its implementation. On the one hand, cooperation and contact with national and international audit stakeholders was further developed. On the other hand, the publication of legally-binding court rulings (in anonymous form) and FAOA enforcement principles made the enforcement process more transparent. Besides implementing the strategy, the focus of the FAOA continues to be on its main legal responsibilities.

We would like to take this opportunity to thank FAOA staff sincerely for the great dedication with which they perform the tasks of the FAOA and realise the current strategy.

State-regulated audit firms

The larger audit firms in Switzerland generated more audit fees overall during the year under review. This fee increase is pleasing but should not obscure the fact that pressure remains on the Swiss audit market and audit fees, particularly during the tendering. The higher fees compared to the prior year relate largely to non-recurring audit work (e.g. forensics). When tendering the audit and approving annual audit fees, audit committees and boards have a duty to ensure that an efficient and effective audit can be performed for the proposed fee.

In the future, the auditor's report to the general meeting of quoted companies will also contain information on key audit matters evaluated during the audit. The comprehensibility of audit reports to investors and other addressees will be improved considerably by the new requirements of ISA 701, respectively FAOA Circular No. 1/2015. The enhanced reporting will lead to disclosure of the most significant financial risks and complex matters the auditor sees and the related audit procedures. The auditor's risk considerations will therefore be visible not only to the board of the audited company but also to investors and

other stakeholders. The quality of the audit process can thus be evaluated better and competition between audit firms can hinge more on qualitative arguments.

Audit digitalisation

Increasing digitalisation is also changing audit fundamentally. Modern technologies, such as data analytics, point to new possibilities. For example, a whole database can be audited in an automated way and, on the other side, manual sampling based on defined criteria can be reduced. The auditor will still have a valuable role to play here: The auditor's profound business knowledge is needed to ask the right questions in the data analytics and to recognise relevant relationships. The auditor's experience is also needed to question management's estimates. However, the profession, or rather the demands on the auditor, are changed significantly by this development.

Artificial intelligence technologies of the future are being discussed intensely today. Mid-term, such technologies have the potential to support the auditor, particularly in the area of auditor judgement. However, professional scepticism toward apparently correct information is likely to remain a human trait which is hardly replaceable.

Another significant question is whether all audit firms can or want to make the necessary investment in digitalisation. In this area, smaller audit firms would be well-advised to join forces and finance the necessary investments together. It also appears possible for audit firms to outsource this field to specialized companies.

Overall, reporting developments and emerging technological advances are to be seen as opportunities for the audit profession to improve audit quality and make the benefits of audit more apparent to the public. The new enhanced audit report requires a more intensive examination of the audit

engagement and will increase confidence in the audit. Mid-term, the audit profession will change considerably, generally-speaking become more relevant and, most certainly, continue to exist in a new form in the future.

Pension scheme audits

There is heightened public interest in the audit of pension schemes. In its inspections of pension scheme audits, however, the FAOA repeatedly finds serious violations of the applicable duty of care. These violations

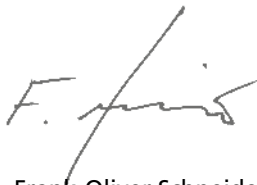
are addressed in detail in this annual report (see separate section). Analysis of these violations raises the question as to whether the legal requirements towards pension scheme auditors and auditors-in-charge are sufficiently selective. This question is all the more relevant as, at a time of neg-

ative interest rates and investment crisis, it can be assumed that pensions schemes will be increasingly compelled to accept higher risks. In this difficult current situation, the work of the auditor contributes greatly to confidence in a sustainable occupational pension.

Berne, 18 January 2017



Thomas Rufer
Chairman of the Board of Directors



Frank-Oliver Schneider
Chief Executive Officer



Key activities 2016

Financial and Regulatory Audit

State-regulated audit firms continue to be inspected periodically. The scope of these inspections is based on an annual risk analysis. Since 2015, the FAOA covers the regulatory as well as financial audit area. A joint inspection was again performed with the US PCAOB at a large audit firm. The volume of whistleblowing investigations in the year under review was comparatively high.

Legal and international

Almost all pertinent legal proceedings went in favour of the FAOA in the year under review. It is noteworthy that the Federal Supreme Court decided that the FAOA may investigate whistleblowing cases even without an explicit legal basis. In the international area, the Federal Council decided upon a moderate de-regulation of the extra-territorial jurisdiction of the FAOA (Art. 8 AOA), whereby the initiative for the submission came from the FAOA.

Licensing

By law, audit firms must renew their licences every five years. Only a few licence renewal applications were received in the year under review. The next great renewal wave is only expected to start in 2018. The number of new licence applications from both firms and individuals was similar to last year.

Third party notifications

The FAOA received 36 (prior year: 35) third party notifications of possible violations of law or professional law in the year under review. Of these, ten (prior year: five) relate to the work of state-regulated audit firms. Eligible and credible notifications lead to FAOA fact-finding. No proceedings (prior year: five) have been initiated to date as a result of notifications received in the year under review. However, two offences relating to auditing without a licence were reported to the prosecuting authorities as a result of notifications.

Regulatory developments

Current projects

Extra-territorial jurisdiction of the FAOA

The Federal Council has not yet implemented the extra-territorial jurisdiction of the FAOA with respect to the auditors of foreign bond issuers, but it submitted a dispatch to the Federal Assembly on 1 July 2015 with a plan for moderate de-regulation. The Federal Assembly approved the draft unchanged on 30 September 2016.

FAOA oversight of the auditors of unquoted foreign bond issuers lapses with the amended law (Art. 8 para. 1 letter b AOA 2016). Oversight of the auditors of foreign-domiciled material subsidiaries is also waived. The latter applies to both share and bond issuers irrespective of whether the issuer is Swiss or foreign-domiciled (repeal of Art. 8 para. 1 letters c and d AOA 2016). In addition, foreign-domiciled bond issuers can waive FAOA oversight of their auditors where there is no, or no equivalent audit oversight authority in their country of domicile. However, investors must be informed explicitly of the absence of state oversight of the auditor (Art. 8 para. 3 letter b and para. 5 AOA 2016). See further remarks under «International» - «Extraterritorial scope of the AOA».

Federal Financial Services Act (FFSA) and Financial Institutions Act (FinIA)

On 4 November 2015 the Federal Council adopted the FFSA and FinIA dispatch. FinIA regulates oversight of all financial service providers providing any form of asset management in one integrated act. The Council of States discussed the draft on 14 December 2016 and transferred it to the National Council. The following regulations are of particular interest to the audit industry:

- Asset managers and trustees will be overseen formally by FINMA but newly-created oversight authorities (OA) (Art. 57 f. D-FinIA in conjunction with Art. 43a f. D-FINMASA) will be responsible for ongoing su-

pervision. As the «extended arm» of FINMA, the OA ensure that asset managers and trustees comply with licensing conditions and legal requirements in performing their work. All regulatory functions on the other hand, including the authority to sanction, are concentrated under FINMA. OA may also supervise financial intermediaries as defined under anti-money laundering law. It is therefore clear that OA, especially the current self-regulatory organisations (SRO), are to be active in the fight against money laundering. In contrast to asset managers and trustees, qualified asset managers¹, fund managers and investment firms are supervised by FINMA. They are to engage an FAOA-licensed regulatory audit firm to perform the regulatory audit. One of the prerequisites is that a state-regulated audit firm licence is held. In addition, the entity and consolidated financial statements are subject to ordinary audit. The other asset managers and trustees are either audited by the OA or are to engage a regulatory audit firm to perform the regulatory audit. The regulatory audit firm licence requires a basic FAOA auditor licence; the same applies to the regulatory auditor-in-charge. With the repeal of Art. 43o D-FINMASA it is unclear who is to approve the special licence (most logically the OA; this is to be clarified). Regulatory audit periodicity is determined by the OA, respectively FINMA (from one to four years in each case).

- State-regulated audit firms will now be licensed for an unlimited period of time (Art. 7 para. 3 D-AOA).
- SRO in the AMLA area will be recognised by FINMA if, amongst other things, they ensure that the regulatory auditors and regulatory auditors-in-charge they engage to perform the control function meet statutory licensing conditions (Art. 24 para. 1 letter d in conjunction with Art 24a D-AMLA). As there will be no financial intermediaries under the direct supervision

of FINMA (DSFI) in the future (they must join a recognised SRO within one year of FinIA coming into force, Art. 42 para. 1 D-AMLA), the licences granted by the FAOA to regulatory audit firms and regulatory auditors-in-charge of such DSFI under current law will be cancelled (Art. 9a para. 4 and 5 D-AOA). Regulation of the relevant licensing conditions is transferred to AMLA. The basic requirement remains that the regulatory audit firm and regulatory auditor-in-charge have an FAOA auditor licence. For the final year before FinIA comes into force, the DSFI regulatory audit remains under FAOA oversight (dispatch on Art.42 D-AMLA).

- The Council of States has established new legal foundations for providing easier market access to FinTech companies, by way of a separate licensing category. These companies are defined as entities primarily working in finance and accepting public deposits of up to CHF 100 million in a professional capacity or soliciting them publicly without investing or paying interest on them. These companies are only required to account under the Code of Obligations (CO), and are thus not required to prepare «true and fair view» financial statements, unlike most other financial institutions (Art. 1a^{bis} para. 3 letter a D-BankA). They are required to have their entity or consolidated financial statements audited under the CO (Art. 1a^{bis} para. 3 letter b D-BankA), which permits a limited audit or the waiver of an audit where relevant thresholds are not exceeded (Art. 727 f. CO). In addition, with respect to the regulatory audit that is still required, the Federal Council can provide for lighter licensing conditions for regulatory auditors and auditors-in-charge

¹ A qualified asset manager is one whose business it is to manage assets on behalf of, and for the account of, collective investment schemes or pension schemes (Art. 20 para. 1 D-FinIA). There are various exceptions to this definition (Art. 20 para. 2 D-FinIA).

(Art. 1a^{bis} para. 3 letter c D-BankA in conjunction with Art. 9a para. 4 D-AOA).

The FFSA creates uniform competition rules to improve customer protection. The Act includes rules for all financial services providers with respect to the provision of financial services and the offer of financial instruments. The FFSA is not expected to have direct consequences for the audit industry.

Amendment of company law

On 23 November 2016, the Federal Council adopted the dispatch to parliament on the amendment of the Code of Obligations (company law, CO). The following points are of particular note from an audit perspective:

- The draft introduces a so-called «capital band». Such a band is also compatible with the waiver of the limited audit if the capital band only foresees the possibility of increasing share capital (Art. 727a para. 2 D-CO). If the lower threshold of the capital band is set lower than the share capital entered in the commercial register, a licensed audit expert must issue an audit confirmation analogous to that issued with respect to a capital reduction (Art. 653w para. 1 section 2 D-CO).
- The general meeting can resolve to pay an interim dividend when, amongst other things, an interim balance sheet (see also Art. 960f D-CO) has been audited by the auditor before the resolution of the general meeting (Art. 675a para. 2 D-CO). Interim dividends cannot therefore be paid by companies that have waived the audit (Art. 727a para. 2 D-CO).
- If the last financial statements show that net assets no longer cover two thirds of aggregated share capital, capital reserves and retained earnings, the board of directors performs a review of the financial situation of the company and takes

measures to rectify the capital loss (Art. 725a para. 1 D-CO). If the company does not have a statutory auditor the last financial statements must, in addition, be subjected to a limited audit by a licensed auditor before their approval (Art. 725a para. 2 D-CO); this audit requirement lapses if the board of directors applies to the court for a moratorium (Art. 725a para. 3 D-CO). The statutory auditor, respectively licensed auditor, acts «with due haste» (Art. 725a para. 4 D-CO).

- If there are reasonable concerns that the liabilities of the company are no longer covered by its assets the board of directors must immediately prepare interim financial statements to going concern and liquidation values. Interim financial statements to liquidation values are not required where the assumption of going concern is given and no over-indebtedness is shown in the interim financial statements. If going concern cannot be assumed financial statements to liquidation values suffice (Art. 725b para. 1 D-CO). The board of directors must engage the statutory auditor, or if there is none a licensed auditor, to audit the interim financial statements (Art. 725b para. 2 D-CO). If both interim financial statements show company over-indebtedness the board of directors notifies the court. The court opens insolvency proceedings or proceeds according to Article 173 of the Federal Law on Debt Collection and Bankruptcy (Art. 725b para. 3 D-CO; moratorium or composition agreement). Court notification is not required where creditors to the amount of the over-indebtedness consent to be subordinated to all other creditors and defer their claims, provided that the subordination covers the amount of the debt and interest payments for the period of the over-indebtedness; or so long as there is a reasonable expectation that the over-indebtedness will be rectified within a reasonable time, not longer than 90 days after the audited interim financial state-

ments become available, and the over-indebtedness will not increase materially (Art. 725b para. 4 D-CO). If the company does not have a statutory auditor the licensed auditor has the notification duties of a statutory auditor performing limited audits (Art. 725b para. 5 D-CO). The statutory auditor, respectively licensed auditor, acts «with due haste» (Art. 725b para. 6 D-CO).

- Properties and participating interests whose actual value has risen above purchase price or production cost can be revalued up to this value to eliminate a capital loss or over-indebtedness (Art. 725c para. 1 D-CO). However, this is only permissible if the statutory auditor, or if there is none a licensed auditor, confirms in writing that the legal provisions have been complied with (Art. 725c para. 2 D-CO, equating to the current Art. 670 CO).
- Where the share capital of a company is not denominated in Swiss francs (see also Art. 621 D-CO), for the purpose of determining audit law thresholds (Art. 727 para. 1 section 2 CO) the reporting date exchange rate applies to the balance sheet total and the average rate for the year applies to sales (Art. 727 para. 1^{bis} D-CO).
- It is clarified that the independence provisions of the law also apply to companies that are controlled by, or control, the audited company or the auditor. The management principle is thereby replaced by the control principle (Art. 728 para. 6 D-CO).
- The auditors of quoted companies now audit the remuneration report as to compliance with the law and statutes (Art. 728a para. 1 section 4 D-CO).
- The general meeting can no longer dismiss the auditor unconditionally but only on important grounds (Art. 730a para. 4 D-CO). The grounds must be disclosed in the notes to the financial statements (Art. 959c para. 2 section 14 D-CO).

- Individuals with auditor liability who have contributed to a loss through carelessness alone are liable up to the amount they would have had to meet in the event of recourse (so-called differentiated joint-liability, Art. 759 para. 2 D-CO).
- In limited liability company legislation, a legislative error has been corrected under which a separate group auditor is to be elected alongside the statutory auditor (Art. 804 para. 2 section 3 D-CO).

Expert mission on required legislative amendments to audit law

With the results of consultation on the ongoing amendment to company law (see above) as a backdrop, the Federal Council instructed the Federal Office of Justice and Police (FOJP) to obtain clarification on the legislative measures required with respect to, and the international development of, audit and audit oversight law. The respective reports are to be available to the Federal Council in autumn 2017 for the determination of further action. In giving this order to analyse, the Federal Council aims to create a sound foundation for the possible re-design, liberalisation or tightening of audit and/or audit oversight law.

By way of a questionnaire, the experts appointed by the Federal Office of Justice (FOJ) asked important interest groups for their views on the need for legislative measures. The FAOA believes that current law has generally been successful. As in every legal area, certain aspects can be optimised but, even taken together, these do not require major legislative measures. The FAOA does believe, however, that pension scheme audits (only pension schemes, not employer-sponsored welfare funds) should, in the future, be performed only by state-regulated audit firms and that an additional special licence should be introduced if necessary (also see the remarks on postulate Ettlín and within «Enforcement and court rulings» – »Pension scheme audits«).

Parliamentary initiative Schneeberger

With the parliamentary initiative «KMU-taugliche Lösung sichern. Eingeschränkte Revision zum Schutz unserer KMU verwesentlichen» of 29 June 2015 (ref. no. 15.472), National Councillor Daniela Schneeberger (FDP/BL; concurrently Central President of TREUHAND | SUISSE) proposed that legal requirements for the limited audit be reduced significantly in the areas of independence, one-off audit services, audit report recommendation to approve the financial statements, duty to notify, documentation and liability.

The TREUHAND | SUISSE proposal is not supported by the other professional associations though. The instrument «limited audit» has generally proved a success in practice. There is no need for a far-reaching change to the law, respectively there is no identified economic need. A dilution of legal requirements on this large scale would, to the contrary, detract from the benefits and reputation of the limited audit over the long term. The FAOA therefore takes a negative stance towards the initiative.

On 19 August 2016, the National Council Committee for Legal Affairs voted 12 to 7, with 4 abstentions, to instruct its Council not to pursue the initiative. The Plenary of the National Council is yet to deal with this matter.

Postulate Ettlín

With the postulate «Keine neue Soft-Regulierung durch die Oberaufsichtskommission Berufliche Vorsorge» of 28 September 2016 (ref. no. 16.3733), State Councillor Erich Ettlín (CVP/OW) wishes to instruct the Federal Council to examine whether the Occupational Pension Supervisory Commission (OPSC) should be instructed not to issue any directive of a licensing nature to pension scheme auditors. The regulatory authority of OPSC is to be restricted or its remit amended as necessary.

The justification given for the initiative is that the draft directive, «Anforderungen an die Revisionsstellen», goes beyond the regulatory authority of the OPSC (Art. 64a para. 1 letter f Occupational Pensions Act (OPA)). The question as to whether quality improvements are needed in the pension scheme audit segment is to be considered as part of the ongoing mission on the legislative measures required within audit and audit oversight law (see above). This avoids duplication of effort between the OPSC and the FAOA.

Notwithstanding the above, on 20 October 2016 OPSC issued the contentious directive. This requires that, as from 1 January 2017, every pension scheme auditor-in-charge must evidence at least 50 chargeable pension scheme audit hours and four specialist training hours per calendar year (section 2.2 of Directive 03/2016 on quality assurance in the OPA audit).

The FAOA does not regard the concerns of State Councillor Ettlín as unwarranted. As already mentioned, the FAOA repeatedly finds serious deficiencies in pension scheme audits (see also «Enforcement and court rulings» – «Pension scheme audits» below). The FAOA therefore supports the aim to establish specific licensing conditions for pension scheme auditors and auditors-in-charge and place them under FAOA oversight if necessary. It believes, however, that an appropriate legislative foundation is required for this and that this should be established within the AOA. In 2014 the legislator decided likewise as regards the various audit firm and auditor-in-charge licences in the financial markets sector (so-called «bundling initiative», AS 2014 4073, in force since 1 January 2015) and therefore showed that there was also a political wish to concentrate audit licensing and oversight under the FAOA.

On 2 December 2016, the Federal Council announced that the compatibility of the directive at issue with underlying legislation would be examined and proposed adoption of

the postulate. The Council of States followed this recommendation on 6 December 2016.

Completed projects

AMLA «trader» audits

Since 1 January 2016 a new category of so-called «traders» exists under AMLA, individuals and companies that are not financial intermediaries according to AMLA but still have a certain duty of care thereunder. Traders are defined as individuals and legal entities that trade in goods professionally and receive more than CHF 100,000 during the course of a trade (Art. 2 letter b in conjunction with Art. 8a AMLA). Traders must engage an auditor to review compliance with the applicable duty of care, whereby auditors under Art. 5 AOA or audit firms under Art. 6 AOA may be engaged. The auditor must have the necessary technical knowledge and experience (Art. 15 paras. 1 and 2 AMLA).

The ordinances clarify that the responsibility of the trader to engage an auditor is independent of the responsibility to have the entity and, if necessary, group financial statements audited under the CO (so-called «opting-out» under Art. 727a CO; Art. 22 para. 1 AMLO).

In the explanatory report on the ordinances it is further clarified that where an individual is engaged as auditor, Art. 8 para 1 AOO applies (to this and the subsequent explanatory report on the Anti-Money Laundering Ordinance (AMLO) – Implementation of the FATF recommendations of 9 July 2016, page 11). This means that the individual must be entered in the commercial register as a sole proprietorship with FAOA auditor licence before being permitted to perform audits at traders.

As mentioned, the auditor must have the necessary technical knowledge and experience of AMLA audits to assure a proper audit. It is the auditor's own responsibility to determine

whether they are competent to perform the audit. The technical knowledge and experience requirements may be met, in particular, if the appointed auditor and the individual performing the audit (auditor-in-charge) hold an FAOA or an SRO licence to audit under AMLA (Art. 9a AOA or Art. 24 para. 1 letter d AMLA) (explanatory report, page 11).

Quality assurance in sole proprietorships

A particular condition an audit firm has to fulfil to be granted an FAOA licence is to have an internal quality assurance system and to monitor its appropriateness and effectiveness (Art. 6 para. 1 letter d AOA in conjunction with Art.9 para. 1 AOO). Such a system requires two expert individuals however; if there is only one the work of that individual cannot be checked, or not sufficiently. According to current law, an audit firm that performs only limited audits at small and medium-sized enterprises has to either implement an internal quality assurance system or join a self-regulatory peer review system by 31 August 2016 (Art. 9 para. 2 in conjunction with Art. 49 para. 2 AOO).

The Federal Council believes though that the audit profession has failed to establish such a self-regulatory peer review system. As there would have been too little time for the almost 1,500 affected audit firms to implement an internal quality assurance system before 31 August 2016, the Federal Council extended the deadline by a year to 1 September 2017. In implementing this decision, the FAOA updated its Circular No. 1/2014 on the internal quality assurance system of audit firms (Circular 1/2014) (margin note 11) and made several editorial changes (margin note 3 and appendix).

Postulat Schneeberger

With the postulate «Steigende Belastung für Treuhandunternehmen.

Kontrolle kann Vertrauen nicht ersetzen» of 24 September 2014 (ref. no. 14.3778), National Councillor Daniela Schneeberger (FDP/BL) asked the Federal Council for a cost analysis regarding fiduciary industry regulation. What was sought was essentially a breakdown of costs, a benefit analysis and proposals on how to reduce unnecessary bureaucracy. The view was thereby taken that the FAOA, amongst others, makes the life of fiduciary companies unnecessarily difficult with a succession of new regulations and controls.

On 19 November 2014, the Federal Council proposed rejection of the postulate to parliament. It took the view that the task had already been completed for three reasons:

- First, most of the specific activities of fiduciary companies are not state-regulated, or at most are regulated by the fiduciary industry itself. Thus (with the exception of the Canton of Ticino), there is no state licensing or oversight authority for companies that perform bookkeeping, prepare financial statements, manage properties, offer tax advice or advise companies. There were consequently no relevant state regulations to examine.
- Secondly, while there certainly are general state regulations, they apply not just to fiduciary companies but to all companies. The areas of statistics, social insurance, accounting and audit, corporate and value added taxes and professional training come to mind. At the end of 2013 the Federal Council prepared a detailed report on the costs of regulation in these areas, with 32 improvement proposals.
- Thirdly, as regards audit, there is a narrowly-defined part of fiduciary company activity that is overseen directly by the FAOA, and thus by federal government. Here also, the relevant inquiries were made in the above-mentioned report of 2013 on regulatory costs. These showed that audit oversight costs

were accepted by the companies surveyed and deemed reasonable by experts. No need for legislative measures was identified.

It should also be mentioned that, according to the Federal Council reports of 2006 and 2014 on the freelance professionals, (fiduciaries are freelance professionals), the fiduciary industry has also seen above average growth in recent years. This is not least due to the fact that new regulations often generate a need for advice, which is then satisfied by the fiduciary industry.

The Federal Council believes that the fiduciary industry is basically well on track. Nonetheless, easing the administrative burden on companies is a core element of its growth policy and the corresponding initiatives continue.

The postulant withdrew the postulate on 14 September 2016, before it could be discussed by the National Council that same day.

Circular No. 1/2008

Circular No. 1/2008 stipulates the standards to be complied with in providing statutory audit services to public interest entities (PIE). In the sense of following international professional law, the FAOA decided on 28 November 2016 to amend the Circular with effect from 15 December 2016.

The following points are noteworthy: First, SAS 880 (review of public takeover offers) was amended by EXPERTsuisse in response to the new legal regulations of FMIA. Secondly, ISA 701 (key audit matters) and related amendments to other ISA were included. Circular No. 1/2015 remains in force, however, until SAS 701 can be brought into force. Thirdly, at the suggestion of the Audit Committee of EXPERTsuisse, the opportunity was taken to delete those SAS and ISA from the Circular that do not involve statutory audit services. Fourthly and

lastly, the new margin note 4^{bis} clarifies that the so-called «conforming amendments» of the ISA are also covered by Circular No. 1/2008, even if no complete new standard with new effective date has come into force.

Financial Audit

Introduction

The structure of the audit market hardly changed compared to the prior year. The «Big 3» audit firms, PwC, EY and KPMG continue to audit the vast majority of public companies and other PIEs. This effective oligopoly should not obscure the fact that there is intense competition between these audit firms today. Driven by EU reforms, further movement is anticipated in the audit market. More voluntary audit tenders are expected.

The FAOA generally inspects state-regulated audit firms every three years. This three-year cycle excludes:

- Those audit firms that audit more than 50 PIEs: These are inspected annually and currently include only the five largest audit firms.
- Those audit firms that audit only financial intermediaries under the direct supervision of FINMA (so-called «DSFI»): A five-year cycle applies here.

A total of 32 audit and regulatory audit firms held a state-regulated audit firm licence at the end of 2016. Eight

firms may only audit DSFI and non-PIEs. Two firms are foreign audit firms that were inspected in the year under review due to the partial enactment of Article 8 AOA.

2016 inspections

The FAOA has completed a total of 90 inspections since the enactment of the AOA. Of these, 13 inspections were performed in the year under review², one of which was performed jointly with the PCAOB (so-called «joint inspection»). The financial statements of 25 companies were the subject of file reviews as part of the 13 inspections.

The selection of audit engagements for an FAOA inspection is risk-based. The market capitalisation of public companies is one important selection criterion. All 20 SMI companies had been subject to an FAOA file review by 31 December 2016. Certain quality aspects of the financial audit at the two, from a global perspective, systemically important Swiss banks (G-SIBs), UBS AG und Credit Suisse Group AG, have been assessed annually by way of a file review since 2013.

In addition to market capitalisation, the FAOA considers other criteria when selecting audit engagements for inspection, such as a major change in audit fees or a change of auditor. A further criterion is a modified audit report at a PIE.

Figure 1
Overview of FAOA inspections and Comment Form findings 2008–2016

Categories	Largest five audit firms		Other		Total	
	01.04.2008 – 31.12.2016	Of which 2016	01.04.2008 – 31.12.2016	Of which 2016	01.04.2008 – 31.12.2016	Of which 2016
Number of inspections	39	5	51	8	90	13
Comment Form Findings Firm Review	125	1	178	5	303	6
Comment Form Findings File Review	394	38	289	19	683	57
Number of inspected files ³	122	16	51	9	173	25

² The inspection fieldwork was completed at a further two of the largest five audit firms. Since the findings process is still at an early stage these are not covered by the Annual Report 2016.

³ 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.

Firm Review

The absolute and average number of findings per inspection at the five largest and at the smaller audit firms continue to decline compared to prior years. This may be due to the relative consistency of ISQC 1 requirements and the increased awareness of those responsible for quality. With respect to the five largest audit firms, it should be noted that the FAOA focuses on file reviews in the intermediate years between PCAOB inspections in Switzerland. This has led to a reduction in the number of firm-level findings in such cases. In the year under review the average number of firm review findings per inspection at the smaller audit firms was around three times as high as at the five largest audit firms. This is despite the fact that the quality assurance systems of the smaller audit firms are less complex than those of the five largest audit firms, the circumstances being simpler. Nonetheless, the standard of quality assurance systems can generally be described as good.

File Review

A total of 25 (prior year: 19) file reviews were conducted and completed in 2016. The 13 inspections resulted in a total of 57 findings. The number of findings per file review thereby fell pleasingly from 3.1 to 2.3 compared to prior year. Specifically, the values at the five largest and at the smaller audit firms fell from 2.9 to 2.4 and from 3.8 to 2.1 respectively. With respect to file reviews, audit quality is heavily dependent upon the partners and staff involved, as well as the external environment. Audit firms should hence continue to focus on the consistency of audit quality.

Under the requirements of Circular No. 1/2010⁴, those audit engagements for which the ratio of non-audit to audit fees exceeds 1:1 in a

business year are to be reported per 30 June. The non-audit services provided, together with the independence safeguards put in place, are to be disclosed for the reportable engagements. As per 30 June 2016, the FAOA had received four reports (prior year: 12 reports), which were critically assessed and, depending on the situation, taken account of in the respective file review strategy.

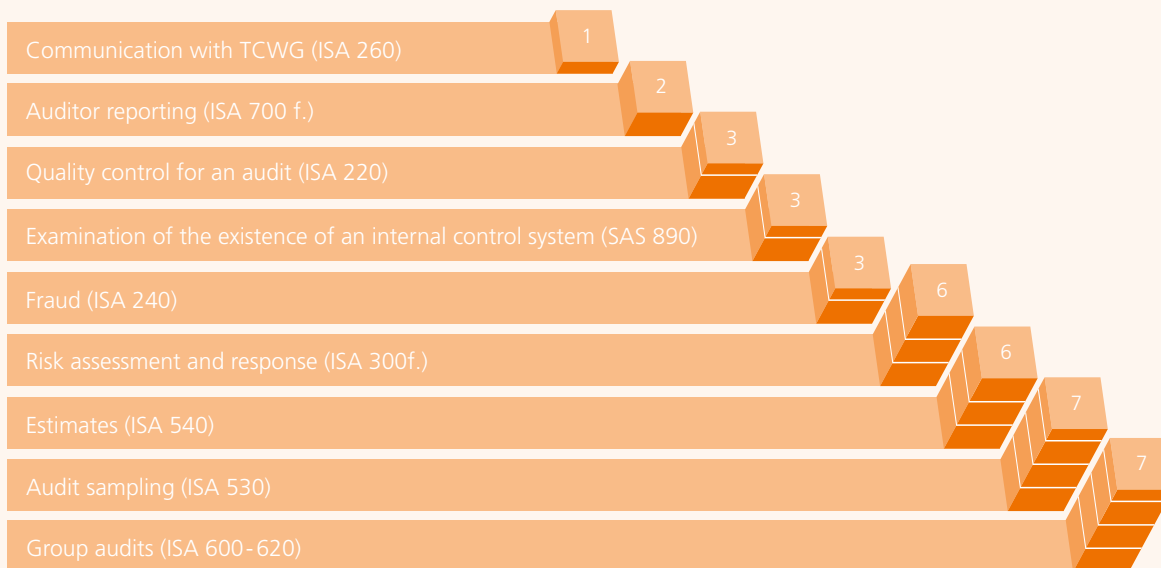
The 2016 file review findings for the five largest and for the smaller audit firms are shown by category in the figures below⁵.

⁴ FAOA Circular 1/2010 of 31 March 2010 on the reporting of state-regulated audit firms to the oversight authority, section 22 letter b.

⁵ For comparability purposes, findings that relate to Swiss Auditing Standards or US auditing standards have been allocated to the identical or comparable ISA.

Figure 2

Type and number of findings from the 2016 file reviews at the five largest audit firms (total 38 Findings)



In the year under review the FAOA identified the most findings in the areas of «group audits», «audit sampling», «estimates» and «risk assessment and response».

In various file reviews it was found that the group auditor obtained insufficient positive assurance from component auditors on material account balances. Against this backdrop, robust audit procedures by the group auditor on non-significant components are of great importance. Examples include auditing the effectiveness of group-wide controls and performing appropriate analytical review procedures. If the group auditor nonetheless concludes that audit procedures performed on significant components do not provide sufficient audit evidence to support the audit opinion, the group auditor is also required to perform specific audit procedures on certain non-significant components. The planning phase is thereby of central importance. The group auditor is only in a position to determine the type of work to be performed at components and draft detailed audit instructions to the component auditors based on this, once a good understanding has

been obtained of the group, its components and its environment. In some instances, it was found that the component auditors failed to comply with the requirements of the group audit instructions without this being taken account of adequately in the group auditor's risk assessment. It is also of note that the larger public companies generate their material sales abroad. Here it is important that the group auditor utilises on-site working paper reviews to a greater extent in assessing the quality of component auditors' work. The inclusion of a multi-year rotation plan within audit planning is to be recommended.

The auditing standard on audit sampling includes clear requirements that have generally been further refined within the individual internal audit methodologies of the respective audit firms. Audit sampling is used in auditing the effectiveness of controls as well as for substantive testing. Due to the importance and number of findings in this area, the FAOA has determined it to be a point of focus for the 2017 inspections (see section «Points of focus for 2017 inspections»). The following issues were found repeatedly here.

- Sample selection was not performed in such a way that every item within the overall population had a chance of being selected;
- Where sample testing was performed at the interim, the period remaining to the balance sheet date was not adequately considered;
- Substantive testing samples did not cover the whole population sufficiently. No meaningful conclusion could thus be drawn for the total population;
- The nature and cause of exceptions and incorrect presentation were not appropriately assessed.

As in the prior year, findings on the audit of estimates relate most particularly to the account balances goodwill and other intangible assets. Contrary to auditing standard requirements, certain audit teams obtained insufficient audit evidence to support management's estimates and assumptions for these balances. This also includes, for example, a critical assessment of the assumptions used in the business plans of the prior year. Information received from

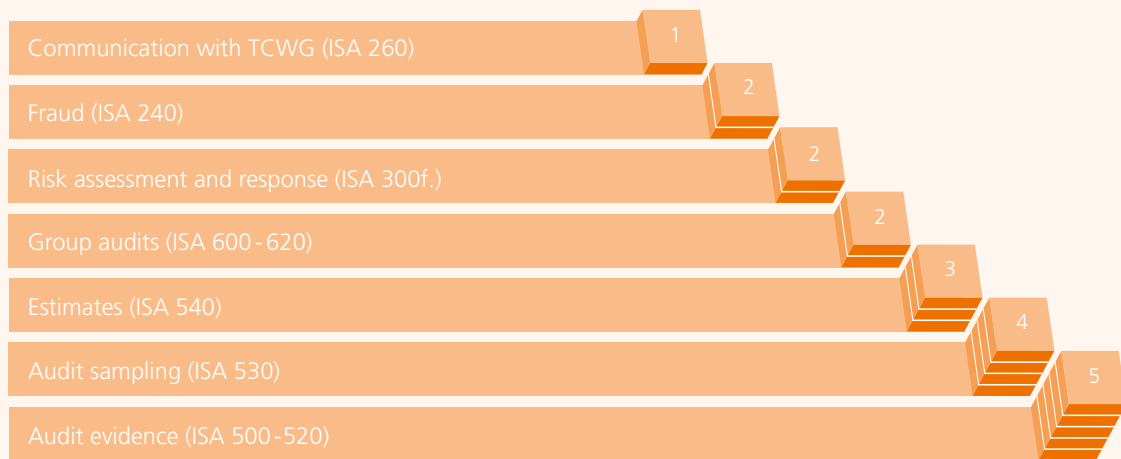
management is also to be confirmed using other audit procedures.

Risk assessment and response also covers general IT and application controls. If an auditor wishes to rely on the effectiveness of general IT and application controls these controls have to be tested adequately. The auditor cannot otherwise rely on system-generated documents that,

in turn, form a basis for the audit of various account balances. In some instances, however, reliance was placed on IT and application controls without them being tested adequately. It often appears that these findings result from a lack of professional scepticism and the insufficient assessment of, and response to, risks of material misstatement.

Figure 3

Type and number of findings from the 2016 file reviews at the smaller audit firms (total 19 findings)



At the smaller audit firms deficiencies in audit evidence, audit sampling and the audit of estimates were found repeatedly. In many cases insufficient audit evidence resulted from inadequate planning.

IFIAR survey on inspection results

IFIAR published the results of a broad-based survey on 3 March 2016⁶. 29 IFIAR members took part in the survey. This is already the fourth survey of this type, identifying common findings at the six largest global audit firms on an anonymous basis. The survey concentrates particularly on file review findings at PIEs and systemically important financial institutions. Based on the survey, IFIAR negotiates with the six large audit firms⁷ at a global level. The negotiations aim to agree on joint measures to improve audit quality.

Analysis of FAOA findings and those of other oversight authorities shows similarities in the following areas, amongst others:

- Recoverability of fair-valued assets
- Internal controls
- Revenue recognition
- Group audits
- Identifying and responding to risks of material misstatement

IFIAR members continue to believe that the global audit networks and local audit firms must make further coordinated efforts to permanently eliminate recurring deficiencies in the above-mentioned areas. IFIAR reached an agreement with the six largest audit firms to meet this goal. Specifically, the number of PIE companies with at least one finding is to be reduced from 39 percent to 29 percent over the next four years (reduction around

25 percent). As in the prior year, the importance of the root cause analysis for deriving appropriate and sustainable measures was further highlighted. The FAOA has also drawn its conclusions from this. First, the criteria for classifying a file review finding as a comment form have been amended to take greater account of the potential likelihood and extent of its impact on the consolidated financial statements. This may tend to reduce the number of findings in the future. Secondly, the FAOA has augmented its assessment of the quality of audit firms' root cause analyses with respect to internal monitoring and FAOA findings.

⁶ www.IFIAR.org > IFIAR Global Survey of Inspection Findings.

⁷ BDO International Limited, Deloitte Touche Tohmatsu Limited, Ernst & Young Global Limited, Grant Thornton International Limited, KPMG International Cooperative and PricewaterhouseCoopers International Limited.

Points of focus for 2016 inspections

The FAOA published its points of focus for the 2016 financial audit inspections in the 2015 Activity Report and examined these in detail in the year under review⁸:

- Audit of income tax positions in the income statement and balance sheet (ISA 540/IAS 12)
- Audit of the cash flow statement (ISA 500/IAS 7)
- Audit of earnings per share (ISA 500/IAS 33)

The FAOA analysed the internal guidelines of the five largest audit firms with respect to these inspection focus areas and tested their application on a sample basis.

estimates and assumptions regarding forward-looking information. Most especially as regards deferred tax assets relating to carried forward losses, an assessment has to be made as to the probability that future taxable profits will be available. This requires the audit team to perform robust audit procedures with professional scepticism.

The FAOA assessed compliance with the auditing and accounting standards that apply to the audit of tax positions in its file reviews. Out of a total of 12⁹ selected audits covering various industries, the FAOA inspected the audit of tax positions in eight. All but two companies prepared their financial statements under IFRS.

Audit of income tax positions in the income statement and balance sheet

Subject to certain selective amendments, the accounting standard IAS 12, «Income taxes», has now been in force in its current form since 1 January 1998.

The audit of taxes can present a challenge to audit teams where there are groups and complex tax structures, as various auditing standards (e.g. ISA 500, ISA 540, ISA 600) can come into play alongside IAS 12. Robust audit planning, in which the auditor evaluates fundamental questions, always serves as good preparation. This includes, for example, evaluating the complexity of group tax structures and risks and the significance of deferred taxes. The involvement of experts by management and the need to involve an expert also has to be evaluated. Especially with groups and differing tax regimes, the complexity of the tax area increases the need for expert tax knowledge. Where there are material tax positions at components proper group audit instructions and communication with the group auditor are essential. The audit of deferred tax involves uncertainties,

⁸ For the results of the Regulatory Audit 2016 points of focus see section «Regulatory Audit».

⁹ The inspection reports on two of the five largest audit firms were yet to be finalised at the reporting date and are therefore not included in the evaluation.

Figure 4
Summary of files selected for the inspection of tax positions

File	Risk assessment			Auditor's specialist (group)	Deferred tax assets			Deferred tax liabilities	
	Group audit	Tax structure	Significant risk		Temporary differences	Losses carried forward	Not capitalised	Temporary differences	Not accrued
1	Yes	Simple			Yes	Yes		Yes	
2	Yes	Simple			Yes			Yes	
3	Yes	Complex	Yes	Yes	Yes	Yes	Yes	Yes	Yes
4		Simple		Yes	Yes			Yes	
5	Yes	Simple			Yes	Yes	Yes	Yes	Yes
6	Yes	Simple			Yes	Yes		Yes	
7	Yes	Complex	Yes	Yes	Yes	Yes	Yes	Yes	Yes
8	Yes	Simple		Yes	Yes	Yes	Yes	Yes	Yes

In two of the inspected audits, group tax structures were considered complex based on risk assessment. There was consequently deemed to be a significant risk of material misstatement at these companies.

The computation of tax amounts and the preparation of the tax notes was undertaken by the tax department of the audited company in each case. External tax specialists were generally not involved, or only in an advisory capacity and for specific issues (e.g. transfer pricing). Half the audit teams inspected involved their own specialists. These included the two audits in which tax positions were deemed a significant risk. The specialist of the group auditor¹⁰ covered all tax relevant matters, such as the determination of parameters and computation methods for current and deferred taxes. This involved auditing holding-level tax positions on the one hand and evaluating component auditor reporting on the other.

The group audit instructions were adequate in this area. Additional local specialists were involved at component audits with significant tax risks. The component tax audit at the other companies was performed by the component auditor but coordinated and supervised by the group auditor.

No findings resulted from the FAOA inspection of current tax working papers.

All companies whose audit was inspected disclosed material deferred tax assets and liabilities relating to temporary timing differences. Six companies capitalised deferred tax assets arising from carried forward losses. Additionally, unrecognised deferred tax assets and liabilities were disclosed in the notes in four cases. The FAOA identified deficiencies in the audit of deferred tax assets in two of the files sampled, each of which led to a finding.

In the first case, material deferred tax assets arising from temporary differences were capitalised. The underlying assumptions and estimates (e.g. budgets) were not audited with sufficient scepticism. The principle applying here is that deferred taxes may only be capitalised where it is probable that there will be sufficient future taxable profits to use the temporary differences against. In addition to the above, the auditor in question also failed to challenge the assumptions and estimates of management with respect to provisions for uncertain tax positions or assess the run-off of the respective prior year provisions.

In the second case, neither the group auditor nor the component auditor performed sufficient audit procedures over the recoverability of material deferred tax assets arising from temporary differences and tax losses carried forward. The accounting standards require that the book value of tax assets is tested for recoverability at each period end. Auditor professional scepticism is especially important in the audit of deferred tax assets and tax provisions due to estimation uncertainty, which arises from such factors as the number of tax authorities involved, the complexity of the company's tax structures and assumptions concerning future earnings.

To sum up, the FAOA inspections showed that, with the exception of both above-mentioned findings, the inspected audit teams audited the tax positions with due care and professional scepticism. Specialists were also involved where significant risks existed. The FAOA applauds the involvement of specialists in complex situations.

¹⁰ The specialist of the auditor in one case where there were no consolidated financial statements.

Audit of the cash flow statement

Subject to certain selective amendments, the accounting standard IAS 7, «Statement of cash flows», has now been in force in its current form since 1 January 1994. The cash flow statement groups cash flows under operating, investing and financing activities. It also forms part of the primary financial statements and is an important performance indicator for stakeholders.

The FAOA assessed compliance with the auditing and accounting standards that apply to the audit of the cash flow statement in its file reviews, which covered nine audits across various industries¹¹.

Three of the five largest audit firms use a standard cash flow statement audit programme. The FAOA found from its sample that audit teams documented the cash flow preparation process satisfactorily but did not rely on the effectiveness of controls. The FAOA assumes that a purely substantive approach was taken on efficiency grounds. In eight of the nine sampled cases management prepared the cash flow statement under the indirect method. Alongside material cash flows from investing and financing activities, the audit team therefore also audited the non-cash expenses and income added to, respectively deducted from, the operating result.

Substantive testing was designed and performed satisfactorily in terms of nature and scope with one exception. In this case the operating cash flow contained an error which exceeded planning materiality. In addition, two other significant cash flow statement positions were not audited sufficiently.

Audit of earnings per share

The accounting standard IAS 33, «Earnings per share», has now been in force in its current form since 1 January 2005. Quoted companies that prepare their entity, respectively group, financial statements under IFRS must

disclose earnings per share on their income statement¹². The aim of this requirement is to improve comparability of results for different companies and over multiple accounting periods. Earnings per share is a basis for determining the price-earnings ratio¹³ that is, in turn, central to share valuation.

Compliance with relevant audit and accounting standards was examined for a total of nine audit engagements¹⁴. Seven involved checking compliance with IFRS, one compliance with US-GAAP¹⁵ and one compliance with Swiss GAAP FER¹⁶. Earnings per share was not identified as a significant risk on any of the engagements. However, in two engagements the audit team determined IFRS compliance of the entity, respectively group, financial statements to be a significant risk. In three of the nine cases the entity, respectively group, financial statements were additionally reviewed by an accounting specialist independent of the audit team. Surprisingly, in the cases where IFRS compliance had been determined to be a significant risk no additional IFRS specialist review was arranged. The auditor-in-charge did not review the audit working papers relating to earnings per share in any of the audit engagements examined. The audit teams on all the engagements examined used so-called «disclosure checklists», the purpose of which is to achieve complete and accurate financial statement disclosure. One of the largest audit firms had developed a separate audit programme that audit teams were required to use in addition to the disclosure checklist. None of the audit firms inspected required consultation with respect to earnings per share.

Although other studies¹⁷ suggest that the computation and disclosure of earnings per share is subject to a relatively high error quota, the FAOA had only two findings on compliance with accounting standards at the audit engagements examined. In one case, it was found that the calculation of diluted earnings per share wrongly included shares that had already been issued. This did not affect disclosure

materially due to the small number of shares. In a second case, the financial statements did not disclose diluted earnings per share even though the audited entity had a dilutive participation plan. These findings may have resulted from a lack of accounting specialist involvement or a lack of review by an experienced audit team member.

In five of nine cases earnings per share was also disclosed in a part of the financial statements (so-called «other information») that is generally unaudited (e.g. management report, summary of performance indicators). In one case sampled, an earnings per share amount «normalised» for special items, such as restructuring and impairment charges, was disclosed by the company in the unaudited part of the financial statements alongside the IFRS earnings per share. On the positive side, it is to be noted that the company informed readers of the differing computational bases and disclosed a reconciliation¹⁸.

¹¹ The inspection reports on two of the five largest audit firms were yet to be finalised at the reporting date and are therefore not included in the evaluation.

¹² Analogous to other national and international accounting standards.

¹³ The price-earnings ratio shows share price in relation earnings per share.

¹⁴ The inspection reports on two of the five largest audit firms were yet to be finalised at the reporting date and are therefore not included in the evaluation.

¹⁵ Financial Accounting Standards Board (FASB), Accounting Standards Codification (ASC) Topic 260, Earnings per Share.

¹⁶ Swiss GAAP FER 31, Ergänzende Fachempfehlungen für kotierte Unternehmen, Paragraph 5. FER 31 is first effective for financial statements beginning on or after 1 January 2015.

¹⁷ Refer particularly to Hüttche Tobias, Dicke Bretter, wenig Späne – Entdeckte Fehler in der IFRS-Rechnungslegung. Eine Analyse von Fehlern in Finanzberichten, den Ursachen und Hinweisen zu ihrer Vermeidung, Der Schweizer Treuhänder 2012, page 79 f.

¹⁸ In this regard, reference is made to the IFAC guideline «Developing and Reporting Supplementary Financial Measures – Definition, Principles, and Disclosures», that aims to achieve the consistent and transparent disclosure of «non-GAAP measures» by reporting companies.

For the responsibilities of audit teams regarding other information reference is made to ISA 720 (revised)¹⁹, first effective for the audit of entity, respectively group, financial statements ending on or after 15 December 2016. This requires the inclusion of a separate paragraph on other information in the auditor's report. Specifically, in addition to identifying the other information and those responsible for preparing it, the audit team also states whether its review has identified inconsistencies or errors.

Root cause analysis and measures Annual process for organising the root cause analysis and determining measures

After inspections are completed the respective audit firms are provided with a draft report. The audit firm is then asked to send the FAOA written root cause analyses, measures and deadlines for the findings. It should be noted here that responsibility for drafting the root cause analyses and measures for file-level findings lays primarily with audit firm management and not the engagement team concerned. The FAOA assesses the reasonableness of the proposed measures by developing its own potential root causes and measures for the findings. The proposed measures and deadlines proposed by the audit firm are then taken over and firmed-up or re-worded by the FAOA if necessary. The audit firm has one year to implement the agreed measures. The FAOA assesses the adequacy of implementation in the following year.

The cause of findings is determined using professional judgement and is an iterative process that has to be conducted in a uniform way. The «5-Why-Method»²⁰ is commonly used in practice²¹. The more standardised and sound the execution of the root cause analysis is, the more sustainable are the measures.

The FAOA differentiates between engagement and firm-related measures at file level. The latter are particularly

used if the FAOA has identified recurring findings that suggest systemic risk. In determining root causes and measures the areas considered by the FAOA include:

- Vision and strategy (e.g. determination and realisation of sales and profit targets);
- Internal and external communication (including «tone at the top»);
- Quality assurance process (including controls);
- Directives, regulations and audit requirements;
- Tools and aids.

It is then determined whether the causes arose from the violation of internal requirements or whether the auditor-in-charge and EQCR failed to meet their responsibilities toward audit planning, direction, supervision and execution appropriately.

The FAOA generally requires certain specific measures on every inspection. First, the inspection results are to be communicated to all employees by the CEO and head of audit. Secondly, greater involvement of the auditor-in-charge and EQCR at file-level is expected. At the five largest audit firms a person independent of the engagement team is also to check the implementation of measures and record the results in writing.

By way of example, the following specific measures were agreed to with audit firms:

- Independence procedures include more formal consultations and a severer sanction catalogue. In this regard, the respective audit firm appointed an additional person (Risk-Manager).
- With respect to the audit of goodwill, engagement teams at all public companies are to follow a directive and separate audit programme.

- Prohibition of an auditor-in-charge from providing audit services to a company in a specific industry.
- Prohibition on serving as an EQCR on public companies due to function.

In the case of severe deficiencies, the FAOA can also use the civil²² and criminal law provisions²³ of the AOA. See chapter «Enforcement und court rulings» in this regard.

Analysis of recurring findings from the last five years

With the aim of assessing recurring findings and for the first time, during the year under review the five largest audit firms summarised the internal monitoring and FAOA findings of the previous five years or more. Potential root causes and measures were then determined. The results from four audit firms were discussed at separate meetings²⁴. The FAOA will take appropriate account of the information obtained in determining its strategy for the forthcoming inspections. It is pleasing that this process has already led to the voluntary initialisation of concise measures.

¹⁹ ISA 720 (revised), «The Auditor's Responsibilities relating to Other Information», is effective for the audit of financial statements ending on or after 15 December 2016.

²⁰ The 5-Why-Method [...] is a quality management method to determine cause and effect. The use of the five «why?» questions is aimed at determining the cause of a defect or problem. The number of questions is not limited to five, this number being symbolic. It is important that questions continue to be asked until the process step causing the problem is identified unequivocally and cannot be apportioned further.

²¹ An alternative method could also be, for instance, the «Fishbone Diagram».

²² Art. 16 para. 4, 17 and 18 AOA.

²³ Art. 39 f. AOA.

²⁴ The meeting with the fifth audit firm takes place in January 2017.

Preliminary fact-finding and proceedings

In addition to routine inspections, event-driven preliminary fact-finding and proceedings are also conducted at state-regulated audit firms. The FAOA hereby takes particular account of plausible information from third parties. In the year under review the FAOA received eight notifications from third parties relating to the work of state-regulated audit firms. Preliminary fact-finding was conducted as a result of these notifications during the reporting year but no proceedings were opened. Certain work that began in the prior year could not be finalised during the year under review (e.g. FIFA case).

The FAOA has collected performance indicators from the Big 5 audit firms for eight years now. The FAOA uses these performance indicators primarily for the timely analysis and identification of trends and factors that may impact audit quality. In addition, the performance indicators are used for risk assessment and inspection planning.

The FAOA collects a total of 12 performance indicators. In 2014 many of the performance indicators were revised and further developed to improve their informative value and comparability.

Audit quality indicators

The importance of audit quality indicators (AQI) continues to increase at the international level. This growing trend is underlined by various projects. In July 2016, the FEE (now: Accountancy Europe) published an updated summary of nine different organisations from across the world that have developed AQI, including the FAOA²⁵. Further, in February 2016, IFAC provided information on a project of the Center for Audit Quality CAQ for measuring audit quality through key indicators²⁶. These key indicators will be provided to audit committees. ACRA, the oversight authority in Singapore, made a framework available that includes eight AQI and can be used voluntarily by public company audit committees from 2016²⁷. In 2014 the six largest UK audit firms mutually agreed to publish a number of performance indicators in their transparency reports²⁸. A US audit firm has also already started to disclose 16 performance indicators voluntarily²⁹.

²⁵ The information is included in a so-called «Information Paper» under the title «Overview of Audit Quality Indicators Initiatives; Update to December 2015 edition». The 2016 Annual Report of «Accountancy Europe» also deals with this subject (www.accountancyeurope.eu > publications > annual report; page 24).

²⁶ www.ifac.org > Global Knowledge Gateway > Viewpoints > Audit Quality Indicators.

²⁷ www.acra.gov.sg > Publications > Guides > ACRA's Audit Quality Indicators Disclosure Framework.

²⁸ www.frc.org.uk > home > publications > FRC Team, Professional Oversight > 30 March 2015 Transparency Reporting by Auditors of Public Interest Entities: Review of Mandatory Reports.²⁹ www.pwc.com > PwC US > Audit and Assurance > Our focus on audit quality > 2016 Audit Quality Report.

²⁹ www.pwc.com > PwC US > Audit and Assurance > Our focus on audit quality > 2016 Audit Quality Report.

Figure 5

Comparison of selected performance indicators relating to the audit function of the five largest stateregulated audit firms

Audit quality indicator	2013		2014		2015		2016	
	from	to	from	to	from	to	from	to
Average annual revenue per audit partner in CHF mio.	1.6	4.3	1.7	4.2	1.9	4.5	1.8	4.2
Ratio of non-audit fees to audit fees								
- SMI companies	n.a	n.a	0.1	0.4	0.2	0.4	0.2	0.5
- Non-SMI public companies	n.a	n.a	0.1	0.3	0.1	0.4	0.0	0.2
Number of staff per partner	6.8	13.5	7.1	14.0	7.2	15.8	7.4	15.3
Staff turnover in %	12	26	13	26	13	25	12	27
Average number of EQCR³⁰ hours								
- SMI companies	n.a	n.a	39	151	37	115	25	116
- Non-SMI public companies	n.a	n.a	7	18	6	17	8	17
Average number of auditor-in-charge hours								
- SMI companies	n.a	n.a	270	719	227	746	351	700
- Non-SMI public companies	n.a	n.a	69	112	71 ³¹	110	75	113
Number of foreign shared service centre hours as a % of overall hours at public companies	n.a	n.a	0	5	0	8	0	7
Number of consultations per public company audit	n.a	n.a	0	0.4	0	0.3	0.1	0.4

- The highest and lowest average annual revenue per partner fell compared to the prior year due to an increase in the number of partners. At the other three audit firms the average revenue per partner increased. Over the last four years the same two audit firms have shown the highest and lowest average annual revenue. This performance indicator is affected by the size, or rather fee volume, of the companies audited and on the staff to partner ratio. The audit firm with the lowest, respectively highest, revenue per partner consequently has for years had the lowest, respectively highest, number of staff per partner.
- The FAOA sees the ratio of non-audit to audit fees at public company audit clients as a risk factor as regards independence. Compared to the prior year, the range for this performance indicator has increased at SMI companies and fallen at other public companies. In the reporting year 2016 one audit firm shows a value for SMI companies that is more than double the average for the other audit firms. This audit firm has also shown the highest amount for SMI companies since 2014. It should be noted in this respect that the highest average ratio of 0.5 is lower than the EU limit of 0.7. The notifications made to the FAOA further show that only four engagements (prior year 12 notifications) exceeded the 1:1 threshold and thus exceeded the EU limit.
- The range for staff turnover increased compared to the prior year and shows major differences between audit firms. One audit firm has shown the highest staff turnover in three of the last four years. At two other audit firms staff turnover increased compared to the prior year and at the remaining two it fell. One audit firm has shown the lowest staff turnover since the performance indicators were first collected.

³⁰ Engagement Quality Control Reviewer.

³¹ One audit firm corrected this prior year performance indicator.

- An EQCR must be used at public companies. At three audit firms the number of EQCR hours per public company fell between 14 and 32 percent. The average number of EQCR hours per public company varies widely between audit firms. The larger the audited engagements, the higher the proportion of EQCR hours. The average number of EQCR hours at SMI companies is also several times that at other public companies. The average number of hours is subject to annual fluctuations and affected by engagement-specific factors.
- There is a significant difference between audit firms in the average number of auditor-in-charge hours at SMI companies. This performance indicator rose 22 percent, respectively 55 percent, at two audit firms and fell six percent, respectively seven percent, at two others. The reasons for the differences are basically the same as for the average number of EQCR hours per public company. Here as well, the average number of auditor-in-charge hours at SMI companies is several times that at other public companies.
- Until now two of the five large audit firms have deployed foreign shared service centres (SSC). During the year under review another audit firm began to outsource certain audit work to a foreign SSC. These hours will be included in the next FAOA survey. The involvement of domestic SSC is not considered in this performance indicator. The amount of the performance indicator fell at one audit firm and rose at the other.
- Consultations have increased at both the upper and lower end of the range compared to the prior year. The proportion of formal consultations to audited public companies is the same at three audit firms. At these firms, around two formal consultations are made per ten public companies. The FAOA believes that consultation on complex questions improves audit quality.

Cooperation with stock exchanges

To avoid duplication the FAOA coordinates its financial audit oversight activities with the stock exchange.

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 overlaps. The FAOA assesses the audit activities of audit firms. SER, on the other hand, assesses issuers' compliance with their responsibilities under the listing regulations. The focus of FAOA inspections is upon auditor compliance with legal and professional requirements, and not directly upon compliance with accounting standards. Should the FAOA find material breaches of accounting standards during its inspections, it notifies the responsible exchange in writing. There were no such notifications in the year under review.

Standard setting

Swiss Auditing Standards

Companies preparing financial statements under Swiss GAAP FER usually have them audited exclusively under SAS. Companies preparing their financial statements under international standards (e.g. IFRS, US GAAP) must always be audited under SAS in addition to the relevant international auditing standard (ISA, PCAOB) (Circular No. 1/2008). In this context, the FAOA continues to support the timely transfer of ISA into SAS. Differences currently exist between ISA and SAS as regards changes to ISA 260, ISA 315, ISA 570 and ISA 610 that have not been adopted. Differences also exist as regards the audit report and the audit of other information (ISA 700, 701, 705, 706, 720). Differences with respect to the new audit report were eliminated by Circular No. 1/2015.

International auditing standards

The FAOA issues its own auditing standards only in exceptional cases. In this connection, however, the further development of international and national auditing standards is an important element in improving audit quality. The FAOA develops responses to drafts of new or revised standards in collaboration with other oversight authorities. Each of the responses is published on the FAOA website.

Through its cooperation with the EAIG and IFIAR, the FAOA submitted comment letters on various IESBA and IAASB proposals:

- In April and May 2016 the EAIG and IFIAR submitted comment letters on the independence-related «Proposed Revisions Pertaining to Safeguards in the Code of Ethics for Professional Accountants - Phase 1».
- In June 2016 IFIAR responded to the IAASB's invitation to comment on «Enhancing audit quality in the public interest», which proposes changes to various auditing standards.

The current activities of the IAASB, based on the discussion paper on enhancing audit quality, will lead to revised standards. The extensive comments received have led the IAASB to prioritise the quality control and group audit areas.

Points of focus for 2017 inspections

The FAOA has selected the following points of focus for the 2017 routine inspections of state-regulated audit firms:

Financial audit

- ISA 701 reporting, respectively FAOA Circular No. 1/2015 (new audit report with key audit matters).
- Audit of provisions in the balance sheet and income statement (ISA 540/IAS 37)
- Evaluation of sample testing for material audit balances (ISA 530)

Regulatory audit

- Internal organisation and audit procedures relating to ICS effectiveness
- Audit of AMLA requirements, particularly business relationships, higher risk transactions and the identification of PEP's
- Fulfilment of the current and applicable FINMA minimum audit requirements

Further points of focus arise from the individual analysis of specific circumstances and relate to the application of the relevant auditing or accounting standards.

Cooperation with audit committees

Audit Committees have a major influence on audit quality. Consequently, contact with Audit Committee chairmen was maintained in the year under review. In each case, contact is made as part of the file reviews at state-regulated audit firms and is now conducted by way of face-to-face meetings.

The communication with audit committees is aimed at gaining a better picture of the cooperation between

the auditor and the audit committee. Professional cooperation can significantly enhance the professional scepticism of the auditor towards management. This is particularly so where the audit committee creates an environment which makes it easier for the auditor to challenge management.

In the year under review and for the first time, the FAOA reviewed audit engagement proposals from the five largest audit firms. This review provided the FAOA with an understanding of the information audit committees are supplied with as regards audit quality. It is notable that audit firms strongly emphasised their competence in the data analytics area, even though the implementation of the relevant technology in Switzerland is not far advanced in some cases. It was also found that fees fell after the tender process in most cases.

AQI were either not supplied to audit committees or only sparingly. The FAOA supports the emerging trend to prepare such performance indicators for audit committees. This information helps an audit committee assess the quality of the audit firm and the auditor-in-charge. In doing so, the performance indicators only supplement other measures (meetings with the individuals responsible etc.). The AQI also play a part in putting more focus on quality in the competition between audit firms and less on quantitative factors. The FAOA is not presently seeking to define performance indicators by regulation. It would prefer that they become established by way of self-regulation or best practice.

The FAOA will further develop its contact with audit committees where possible. A seminar for audit committees is thus planned for future years, if necessary in cooperation with professional or economic associations. The existing guide for audit committees³² will also be updated periodically based on experience gained.

Data Analytics

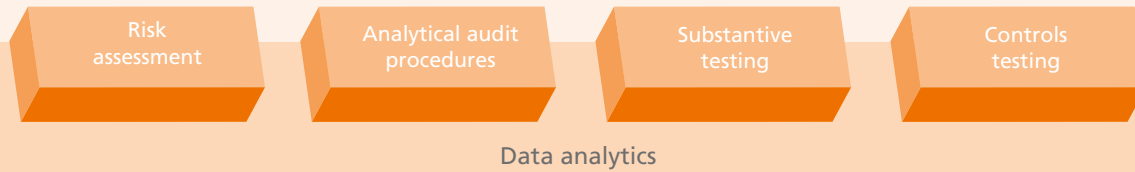
With rapid technological developments, accompanied by ever faster and more complex data processing, the audit industry is increasingly focused on looking at company data holistically. The use of data analytics technology in a mass data environment can improve audit quality. This increases expectation on the part of both audit client and auditor that there will be a push to use such technology in the audit. The present focus is on developing data analytics tools and techniques.

This presents a new challenge to the auditor, particularly on audits of larger and international companies. The analysis of mass data places new and exacting demands on auditor skills and competencies and requires large investment in hardware and software³³. Depending on their application, data analytics allow for more relevant information to be used for risk assessment, for in-depth substantive testing and for comprehensive controls testing. It appears possible to achieve 100% coverage in testing control effectiveness. Moreover, the analytical procedures can be supported by external data, such as external pricing sources for interest rates, exchange rates, share prices, growth rates (e.g. peer group turnover, gross domestic product) and other benchmarks. This can involve simple routines or highly complex calculations. The auditor must be able to understand the latter to assess the results.

³² The Audit Committee Guide contains the professional opinions of the FAOA. These professional opinions are only recommendations and not «soft law».

³³ Data analytics for external auditors – International Auditing Perspectives; an International Accounting, Auditing & Ethics initiative, ICAEW 2016.

Figure 6
The use of data analytics goes beyond traditional analytical audit procedures³⁴



The largest four audit firms have developed their own global-level platforms for data analytics tools, while the medium-sized audit firms tend to cooperate with third party providers. Small audit firms hardly appear to have considered the use of data analytics as yet though.

The proposals of the largest four audit firms show the use of data analytics as a special differentiating factor.

The FAOA inspected a sample of the largest 2015 proposals. Various analytical techniques are offered, dependent on the IT environment of the prospective audit client. These range from the complete analysis of data or controls in a particular audit area (e.g. debtors) to particular audit aspects, such as the audit of fraud risk. The following table shows the results of the inspected proposals.

Figure 7
Use of data analytics techniques in proposals

Percentage of inspected proposals in which data analytics are used	Audit firm A	Audit firm B	Audit firm C	Audit firm D
Identification and assessment of risks	80 %	14 %	0 %	60 %
Audit of processes and controls	80 %	43 %	80 %	100 %
Audit of transactions	80 %	86 %	100 %	0 %
Journal entry testing with respect to fraud	20 %	43 %	80 %	80 %

The sample illustrates that data analytics are generally to be used in the audit of potential clients for analysing financial processes and controls and for testing transactions. Data analytics are also often to be used for more effective journal entry testing. Two of the four audit firms regularly offer the use of data analytics already in the planning phase, for risk identification and assessment. It is apparent from the sample, however, that two audit firms plan to use analytics tools neither for risk analysis nor for transactions testing. Ultimately

though, the proposal offer depends on the resources and analysis tools the audit firm has.

The most varied statistics³⁵ can be compiled and visualised with data analytics, offering insightful information to both the audit team and the client. Only exceptions are investigated as part of audit data analytics. Expected exceptions must first be separated from the unexpected, as only the latter are significant to the auditor. This requires the users of analytics tools to have been trained

appropriately and understand the analytics. If searches are not properly set, thousands of exceptions requiring investigation may be reported.

In the year under review the FAOA looked at these developments intensely for the first time to assess their impact on audit quality.

³⁴ Data Analytics Working Group – Exploring the Growing Use of Technology in the Audit, with a Focus on Data Analytics (IAASB).

³⁵ For example, performance indicators and trends by region or subsidiary, number of manual bookings.

The first phase involves understanding how far advanced the audit firms are in developing their aids and to what extent data analytics are used in the audit. Our interviews with those responsible at the largest four audit firms show that the technologies offered varied possibilities but their application is only at an early stage of development. It is still unclear what the precise effects on the audit will be. All firms currently have a great need for training in the introduction and use of analytics tools. At present, gains appear to be in audit quality rather than efficiency. Communication with management and audit committees has also been improved as more detailed information is available on the results of their companies' audits.

Data analytics are not only occupying audit firms and regulators but also standard setters. In mid-2015 the IAASB initiated a data analytics working group³⁶, to gather information on the various ways that data analytics might be used in the audit (e.g. impact on risk assessment, testing methods, analytical procedures and electronic audit documentation). Various interested parties were contacted for this purpose, including audit firms, national auditing standard setters, oversight authorities, IFAC member organisations and their representatives³⁷. The working group also participates in current IAASB projects and initiatives³⁸, thereby investigating the role data analytics could play.

The new requirements can already be seen in the profiles on the job portals of the largest four audit firms. Data specialists familiar with analytics systems are increasingly in demand. This could increase the attractiveness of the auditing profession provided the auditor has increased IT competence. Besides the advantages of data analytics, it must not be forgotten that the ultimate quality of the analyses depends critically on the underlying data (data integrity). Furthermore, the way in which this data is extracted from the various client systems, applications and external data sources and correctly linked together is crucial.

³⁶ Data Analytics Working Group.

³⁷ Request for Input: Data Analytics Working Group – Exploring the Growing Use of Technology in the Audit, with a Focus on Data Analytics (IAASB). Deadline is 15 February 2017.

³⁸ Related to projects and initiatives on professional scepticism, ISA 315 (revised), quality control, group audits, ISA 540, education, ethics and other standards (ISA 240, ISA 320, ISA 330, ISA 500, ISA 520 and ISA 530).

Regulatory Audit

Introduction

Regulatory audit firms and regulatory auditors-in-charge play a decisive role in the Swiss dualistic financial market supervision system. As the extended arm of FINMA they perform the regulatory audits of those supervised by FINMA. Their audit responsibilities are therefore different from those of the statutory auditor.

The bundling submission amendments to the AOA and AOO have been in force since 1 January 2015. The oversight authority of the FAOA has since included all financial and regulatory audit services provided to PIEs.

The volume of the regulatory audit services market is estimated at over CHF 100 million. Over the last few years there has been little change in the market structure of regulatory audit services providers. The big three audit firms, PwC, EY und KPMG, still perform the vast majority of regulatory audits, whereby the FAOA sees intense competition amongst all regulatory audit services providers for regulatory audits that are out for tender.

A total of 19 regulatory audit firms held a licence to audit under financial market legislation at the end of 2016.

Figure 8

Regulatory audit firms according to licence type

Licence type	Number at 31 December 2016	Number at 31 December 2015
Audits under the Banking Act (BankA), the Stock Exchanges and Securities Trading Act (SESTA) and Mortgage Bonds Act (MBA)/ audits under the Collective Investment Schemes Act (CISA)/audits under the Insurance Supervision Act (InsSA)/audits of DSFI	6	6
Audits under BankA, SESTA and MBA/audits under CISA/audits of DSFI	1	1
Audits under BankA, SESTA and MBA	1	
Audits under CISA/audits of DSFI	1	1
Audits under CISA	1	1
Audits under InsSA	1	1
Audits of DSFI	8	8
Total regulatory audit firms	19	18

The number of FINMA-supervised institutions fell during the year, except in the CISA area. The following table shows the number of institutes audited by licensed regulatory auditors at the end of 2016.

Figure 9
Number of supervised institutions by regulatory area

Regulatory area	Number supervised	2016	2015
Banks	Banks and securities traders (without Raiffeisen banks ³⁹)	312	346
	Insurance companies	207	214
Insurers	Insurance groups	6	6
	Fund managers	44	43
CISA	Agents	71	94
	Asset managers	206	178
	Swiss collective investment schemes	1,551	1,542
DSFI	Directly supervised financial intermediaries	198	227

2016 inspections

In 2016, nine⁴⁰ (prior year: eight) regulatory audit firms were inspected, thereof

- five with an annual inspection cycle as they audit more than 50 PIEs,
- two of six audit firms subject to inspection at least every three years, and
- two of eight pure DSFI regulatory audit firms subject to inspection every five years.

- Six banks, comprising two systemically relevant banks, a cantonal bank, two foreign-controlled banks and another bank,
- An insurer,
- An asset manager,
- A fund manager, as well as the collective investment scheme managed by it, and
- Three DSFI.

Audit quality at the eight firms inspected in 2016 was assessed by means of eleven file reviews. The following categories of financial market companies were selected:

³⁹ Additional 271 cooperatively-organised Raiffeisen banks

⁴⁰ The inspection fieldwork was completed at a further two of the largest five audit firms and an audit firm subject to a three-year inspection cycle. Since the findings process is still at an early stage these are excluded from this Annual Report. Conversely, the two inspections that were still to be completed in the prior year are included.

Figure 10

Overview of completed FAOA regulatory audit inspections and Comment Form findings 2016.

Categories	Five largest regulatory audit firms		Other		Total	
	2016	2015	2016	2015	2016	2015
Number of inspections	5	3	4	3	9	6
Comment Form Findings Firm Review Regulatory Audit	3	3	5	6	8	9
Comment Form Findings File Review Regulatory Audit	32	21	13	18	45	39
Number of inspected files	7	9	4	5	11	14

Firm Review

In 2016 nine inspections were performed, of which five were completed. The 2016 firm reviews and the prior year inspections excluded from the Activity Report 2015 resulted in a total of eight comment form findings, including two findings on quality assurance systems whose design was insufficient for the regulatory audit. The remaining comment form findings include various other deficiencies in firm-wide quality assurance controls, controls over the monitoring of regulatory audit and training hours of the regulatory auditor-in-charge being an example.

There are generally more comment form findings per firm review at the smaller regulatory audit firms. Although the quality assurance systems of the smaller regulatory audit firms are generally less complex due to client structures, they are confronted by challenges in the following principal areas:

- Transparency in the performance and formalisation of key controls;
- Continual update of the quality assurance system and controls for changes in regulatory requirements.

File Review

In 2016 eight file reviews were performed, four of which were completed. As in financial audit, the quality of the regulatory audit depends heavily on the engagement team members. Their technical knowledge of regulatory requirements is particularly important.

To ensure audit quality regulatory audit firms must first focus on the consistency of audit quality across audit engagements of different size, complexity, risk and financial market licence type. Secondly, continual regulatory education and training must be provided to the partners involved and monitored adequately.

The following figures analyse, by audit area and cause, findings from a total of eleven file reviews, being those completed in 2016 and those of the prior year excluded from the Activity Report 2015:

Figure 11

Number of regulatory audit file review comment form findings by audit area (45 findings in total)

Risk management	12
AMLA regulations	10
Internal control system, incl. IT	7
Audit planning, incl. risk analysis and audit strategy	4
Tied assets	2
Capital requirements and deposit protection	2
Conceptual separation financial and regulatory audit	2
Regulatory reporting	2
Use of the work of internal audit	1
Liquidity requirements	1
Other	2

The most common comment form findings related to audit procedures in the risk management area (particularly the credit area). Findings on audit procedures relating to compliance with ALMA regulations were also common. The latter also produced many findings in the prior year. The FAOA pays particular attention to the proper audit of the ICS. Seven findings arose in this area.

FINMA must be able to rely on the quality of regulatory audit reporting and planning in carrying out its oversight activities. The FAOA therefore focuses on the comprehensive, clear and objective presentation of facts and audit results. Attention is also paid to proper audit planning. Six of the total of 45 findings include deficiencies in regulatory audit reporting or planning. Of these, four relate to regulatory au-

dit engagements of different size and financial market licence type, audited by four different regulatory audit firms. In one serious case an audit report was provided to FINMA without evidence that the audit procedures stipulated by FINMA had been performed.

The main cause of comment form findings was the failure to obtain sufficient appropriate audit evidence, often

Figure 12

Causes of 2016 regulatory audit file review comment form findings

Insufficient audit evidence	19
Insufficient audit evidence combined with insufficient professional scepticism	12
Deficient regulatory reporting in conjunction with insufficient audit evidence	4
Other	4
Serious violation of auditor's duty of care	2
Conceptual separation financial and regulatory audit	2
Inadequate audit planning	2

associated with insufficient professional scepticism in planning and performing the audit. This resulted in inadequate regulatory reporting to FINMA. Insufficiency of audit evi-

dence concerned sample testing, for example, where sampling risk was not reduced to an acceptably low level by the size and testing of the sample.

2016 points of focus

The FAOA published its points of focus for the 2016 regulatory audit inspections in the 2015 Activity Report

and examined these in detail in the year under review. This examination resulted in the following points:

Audit of compliance with risk management and risk control requirements (Art. 12 BankO, Art. 7 LiqO, Art. 12a CISO)

In many cases, insufficient appropriate evidence was obtained in the credit and interest rate risk area, which is fundamental to banks. Credit exposures and the recoverability of collateral were not scrutinised with sufficient professional scepticism. Furthermore, the scope of sample testing (determination of total population, selection criteria, testing of sample etc.) was incomprehensible.

Using the work of the internal auditor and involvement of external experts (e.g. actuaries)

Deficiencies were found in the use and assessment, as regards ICS effectiveness, of third party audit reports on outsourced systems and functions. For example, ISAE 3402 ITGC reports did not cover the whole audit period and no independent work was performed. In several cases the work and findings of the internal auditor or actuary were insufficiently assessed when relied upon.

Audit of compliance with AMLA requirements

In several cases deficiencies were found in sample design, which should reduce sampling risk to an acceptably low level (margin note 42 of FINMA Circular 2013/3). In certain cases no comprehensive or sufficiently detailed documentation was prepared, such that an informed third party could neither understand nor re-perform the audit procedures (margin note 39 of FINMA Circular 2013/3).

Root cause analysis and measures

The process for conducting root cause analysis and determining measures in the regulatory audit area is basically the same as for financial audit.

The 2016 findings showed the importance of measures to improve knowledge of oversight law. These covered:

- Qualitative and quantitative training concept improvements at the regulatory audit firms;
- Involvement of external specialists;
- Fundamental redesign of audit tools, programmes and checklists;
- Fundamental revision of review levels;
- Fundamental redesign of internal quality assurance system, as well as the implementation and improvement of regulatory audit monitoring.

AMLA developments/audit impact

The past year was marked by numerous prominent money laundering cases concerning the Brazilian Petrobras and the Malaysian State Fund 1MDB, as well as by intense discussion over the role of offshore structures in the financial system. FINMA believes⁴¹ that the risk of money-laundering in Switzerland has increased.

Switzerland is recognised worldwide as a leading location for private client cross-border asset management business. This places correspondingly high demands on Swiss anti-money laundering capabilities. As the extended arm of FINMA, regulatory auditors and regulatory audit firms are particularly called upon:

First, audit procedures relating to money laundering risks require great professional scepticism. Secondly, financial intermediaries and regulatory auditors were confronted by various developments in the regulation

of money laundering risks last year. The revised FATF recommendations⁴² were embedded into Swiss law as per 1 January 2016. These encompassed a revision of the anti-money laundering law, the relevant ordinances, FINMA circulars and the self-regulation standards of the profession. For their part, the financial intermediaries were required to tailor and update their internal regulations and processes.

FINMA defines the content and methodology of the regulatory audit and has determined specific minimum testing requirements for the audit of money laundering risks. Given the increased risk of money laundering, and the amendment of the applicable regulatory bases and specific minimum testing requirements in this area, the FAOA will continue to pay particular attention to audit quality as regards money laundering risks (see also «Regulatory audit points of focus for 2017»).

Monitoring of training hours

The licensing conditions that came into force on 1 January 2015 include requirements with respect to minimum annual training hours. The regulatory audit firms could choose to confirm the compliance of their regulatory auditors-in-charge themselves. Alternatively, each regulatory auditor-in-charge could confirm compliance personally using the appropriate evidence. In the first case, a sample of the hours confirmed is reviewed by the FAOA during its inspections. The personal confirmations of regulatory auditors-in-charge are reviewed by the FAOA on an ongoing basis.

The training hours required for licensing could be verified with few exceptions. In isolated cases training hours were incorrectly reported. The most common fault was to report hours mistakenly under the training regulations of EXPERTsuisse. Under these

⁴¹ FINMA annual media conference of 7 April 2016: Speech by Mark Branson «Geldwäschereibekämpfung ist keine Kür, sondern Pflicht»

⁴² <https://www.admin.ch/opc/de/federal-gazette/2014/9689.pdf>

regulations, 45 minutes can already be accounted for as an hour. This contravenes the AOO however (AOO Art. 11h, para. 1 section b).

The final licensing condition, regarding minimum regulatory audit hours, came into force on 1 January 2017. From this date, all regulatory auditors-in-charge must fulfil a minimum number of regulatory audit hours, dependent on licence type, over a sliding four-year period.

If a regulatory auditor-in-charge determines on the reporting date that they do not meet the minimum number of training or auditing hours, they

may no longer work as regulatory auditor-in-charge on an engagement in the category for which the required number of training or auditing hours have not been met. The regulatory audit firm must also ensure, as part of quality assurance, that the individual is no longer deployed on such an engagement as regulatory auditor-in-charge.

The monitoring of training hours is of central importance to both audit firms and individuals with the applicable special FAOA licence to audit under financial market legislation. The FAOA has noted in its inspections that the exact number of required

training hours has been met. Such cases carry the risk that sample tests by the FAOA may lead to some hours being disallowed, thus endangering the licence.

Examples have resulted from the following circumstances:

- Proscribed double-counting of hours;
- Proscribed crediting of foreign regulatory training;
- Non-compliance with the conditions of Art. 11h AOO.

The following table shows the minimum licensing and licence renewal conditions per category.

Figure 13
Licensing requirements for regulatory auditors-in-charge

Licences	One time			Recurring	
	Professional experience (audit services in CH or abroad, if equivalent)	Regulatory audit hours (in relevant licence area)	Training (in year before licence application and in relevant licence area)	Regulatory audit hours (in last 4 years and in relevant licence area)	Training (per year and in relevant licence area)
Banks, stock exchanges, securities traders, central mortgage bond institutions	8 years	1,500 hours	24 hours	400 hours	24 hours
Insurers	8 years	400 hours	16 hours	100 hours	16 hours
Fund managers, investment funds etc. (CISA)	8 years	800 hours	16 hours	100 hours	16 hours
Financial intermediaries (DSFI)	5 years	200 hours	4 hours	100 hours	4 hours

Various regulatory auditors-in-charge gave up their licences during the year. This especially related to the CISA and DSFI categories. The FAOA is examining a specific licence withdrawal case where the regulatory auditor-in-charge has no training hours valid under Swiss oversight law, having only financial audit and foreign oversight law training.

Cooperation with FINMA

A regular interchange between the FAOA and FINMA took place at all seniority levels in the year under review. In this regard, for example, there is an informal exchange with FINMA prior to every FAOA inspection. Content-wise, information is exchanged that the FAOA needs for selecting files and performing file reviews. The FAOA informs FINMA of the results of the firm and file reviews by providing a copy of the final inspection report, including comment forms and other reportable findings on the regulatory audit.

FAOA regulatory audit seminar 2016

The FAOA held a half day seminar on 26 August 2016 covering the regulatory audit under financial market legislation. The seminar provoked great interest and every seat was taken. Alongside a training session (FAOA experiences, money laundering regulations) the future development of the regulatory audit was discussed with representatives from FINMA and EXPERTsuisse.

International

Introduction

In line with its strategic goals for the period 2016–2019 and under the principle of so-called «home state supervision», the FAOA first and foremost seeks mutual recognition with as many foreign oversight authorities as possible (goal 8). In addition, having regard to the Swiss companies quoted in the US and the significant number of US companies in Switzerland, the FAOA works closely with the US audit oversight authority. Although the EU and EEA countries also follow the principle of home state supervision, there is still an active exchange of information relevant to audit oversight with these countries. International administrative assistance will therefore also remain important to the FAOA in the future⁴³.

Extra-territorial scope of the AOA Implementation of the extra-territorial jurisdiction of the FAOA

To protect investors in the Swiss capital market and in line with comparable foreign regulations, the AOA has an extra-territorial impact. Under the law, foreign audit firms are subject to FAOA oversight if they audit foreign companies with shares quoted on a Swiss stock exchange (Art. 8 para. 1 letter a AOA). Based on this extra-territorial jurisdiction, two foreign audit firms, in Argentina and Israel respectively, were inspected in 2016.

There is no FAOA oversight if the foreign audit firm is already subject to oversight by an equivalent foreign authority recognised by the Federal Council (Art. 8 para. 2 AOA). This mutual recognition of equivalent oversight systems was implemented to avoid administrative duplication. The Federal Council has so far recognised 32 foreign audit oversight authorities as equivalent (see Appendix 2, AOO).

Foreign-domiciled audit firms supervised by an equivalent foreign audit oversight authority must nevertheless notify the FAOA. This duty to notify serves to avoid abuse of the

exemption from Swiss licensing and oversight. The current list of all audit firms with a licence exemption is published on the FAOA homepage and includes 22 audit firms from 11 countries. With a view to Federal Council recognition of further foreign oversight bodies, a second group of around thirty countries was examined in 2016, the aim being to publish an extended list in 2017. It is not necessary for the foreign oversight system to be the same as that of the FAOA. It is more critical that the significant functional elements necessary to ensure the provision of audit services of sufficient quality are in place.

Moderate de-regulation as regards extra-territorial jurisdiction

Prior year experience has shown the appropriateness of moderate de-regulation as regards the extra-territorial jurisdiction of the FAOA. This applies particularly to the auditors of foreign bond issuers and material subsidiaries of foreign issuers. The attractiveness of the Swiss capital market is to be safeguarded without adversely affecting investor protection. With this in mind, the Federal Assembly approved the draft amendment of Article 8 AOA, unanimously and without abstentions, on 30 September 2016. The amended Article should come into force in mid-2017.

The extra-territorial jurisdiction of the FAOA is reduced as follows:

- The law waives oversight of foreign audit firms auditing the issuers of unquoted bonds (Art. 8 para. 1, letter d AOA 2016). This is a move towards the European legal framework. Practice shows it to be very time-consuming to identify unquoted bond issuers or their auditors, especially if the latter are abroad. The expense is unreasonable in proportion to the expected investor protection benefits.
- The list of exemptions for the auditors of Swiss-quoted bond issuers is extended (Art. 8 para. 3 AOA

2016). If the audit firm is not subject to the oversight of a recognised foreign oversight authority there are two possibilities: Either the audit firm can apply to the FAOA for a state-regulated audit firm licence or investors must be informed explicitly of the absence of auditor state oversight (Art. 8 para. 3 letter b and para. 5 AOA 2016). This additional exemption is a compromise solution between Swiss bond market competitiveness, the interests of investor protection and the exercise of effective and efficient audit oversight by the FAOA.

- Finally, oversight of the auditors of foreign material subsidiaries is waived, both for share and bond issuers (Art. 8 para. 1 lett. c and d AOA 2016). This is also a move towards the European legal framework. The above-mentioned problem of issuer identification is also confronted here.

The following measures will serve to implement the amended law for its expected enactment in mid-2017:

- First, the AOO will be amended to reflect the new legal requirements.
- Secondly and as mentioned, alongside the 32 foreign audit oversight authorities already recognised by the Federal Council (see Appendix 2, AOO), more equivalent foreign oversight authorities will be recognised.
- Thirdly, the FAOA will issue its own directive on how bond issuers without, or without equivalent, oversight in their country of domicile are to inform the market that their auditor is not (equivalently) supervised.

⁴³ In 2016 the FAOA received 29 (2015: 19) requests for information or administrative assistance, of which 15 were from EU and EEA oversight authorities and 14 from the USA.

Relations with the European Union

EU audit reform

The new EU audit reform regulations came into force on 17 June 2016. The European Directive⁴⁴ on the statutory audit of annual accounts in general and Regulation No. 537/2014⁴⁵ on the statutory audit of the annual accounts of PIE must be implemented within the respective national law. The reform should primarily improve the transparency of company financial statements, strengthen statutory auditor independence, promote market diversity and unify audit oversight within the EU.

The reform does not affect the FAOA's ability to conclude cooperation agreements with EU member states but does impact international administrative assistance. Many oversight authorities have reorganised or restructured in implementing the reform. The FAOA may have to revise its agreements with them as a consequence.

Joint inspections

Based on its 2014 memorandum of understanding (MoU) with the Financial Reporting Council (FRC) and for the first time, the FAOA performed a joint inspection with its UK partner authority at an audit firm subject to UK oversight. Although cooperation is governed the principle of home state supervision, the MoU provides for the possibility of extra-territorial inspections in exceptional cases.

Memorandum of Understanding on cooperation

The FAOA and the Irish oversight authority, the Irish Auditing & Accounting Supervisory Authority (IAASA), signed an MoU on cooperation in the oversight of audit firms on 15 February 2016. This further strengthens investor protection as regards public companies. The MoU creates, at the same time, greater legal security

for Swiss audit firms registered with IAASA for the purpose of auditing Irish-quoted Swiss companies. The agreement governs the exchange of information and confirms mutual recognition of respective oversight activities. Cross-border inspections are not foreseen. The contents of the MoU are comparable with those made with many other European oversight authorities. The MoU was published on the FAOA website.

Cooperation with the USA

Joint Inspections

The last phase of the second cross-border joint inspection cycle (2014–2016) of the FAOA and the Public Company Accounting Oversight Board (PCAOB) ended with the inspection of one of the five largest Swiss audit firms. Cooperation is based on the Statement of Protocol (SoP; equivalent to an MoU), that the FAOA and PCAOB completed in 2011 and extended in 2014.

Cooperation between the FAOA and the PCAOB continues to develop positively and prove effective. The third inspection cycle begins in 2017. Cooperation will be further developed to achieve an even closer relationship.

PCAOB Regulatory Institute

The PCAOB International Institute on Audit Regulation celebrated its tenth anniversary in December 2016. Current investor protection issues and the condition and stability of the international financial markets were discussed at a conference. The Institute brings together representatives from oversight authorities and international organisations to promote international cooperation and the exchange of ideas and strategies to improve audit oversight.

Relations with other states and organisations

The FAOA took part in the conference of German-speaking oversight

authorities in May 2016. Due to their geographical closeness and legal similarities, representatives from Germany, Austria, Liechtenstein and Switzerland meet at this regular event to discuss the audit oversight issues that face the authorities in their countries.

The FAOA also took part in the International Organization of Securities Commissions' (IOSCO) «Survey on audit committee oversight of auditors». Amongst other things, the FAOA described the Swiss legal and regulatory requirements that apply to auditor oversight by the audit committee. The survey results were published in a report in May 2016.

Multilateral organisations

International Forum of Independent Audit Regulators (IFIAR)

Tenth anniversary of IFIAR

IFIAR celebrated its tenth anniversary on 15 September 2016. Founded by independent audit oversight authorities in 2006, IFIAR now has 52 members, the FAOA having joined in 2007. The last decade was marked by various milestones. Of particular note are:

- The ratification of the IFIAR Charter in 2008;
- The development of 11 basic principles for independent audit oversight authorities in 2011 and
- The publication of the first IFIAR Annual Report in 2012.

IFIAR members approved the Multilateral Memorandum of Understanding Concerning the Co-operation in the Exchange of Information for Audit Oversight (MMoU) in 2015 (see below).

⁴⁴ Directive 2014/56/EU of the European Parliament and of the Council amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts (OJ L158 of 27 May 2014, p. 196 f.).

⁴⁵ Regulation No. 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities (OJ L158 of 27 May 2014, p. 77 f.).

IFIAR is an important platform for disseminating knowledge and exchanging practical experiences with respect to the market environment, and for promoting cooperation and exchanges between audit oversight authorities of various jurisdictions. The CEO of the FAOA remained IFIAR Treasurer in 2016.

The plenary meeting was held in London in April 2016. IFIAR members most particularly approved the establishment of a permanent secretariat in Tokyo, Japan, that is expected to commence operations in April 2017. During 2016 IFIAR also started an advisory group, comprising of senior investor and audit committee representatives. Besides this, IFIAR issued a reference guide for non-member states on the establishment of independent audit oversight systems.

The FAOA remained active in many IFIAR working groups:

- International Cooperation Working Group (ICWG): This working group concerns itself with cooperation and the exchange of information between IFIAR members. The FAOA took part in the examination of MMoU entry candidates (see below).
- Inspection Workshop Working Group (IWWG): The aim of this working group and the annual workshop it organises is to provide inspectors with a forum to exchange ideas and discuss current audit-related questions. The FAOA took part in the 2016 workshop in Abu Dhabi in the United Arab Emirates and made a number of presentations.
- Enforcement Working Group (EWG): This working group dedicates itself to issues relating to the enforcement of applicable standards in individual countries through the use of legal sanctions. The FAOA currently chairs an EWG sub-group that is preparing a survey on existing sanction instruments.

Multilateral Memorandum of Understanding (MMoU)

The aim of the MMoU is to promote, in accordance with respective national laws, the exchange of confidential information among its signatories in the areas of licensing, oversight, inspections and disciplinary investigations. Since the MMoU was approved, the FAOA has taken part from within the ICWG in the assessment of entry applications. The administrative assistance structures of each candidate are examined closely in doing so. The MMoU is to be signed at the Tokyo IFIAR plenary meeting in April 2017.

Committee of European Audit Oversight Bodies (CEAOB)

The CEAOB was formed recently in response to the enactment of the EU audit reform (see «Relations with the European Union» above). It replaces the European Group of Auditors' Oversight Bodies (EGAOB) and creates a new framework for cooperation amongst EU national audit oversight bodies. The CEAOB is made up of senior representatives from the responsible member state authorities and the European Securities and Marketing Authority (ESMA). It is currently chaired by the German Auditor Oversight Body (AOB). The CEAOB can issue guidelines or non-binding opinions to implement the regulation and fulfil its duties. It also promotes the exchange of information and the dissemination of expert knowledge, advises the EU Commission and supports assessments and technical inspections.

The Rules of Procedure of the CEAOB allow an audit oversight authority from outside the EU and EEA to be invited as an observer, subject to the agreement of the members. The observer status carries no voting rights. The FAOA was neither a member nor an observer at the EGAOB. The FAOA will also not seek observer status at the new body as Switzerland is not an EU member state and the importance of CEAOB within the EU will be primar-

ily political. However, the CEAOB has formed various sub-groups that look at specific questions. The «inspections sub-group» is especially interesting to the FAOA. This working group is responsible for the exchange of information, the dissemination of expert knowledge and the propagation of best practices in the inspection area. It is the successor of the European Audit Inspection Group (EAIG), in which the FAOA had observer status. Participation in the EAIG was of great value to the FAOA as the representatives of the EU member state oversight authorities are not only active in the same markets and operate under similar judicial systems but also supervise the same audit firms. The CEAOB granted observer status to the FAOA with its resolution of 25 November 2016.

Colleges of supervisors

The European-level integration of various audit network country firms had already led to the formation of «colleges of supervisors» from the regulatory side several years ago. This concept was adopted within the EU audit reform (see section „Relations with the European Union« above). The modalities for cooperation between the responsible authorities of EU member states also provide for the creation of colleges of supervisors and the mutual delegation of tasks. The colleges deal with questions regarding quality assurance, investigations and inspections of audit firms that provide audit services to PIE.

As the FAOA cannot exchange confidential information about domestic inspections to the same extent as EU member states, it has given up its association with these colleges. Whether the FAOA can collaborate with them in the future depends, amongst other things, on the operational rules they establish.

Licensing

Introduction

The volume of licence application processing is heavily dependent upon the renewal cycle of sole practitioners and audit firms. An audit firm licence is limited to a term of five years. Shortly before expiry of this five-year term, each audit firm must submit a licence renewal application to the FAOA. The total number of first-time licence applications has been relatively stable in recent years. By contrast, licence renewal applications are subject to large fluctuations within the five-year cycle. While the existing licences of a total of 1,982 sole practitioners and audit firms expired around two years ago, only 209 sole practitioners and audit firms were due in 2016. For 2017 another relatively low number of audit firm renewals is expected, with around 100 applications.

Duty to provide information and notify

Being licensed and having an existing entry in the FAOA public register is linked to a duty on registered individuals and audit firms to provide information and to notify. All FAOA licensed individuals and audit firms must notify the FAOA immediately of every matter that is important to the assessment of licensing conditions (Art. 15a AOA). The duty to notify applies until the cancellation of the existing licence. Notification is also required for non-legally binding first or higher instance court judgements, as well as settlements in criminal and administrative criminal proceedings, the issuance of loss certificates, professional law proceedings heard before a professional body, audit-related settlements and civil and administrative proceedings. The duty to notify is met where the relevant on-line entry is amended within ten days and any necessary documentation is submitted to the FAOA. The FAOA checks whether the on-line entries are current based on its own findings and third party notifications. Most particularly, the FAOA finds repeated breaches of the duty to provide information and notify with respect

to address and job changes. Breaches of the duty to notify as a result of business cessations and retirement are also relatively common.

Statistics Licences

Since the FAOA commenced its activities the number of licensed individuals has increased every year. This trend also continued in the year under review. 9,192 individuals now have an FAOA licence. The constant increase in the number of licensed audit firms (including sole proprietorships) was first broken as the first licence renewals began in 2013. Since then the number of licensed audit firms has - largely due to the voluntary waivers in the course of licence renewal - fallen year-on-year. While there were still 3,635 licensed audit firms at the end of 2012, 2,947 audit firms held an FAOA licence at the end of 2016.

The number of licensed state-regulated audit firms is stable compared to the prior year at 32 (prior year: 33).

In the year under review the overall total of licensed individuals and firms exceeds 12,000 for the first time.

Figure 14
Licensed individuals and audit firms as at 31 December 2016⁴⁶

Type of licence	Auditor	Audit expert	Total per 31.12.2016	Total per 31.12.2015
Individuals	2,539	6,653	9,192	8,927
Sole proprietorships	250	272	522	560
Audit firms	798	1,595	2,393	2,420
State-regulated audit firms ⁴⁷	–	32	32	33
Total licences	3,587	8,552	12,139	11,940

Membership of professional associations

Membership of a professional association is not a licensing condition for either individuals or legal entities. The proportion of licensed audit firms having a membership in one of the professional associations has continually increased slightly over the last

few years. In the year under review the number of professional association memberships stagnated for the first time. Around 70 percent of all FAOA-registered audit firms currently have a membership in one of the professional associations. Based on the observations and findings of the FAOA – particularly also in the internal quality assurance system area

– it can be assumed that the additional requirements, regulations and support of the professional associations contribute to improved audit quality. The FAOA therefore considers the large number of professional association memberships held by audit firms to be positive.

Figure 15
Professional association memberships⁴⁸ of licensed audit firms as at 31 December 2016



Against prior year, the number of licensed individuals not belonging to one of the professional associations has increased slightly in absolute terms. The total number of licensed individuals also increased in the year under review. Of the now 9'192 licensed individuals, 3'207 currently

do not have a membership in one of the professional associations. The proportion of licensed individuals belonging to one of the professional associations (65 percent) is almost unchanged compared to the prior year (66 percent).

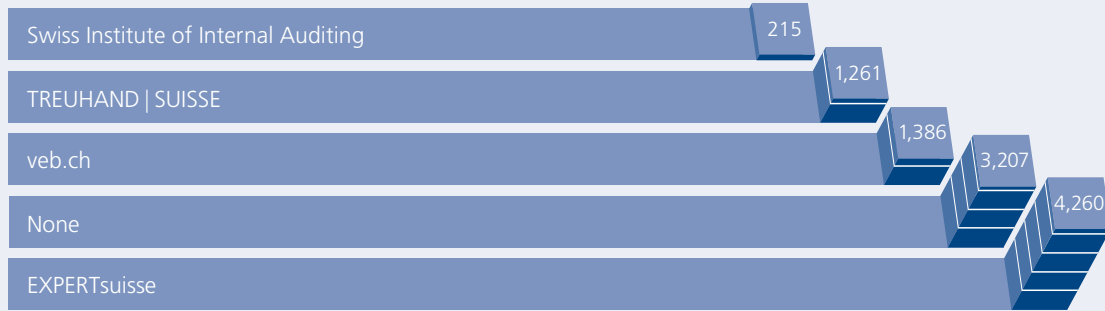
⁴⁶ All numbers refer to legally binding completed proceedings. Pending appeals have not been included. The determining factor is therefore the status of the licensing process at the end of 2016.

⁴⁷ Of which only state-regulated as DSFI-audit firms: 8 (status 31 December 2016). Of which foreign state-regulated audit firms: 2 (status 31 December 2016).

⁴⁸ Incl. multiple answers from individual audit firms with multiple professional association memberships.

Figure 16

Professional association memberships⁴⁹ of licensed individuals as at 31 December 2016



Number of audits

A total of around 1'900 audit firms (incl. sole proprietorships) hold an FAOA audit expert licence. These audit firms may – on condition that their internal quality assurance systems at least meet the requirements of the internal quality assurance system standard SQCS 1 – perform ordinary audits. The following statistics shows that only 27 percent of audit firms with an

audit expert licence also perform ordinary audits. It should thereby be noted that various other audits (e.g. pension schemes) and the audit of certain special transactions also require an audit expert licence. The FAOA statistics only include ordinary audit engagements that require reporting to the general meeting under Art. 728b para. 2 CO. Special law audits and audits under public law regulations (e.g. local authority audits) are not included.

The number of licensed audit firms with one to five ordinary audits has fallen compared to the prior year. By contrast, the number of audit firms with six or more ordinary audits is largely stable compared to the prior year.

Figure 17

Number of ordinary audits (Status: 31 December 2016)

Number of audit firms	2016	2015
1 to 5 ordinary audits:	361	377
6 to 10 ordinary audits:	83	91
11 or more ordinary audits:	78	86
Total number of audit firms performing ordinary audits:	522	554

This fall can be explained by a general fall in the number of ordinary audits within the audit industry. With only 12,444 ordinary audits now compared to 13,849 in the prior year, the fall was surprisingly large. The number of limited audits also shows a slightly negative trend.

⁴⁹ Incl. multiple answers from individuals with multiple professional association memberships.

Figure 18Total number of limited (LA) and ordinary (OA) audits performed⁵⁰ (Status: 31 December 2016)

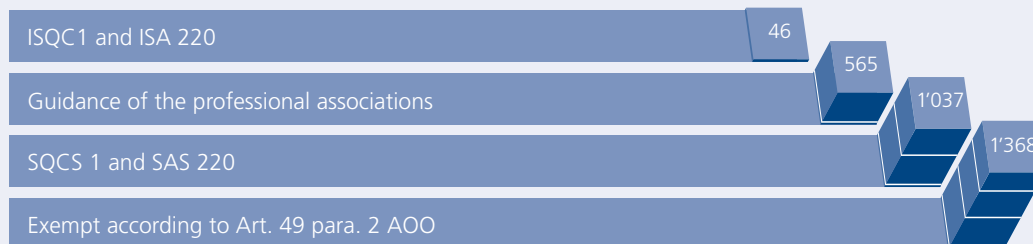
Licence type	Number LA	Number OR	2016	2015
State-regulated audit firms	15,226	9,717	24,943	25,922
Other licensed audit firms	76,170	2,727	78,897	81,694
Total audits performed	91,396	12,444	103,840	107,616

Internal quality assurance

The internal quality assurance standard that audit firms apply is disclosed by way of self-declaration in the FAOA register of auditors and analysed annually by the FAOA.

Figure 19

Audit firm declarations as to applied standard of internal quality assurance at 31 December 2016



Licence renewal

Audit firm licences are legally required to be renewed every five years (Art. 3 para. 2 AOA). Audit firms whose licence renewal is becoming due are contacted by the FAOA around six months before licence expiry and asked to submit the necessary renewal documentation for examination.

In the reporting year, the five-year licences of 209 audit firms expired. A total of 140 of these audit firms submitted a licence renewal application and received a renewed licence after the FAOA had performed the appropriate reviews. 17 percent of audit firms whose licence renewal was due voluntarily waived the renewal. Even though the FAOA does not col-

lect data on the reasons for a waiver, many audit firms have mentioned structural or economic reasons (e.g. owner retirement, firm restructuring, cessation of audit activities) for the waiver. 11 percent of audit firms whose licence renewal was due did not submit any documentation to the FAOA and were deleted from the register of auditors upon expi-

⁵⁰ All data is derived from audit firm on-line self-declarations. It should also be noted that currently 99 percent of audit firms have entered a relevant amount. The FAOA assumes, however, that the majority of the remaining audit firms are largely inactive or do not provide audit services.

ry of the existing licence. A further four percent of audit firms subject to licence renewal gave up the existing licence before expiry. The licences of only four audit firms could not be renewed seamlessly despite the submission of an appropriate application. The isolated non-renewals arose largely from non-compliance with internal quality assurance system requirements, particularly as regards training.

Figure 20
Number of licence renewals granted in 2016

Licence type	Auditor	Audit expert	Total 2016	Total 2015
Sole proprietorships	11	13	24	75
Audit firms	49	64	113	458
State-regulated audit firms	–	3	3	8
Total licence renewals	60	80	140	541

Assessment of internal quality assurance

The FAOA examines compliance with the requirements for a quality assurance system upon initial licensing, as well as every five years upon licence renewal. The basis for this remains the so-called «QS-questionnaire». A risk-based approach is used in determining the depth of this largely formal check. Thus, the internal quality assurance systems of audit firms performing ordinary audits are examined in depth; for example, by reviewing the internal monitoring report.

The QS-questionnaires examined in the reporting year indicate that internal quality assurance systems are appropriate overall. For the points focussed on by the FAOA in assessing the questionnaires, the following aspects are to be highlighted:

- Internal training: In isolated cases audit firms have insufficient controls over training or document them insufficiently. It should be noted that neither self-monitoring by employees nor monitoring by professional associations can replace these internal controls.

- Independence: In some cases, annual independence confirmations are not requested from all employees. It should be noted that important aspects of independence relate to all employees. Thus, no audit firm employee may be a board member of, or exercise another decision-making role at, an audited entity (Art. 728 Abs. 4 OR).
- Internal monitoring: This can either be performed by firm employees or by appointed third parties. Internal monitoring is only effective when it is performed in a serious and critical way, when

identified deficiencies are disclosed and when sustainable remedial measures are defined. Given the numerous practical difficulties involved in an audit, it is unlikely, though not impossible, that an internal monitoring report would contain no deficiencies and remedial measures. The aim must be to improve processes and audit work continually. In individual cases, it was found that QS1 internal monitoring reports did not cover annual firm-specific controls. In some cases it was not specified either that all auditors-in-charge must be covered by internal monitoring at least once every three years. Firms that perform only limited audits and apply IQCS 1 voluntarily are not always aware that they are also required to prepare an annual monitoring report. It was further not always noted that the preparer of the internal monitoring report may not be involved in the audit engagement or engagement-specific quality assurance.

In 2017 there will be a substantial change as regards the internal quality assurance system of those audit firms that have previously been able to exempt themselves from the internal quality assurance obligation. As from 1 September 2017, all audit firms will be required to operate an internal quality assurance system. In safeguarding the internal quality assurance system sole proprietors may use a qualified external individual to perform inspection and control duties. With the implementation of the internal quality assurance system, training requirements apply to all audit firms (incl. sole practitioners) as from 1 September 2017.

In return, it is not expected that sole practitioners will have to join a peer review system, but will instead be free in the organisation of their quality assurance system.



Enforcement and court rulings

Introduction

In the year under review the FAOA made its enforcement activities more transparent (see also goal 7 of the FAOA strategic goals 2016–19): First, since 1 January 2016 it has published all legally-binding court rulings, whether in its favour or otherwise, on its homepage (see new tab «Enforcement»). Only legally-binding rulings are published to avoid premature conclusions being drawn from open proceedings. Secondly, the FAOA published its Enforcement Policy on 30 December 2016. The publication provides the audit profession and other interested parties with greater transparency as to the principles by which it carries out enforcement.

Particular focus is placed below on proceedings relating to pension scheme audits. The FAOA sees the need for regulatory action here (see below and remarks above within «Regulatory developments» – «Current projects» – «Expert mission on required legislative amendments to audit law» and within «Postulate Ettlin»).

Enforcement

In the year under review a total of five licence applications were rejected (prior year: twelve). Eight individuals withdrew their applications or waived their licences during ongoing proceedings (prior year: three). Three applications were not proceeded with due to incomplete documentation (prior year: two). In addition, 11 licence withdrawals were imposed (prior year: 17) and seven reprimands issued (prior year: 34). As expected (see Activity Report 2015), significantly fewer reprimands were issued. Three offences were also reported to the prosecuting authorities (prior year two).

Court rulings

In 2016 the Federal Administrative Court (FAC) and the Federal Supreme Court (FSC) again addressed FAOA orders. A complete list of all rulings made in the year under review is given in Appendix 6. New or significant deliberations from these rulings are noted below.

FAOA competence

Although individuals are licensed for an unlimited period, in return they must continually fulfil licensing conditions. Against this background, the FSC ruled that the FAOA must follow-up on information that might cause compliance with the licensing conditions to be questioned, and also withdraw the licence if necessary. In the court's view, it therefore follows that information conveyed to the FAOA by third parties (Whistleblowing) must also be considered if this suggests possible violations of standards by a licence holder. An explicit legal basis for this is unnecessary⁵¹.

⁵¹ FSC Ruling No. 2C_1026/2015 of 18 July 2016, E. consid. 2.2. see also FAC Ruling No. B-2626/2015 of 19 January 2016, E. 1.5.4.

FAOA discretion

After finding significant deficiencies in the audit of a pension scheme's financial statements (insufficient consideration of legal, regulatory and professional law requirements; lack of an audit plan; insufficient professional scepticism) the FAOA concluded that the auditor-in-charge did not have the necessary basic audit knowledge and withdrew his audit expert licence for five years. The FSC confirmed the length of the withdrawal in the last instance. In doing so, it had ruled that the FAOA may base its decision on an analysis of a single audit engagement. Therefore, the FAOA did not necessarily have to analyse multiple engagements (possibly also from areas other than pensions) to justify a withdrawal⁵². In the same case, the FSC found that the FAOA could expect greater assurance of a proper audit from the auditor-in-charge as there is heightened public interest in the pension scheme audit⁵³.

In the view of the FAC, when considering a licence withdrawal, the FAOA may also take account of audit law violations that pre-date the decision of withdrawal by more than ten years. A necessary pre-requisite is, however, that the licence holder again failed to assure the conduct of a proper audit⁵⁴.

Finally, the FAC found that a temporary licence withdrawal should also have an individual deterrent effect on the licence holder⁵⁵. The latter should thus be deterred from committing further violations questioning his good repute, which should be impeccable at all times.

Audit secrecy

During the course of an investigation into a possible violation of independence requirements and of the duty to notify the court of obvious over-indebtedness, the licence holder referred to audit secrecy in refusing to provide requested information and documents to the FAOA. On appeal, the FAC ruled that the release of documents to the FAOA was not a violation of audit secrecy, the scope of which the appellant had misjudged⁵⁶. The auditor is indeed bound to keep its findings secret and protect the business secrets of the audited company when reporting, making notifications and informing the general meeting (Art. 730b para. 2 CO). However, this applies only to the extent that auditor disclosure is not legally required. The law specifically stipulates that licensed individuals and audit firms must provide the FAOA with all the information and documents it requires to carry out its tasks (Art. 15a para. 2 letter a AOA). The FAOA (staff and officers) is also bound by official secrecy, which protects audit secrecy sufficiently even if disclosures are made to it.

⁵² FSC Ruling No. 2C_860/2015 of 14 March 2016, E. 4.3.

⁵³ FSC Ruling No. 2C_860/2015 of 14 March 2016, E. 5.3 and 5.4.

⁵⁴ FAC Ruling No. B-5434/2014 of 14 July 2016, E. 5.1.2, and No. B-5317/2014 of 14 July 2016, E. 6.1.

⁵⁵ FAC Ruling No. B-7872/2015 of 21 April 2016, E. 4.3.3.

⁵⁶ FAC Ruling No. B-2626/2015 of 19 January 2016, E. 1.5.3. FAC Ruling No. B-2626/2015 of 19 January 2016, E. 1.5.3.

Independence and audit type (ordinary /limited)

The FSC recalled two important points on the subject of independence⁵⁷: First, independence requirements for the limited audit are not fundamentally different to those for the ordinary audit and, secondly, the incompatibilities in Art. 728 para. 2 CO provide guidelines that can also be of importance to the limited audit. The FSC sees this as a matter of established federal court case law.

One-off audit services

The FAC also considered independence as regards one-off audit services. Specifically, this concerned the audit of a company formation report (Art. 635a CO). The court concluded that independence requirements relating to the audit of the entity and consolidated financial statements also apply to the formation audit and even if the newly-formed company waives the statutory audit⁵⁸. The work involved in a formation audit has more in common with the ordinary than the limited audit⁵⁹. In addition to this, independence requirements apply until the newly-formed company is entered into the commercial register, which is why the auditor-in-charge must assure his or her independence until this point in time⁶⁰. The auditor-in-charge's appointment to the board of directors of the audited company and subscription to five percent of its share capital are therefore incompatible with independence. Moreover, a resignation from the board of directors or a subsequent second audit of the formation report by another audit firm do not call the licence withdrawal into question⁶¹.

Procedural law questions

The FAC ruled that a letter in which the FAOA informed a licence holder of the opening of administrative proceedings cannot qualify as an order under the Administrative Procedures Act (APA, SR 172.021). An appeal against such a notice cannot therefore be dealt with⁶².

⁵⁷ FSC Ruling No. 2C_1026/2015 of 18 July 2016, E. 2.1.

⁵⁸ FAC Ruling No. B-7872/2015 of 21 April 2016, E. 3.5.5.

⁵⁹ FAC Ruling No. B-7872/2015 of 21 April 2016, E. 3.5.6.

⁶⁰ FAC Ruling No. B-7872/2015 of 21 April 2016, E. 3.5.8.

⁶¹ FAC Ruling No. B-7872/2015 of 21 April 2016, E. 3.5.8. The FSC overruled the FAC ruling and issued a reprimand instead of a two-year licence withdrawal (FSC Ruling No. 2C_487/2016 of 23 November 2016).

⁶² FAC Ruling No. B-2626/2015 of 19 January 2016, E. 1.5.2.

Pension scheme audits

Broader audit mandate

The pension scheme auditor is more than just a pure financial auditor. Besides the «classic» audit of the financial statements, the pension fund audit also covers questions as to whether the retirement accounts comply with legal requirements; the organisation, management and investments of the scheme meet legal and regulatory provisions; arrangements have been made to ensure loyalty in asset management and compliance of the highest executive body of the pension scheme with the duty of loyalty is monitored adequately; surplus funds or insurance contract policyholder benefits have been appropriated in accordance with legal and regulatory requirements; in the event of a fund shortfall, that the necessary measures have been taken to re-establish full funding; information has been supplied to, and notifications made to, the oversight authorities as legally required; and requirements relating to legal transactions with related parties have been met (Art. 52c para. 1 OPA).

In auditing the organisation and management of the pension scheme the auditor also confirms whether (over and above Art. 728a para. 1 section. 3 CO) an ICS exists that is appropriate to the size and complexity of the scheme. The auditor further tests, sample- and risk-based, whether disclosure of binding interests to the highest executive body of the pension scheme is complete and controlled by the latter. If pension scheme management, administration or asset management is fully or partly outsourced to a third party, the auditor also audits their activities appropriately (Art. 35 OOB2).

In other words, the oversight of pension schemes is not only exercised directly by the oversight authorities, but also indirectly by the auditor. That makes the task of the pension scheme auditor even more of a challenge than the task of auditing financial statements already is.

Licensing requirements

There are currently around 300 audit firms in Switzerland that actively audit pension schemes⁶³. The law requires that the respective audit firms and auditors-in-charge hold an audit expert licence (Art. 52b OPA). There are no specific pension scheme requirements. In particular, there are no requirements as to the total amount of pension scheme audit experience an audit firm, respectively auditor-in-charge, must have. In other words, and not as in the case of, for example, financial institution audits (banks, insurance companies, collective investment schemes etc.), there is no specific special licence and pension scheme auditors are not subject to prudential supervision⁶⁴ either.

Duty of care violations

In the course of administrative proceedings against individuals, the FAOA repeatedly finds serious violations of the appropriate duty of care in the audit of pension schemes:

– A Ticino-registered pension scheme was put into liquidation and the OPA Security Fund had to contribute funds in the double-digit CHF millions to guarantee pensions. The auditor-in-charge had thereby incorrectly confirmed that the financial statements had been prepared in accordance with Swiss GAAP FER 26. No audit plan had been prepared and documented and audit procedures were inadequate and not performed according to legal and professional requirements. The auditor-in-charge also failed to perform additional audit procedures after not receiving notes to the financial statements in spite of several reminders. The auditor-in-charge further failed to perform audit procedures with respect to the investment regulations, management and organisation of the pension scheme. Transactions with related parties and the administrative expenses of the pension scheme were also not audited. The FAOA

withdrew the licence of the auditor-in-charge for five years in 2013 (FSC Ruling No. 2C_860/2015 of 14 March 2016)

– On 18 December 2014, the FSC ordered the auditor of the collective foundation «First Swiss Pension Fund», in joint liability with the members of the foundation board amongst others, to pay compensatory damages of around CHF 9 million, plus interest, for grossly negligent and culpably passive behaviour in connection with its audit. With that, the auditor had to contribute almost a third of the parties' total compensatory damages of CHF 30 million, plus interest. The damages comprised of pension scheme funds that had gone missing during the auditor's term of office and funds contributed by the OPA Security Fund – the pension scheme auditor has a duty to audit the legality of actions taken by the executive bodies, the ICS and the legality of invested assets. In this specific case, the auditor should have been aware of the substantial ex ante risks arising from overlapping responsibilities at the leadership level and from conflicts of interest within the company conglomerate over the collective foundation, which would have led to the conclusion that a «medium risk» existed and that enhanced controls were necessary. Particularly when the collective foundation was unable, even after multiple auditor requests, to provide evidence supporting its main asset (bank account with around CHF 18.5 million; representing 90% of the foundation's assets), immediate tests of detail would have been necessary under these circumstances. The performance of these detailed tests would, despite the absence of an

⁶³ «Dialog statt Weisungen», interview with the Director of OPSC, in: Schweizer Personalsorge, edition 10/2016, page. 5 f.

⁶⁴ An exception applies to investment foundations, that have to be audited by a state-regulated audit firm (Art. 9 Ordinance of 22 June 2011 on investment foundations, ASV; SR 831.403.2).

- audit report, have led to earlier intervention by the responsible oversight body (Federal Social Insurance Office) (source: FSC Ruling 141 V 93 and TREX - Der Treuhanderxperte 2015, 118). The responsible auditor-in-charge voluntarily surrendered her licence.
- During the audit of a collective foundation the auditor-in-charge overlooked, in particular, the following deficiencies in three successive sets of financial statements: First, the collective foundation had purchased a group of companies that took over the management and asset management of the foundation. The price was based, amongst other things, on the expected revenue from the collective foundation mandates themselves. As the purchase helped to reduce administrative costs, the revenue of the purchased group of companies correspondingly fell in part. However, no impairment of the participation in, and an additional loan to, the group of companies was subsequently made in this regard. Secondly, the auditor-in-charge accepted a purchase price valuation appraisal despite the fact that this had been prepared by an affiliate of the auditor, thereby violating independence requirements (prohibition of self-auditing, Art. 728 para. 2 section 4 CO). Thirdly, no audit procedures were performed with respect to the associated transaction with related parties. Fourthly, certain parts of the financial statements were not prepared in accordance with Swiss GAAP FER 26. Fifthly, the compatibility of the purchase with the investment regulations of the collective foundation was not appropriately audited. In 2015 the FAOA withdrew the licence of the auditor-in-charge for four years. In doing so, account was taken of the fact that he had already received an FAOA reprimand in 2010 for an unsatisfactory health insurance scheme audit report.
 - The «Vorsorgestiftung des Gemeindeverbandes der medizinisch-sozialen Dienste des Saanebezirks (ACSMS)», with around 600 insured, engaged an external asset manager. At the beginning of 2015 the foundation was put into liquidation because a British Virgin Island (BVI) fund investment of around CHF 50 million, being around 70 percent of the foundation's funds, could not be repatriated despite being terminated. The assets of the fund were apparently mainly invested in property projects in London, the Czech Republic, Australia and Brazil. The OPA Security Fund contributed CHF 59.1 million to guarantee pensions. In this case a criminal investigation is proceeding. Claims concerning accountability are being examined (source: OPA Security Fund Activity Report 2015). The FAOA is following developments in this matter carefully.
 - An OPSC sample of 100 audit reports showed too high an error quota in the audit reports prepared by pension scheme auditors. Both formal and substantive errors were found. For example, certain confirmations were missing, such as regards loyalty (see above) or an incorrect report template had been used (that for investment foundations or a classic foundation for a pension fund) (source: Schweizer Vorsorge, edition 10/2016, page. 5 f.)
- Against this backdrop, the FAOA questions whether the legal requirements towards pension scheme auditors and auditors-in-charge are sufficiently selective. This question is all the more relevant as, at a time of negative interest rates and investment crisis, it can be assumed that pensions schemes will increasingly (be compelled to) accept higher risks and be confronted with under-funding and remediation measures. In this situation, critical work by the auditor and high quality audit reports contribute greatly to confidence in a sustainable occupational pension.
- There is heightened public interest in the audit of pension schemes (see also FSC Ruling No. 2C_860/2015 of 14 March 2016, E. 5.3), and this public interest should also be taken account of in the licensing and oversight of audit firms active in this area.

Organisation of the FAOA

Legal form	Public-law institution with separate legal identity	
Incorporation within 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	<p>Thomas Rufer (Chairman), Graduate in Business Administration and Swiss Certified Accountant</p> <p>Sabine Kilgus (Vice-Chairman), Prof. Dr., lawyer</p> <p>Wanda Eriksen-Grundbacher, Masters in Accounting Science, Swiss Certified Accountant and US CPA</p> <p>Conrad Meyer, Prof., Dr.</p> <p>Daniel Oyon, Prof., Dr.</p>
	Executive Board	<p>Frank Schneider, Chief Executive Officer, Executive MBA ZFH, Swiss Certified Accountant</p> <p>Reto Sanwald, Deputy to Chief Executive Officer, Head of Legal & International Affairs, Dr. iur., attorney-at-law</p> <p>Martin Hürzeler, Head of Financial Audit, Graduate in Business Administration, Swiss Certified Accountant</p> <p>Heinz Meier, Head of Regulatory Audit, Swiss Certified Accountant</p> <p>Sébastien Derada, Head of Licensing & Support</p>
	Auditor	Swiss Federal Audit Office (SFAO)
Number of staff	At 31 December 2016 30 staff members, representing 26 full-time equivalents, were employed by the FAOA (unchanged from prior year).	
Funding	The FAOA finances itself entirely from the fees and oversight charges levied on licensed individuals and audit firms under oversight. No taxpayers' money is used.	
Legal function	To ensure the proper provision and quality of audit services.	
Responsibilities	Appraisal of licence applications, oversight of the auditors of PIEs and rendering 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.	



Wanda Eriksen-Grundbacher, Swiss Certified Accountant, US CPA, Board of Directors Representative since 1 January 2016.

Index of abbreviations

AHVO	Old-Age and Survivors' Insurance Ordinance (AHV Ordinance) of 31 October 1947 (SR 831.101)
AICPA	American Institute of Certified Public Accountants
AMLA	Anti-Money Laundering Act of 10 October 1997 (SR 955.0)
AMLO	Money Laundering Ordinance of 11 November 2015 (SR 955.01)
AOA	Audit Oversight Act of 15 December 2005 (SR 221.302)
AOO	Audit Oversight Ordinance of 22 August 2007 (SR 221.302.3)
BankO	Banks and Savings Banks Ordinance of 30 April 2014 (SR 952.02)
BBI	Federal Gazette
CAIM	Common Audit Inspection Audit Methodology
CaO	Casino Ordinance of 24 September 2004 (SR 935.521)
CISA	Collective Investment Schemes Act of 23 June 2006 (SR 951.31)
CISO	Collective Investment Schemes Ordinance of 22 November 2006 (SR 951.311)
CO	Swiss Code of Obligations of 30 March 1911 (SR 220)
D-AOA	Draft amendment of 4 November 2015 to the Audit Oversight Act
D-FFSA	Draft Federal Financial Services Act of 4 November 2015
D-FinIA	Draft Financial Institutions Act (FinIA) of 4 November 2015
D-FINMASA	Draft amendment of 4 November 2015 to the Financial Market Supervision Act
DSFI	Directly supervised financial intermediary (supervised by FINMA)
EAIG	European Audit Inspection Group
EEA	European Economic Area
EQCR	Engagement Quality Control Reviewer
EU	European Union
EWG	Enforcement Working Group
FAC	Federal Administrative Court (St. Gallen)
FATF	Financial Action Task Force
FCC	Federal Casino Commission
FDJP	Federal Department of Justice and Police
FEE	Federation of European Accountants (Accountancy Europe since 7 December 2016)
FINMA	Federal Financial Market Supervisory Authority
FINMAG	Financial Market Supervision Act of 22 June 2007 (SR 956.1)
FINMA-PV	Financial Market Auditing Ordinance of 15 October 2008 (SR 956.161)
FMIA	Financial Market Infrastructure Act of 19 June 2015 (SR 958.1)
FMIO	Financial Market Infrastructure Ordinance of 25 November 2015 (SR 958.11)
FOPH	Federal Office of Public Health
FSC	Federal Supreme Court (Lausanne)
G-SIFIs	Global Systemically Important Financial Institutions
G-SIBs	Global Systemically Important Banks
G-SIIs	Global Systemically Important Insurers
IAASB	International Auditing and Assurance Standards Board
ICS	Internal control system

ICWG	International Cooperation Working Group
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
IFIAR	International Forum of Independent Audit Regulators
IFRS	International Financial Reporting Standards
ISA	International Standards on Audit
ISAE	International Standard on Assurance Engagements
ISQC 1	International Standard on Quality Control 1
IWWG	Inspection Workshop Working Group
MoU	Memorandum of Understanding
MMoU	Multilateral Memorandum of Understanding
OA	Oversight Authority
OOB2	Ordinance on the Occupational Old-age, Survivors' and Disability Benefit Plans of 18 April 1984 (SR 831.441.1)
OPA	Occupational Pensions Act of 25 June 1982 (SR 831.40)
OPSC	Occupational Pension Supervisory Commission
OTC	Over-the-Counter, off-market trading by financial market participants
PIE	Public Interest Entity
PCAO	Parliamentary Control of the Administration Office
PCAOB	US Public Company Accounting Oversight Board
SAS	Swiss Auditing Standards of EXPERTsuisse
SCWG	Standards Coordination Working Group
SER	SIX Exchange Regulation
SHIA	Supervision of Health Insurance Act of 26 September 2014 (SR 832.129)
SMI	Swiss Market Index
SoP	Statement of Protocol
SQCS 1	Swiss Quality Control Standard 1
SR	Official Compendium of Swiss Federal Law
SRO	Self-regulatory organisation
SSC	Shared Service Centre
VegüV	Ordinance against exorbitant compensation at public companies of 20 November 2013 (SR 221.331)

Additional Swiss audit licences

Particularly for audit activities in the areas shown below, a special licence of the FAOA or a special-law licence of another authority is required, based on a basic licence under the AOA. In some audit areas, a basic FAOA licence is sufficient (status: 01.01.2017).

Financial/regulatory audit in the area of	Basic licence under the AOA: Audit firm	Basic licence under the AOA: Auditor-in-charge	Responsible for special/special-law licence	Additional requirements
Banks/financial market structures ⁶⁵ /finance groups/securities traders/public tender offers/central mortgage bond institutions	State-regulated audit firm	Audit expert	FAOA	Art. 9a AOA, Art. 11a f. AOO
Collective investment schemes ⁶⁶	State-regulated audit firm	Audit expert	FAOA	Art. 9a AOA, Art. 11a f. AOO
Insurance	State-regulated audit firm	Audit expert	FAOA	Art. 9a AOA, Art. 11a f. AOO
Financial intermediaries (anti-money laundering)	Auditor (State-regulated audit firm) ⁶⁷	Auditor	FAOA/SRO ⁶⁸	Art. 9a AOA, Art. 11a f. AOO and Art. 24 AMLA
Pension schemes	Audit expert ⁶⁹	Audit expert	(OPSC)	–
Health insurance schemes	Audit expert	Audit expert	(FOPH)	–
Casinos	Audit expert	Audit expert	FCC	Art. 75 CaO
AHV Swiss Compensation Office audits	Audit expert	Audit expert	FSIO	Art. 165 AHVO

⁶⁵ Comprising stock exchanges, multilateral trading systems, central counterparties, central depositories, transaction repositories and payment systems.

⁶⁶ Comprising fund managers, investment funds, open-ended investment schemes (SICAV), limited partnerships for collective investment schemes, investment companies with fixed capital (SICAF), asset managers and managers of collective investment schemes, as well as representatives of foreign collective investment schemes.

⁶⁷ In principle, the licensed audit firm need only meet the requirements for an audit firm licensed as an auditor but if it also audits a financial intermediary supervised directly by FINMA (DSFI) under the provisions of AMLA it must have the status of a state-regulated audit firm.

⁶⁸ The FAOA is responsible for the licence to audit DSFI. The licence to audit financial intermediaries that are members of an SRO is the responsibility of the respective SRO (Art. 11a AOO).

⁶⁹ There is one exception: Only audit firms that hold a state-regulated audit firm licence can act as the auditor of investment foundations (Art. 9 of the Ordinance of 22 June 2011 relating to investment foundations, ASV, SR 831.403.2).

State-regulated audit firms

Status: 31 December 2016

No. FAOA	company/name	Location
500003	PricewaterhouseCoopers AG	Zürich
500012	T + R AG	Gümligen
500038	Grant Thornton Bankrevision AG	Zürich
500149	OBT AG	St. Gallen
500241	MAZARS SA	Vernier
500420	Deloitte AG	Zürich
500498	PKF Wirtschaftsprüfung AG	Zürich
500505	Treuhand- und Revisionsgesellschaft Mattig-Suter und Partner	Schwyz
500646	Ernst & Young AG	Basel
500705	BDO AG	Zürich
500762	Balmer-Etienne AG	Luzern
501091	Provida Wirtschaftsprüfung AG	St. Gallen
501382	Berney & Associés SA Société Fiduciaire	Genève
501403	KPMG AG	Zürich
501470	Ferax Treuhand AG	Zürich
501570	Fiduciaire FIDAG SA	Martigny
501839	Grant Thornton AG	Zürich
502658	Treureva AG	Zürich
504689	SWA Swiss Auditors AG	Pfäffikon
504736	PKF CERTIFICA SA	Lugano
504792	Asset Management Audit & Compliance SA	Genève
505046	MOORE STEPHENS EXPERT (ZURICH) AG	Zürich
505062	AML Revisions AG *	Zürich
505065	TEBOR Treuhand AG *	Zug
505070	VQF Audit AG *	Zug
505077	CF Compagnie fiduciaire de révision sa *	Genève
505081	MOORE STEPHENS REFIDAR SA *	Genève
505093	RFC – Révision Fiscalité Conseils SA *	Satigny
505106	Révisions LBA Romandie Sàrl *	Montreux
505113	GFC Audit & Compliance SA *	Carouge
600001	Deloitte & Co. S.A.	Buenos Aires
600002	Kost Forer Gabbay & Kasierer	Tel Aviv

* Licensed only for the audit of DSFI.

Cooperation with foreign authorities

Status: 31 December 2016

Country	Authority	Agreement
Germany	German Auditor Oversight Body (AOB)	MoU (2012)
Finland	Auditing Board of the Central Chamber of Commerce (AB3C)	MoU (2014)
France	French High Council for Statutory Auditors (H3C)	Cooperation Protocol (2013)
Ireland	Irish Accounting and Auditing Supervisory Authority (IAASA)	MoU (2016)
Canada	Canadian Public Accountability Board (CPAB)	MoU (2014)
Liechtenstein	Financial Market Authority (FMA)	MoU (2013)
Luxembourg	Commission de Surveillance du Secteur Financier (CSSF)	MoU (2013)
Netherlands	Netherlands Authority for the Financial Markets (AFM)	MoU (2012)
USA	Public Company Accounting Oversight Board (PCAOB)	SoP (2011) Addendum (2014)
UK	Financial Reporting Council (FRC)	MoU (2014)

Court rulings 2016

Status: 31 December 2016

The following is a complete list of the 2016 rulings of the federal courts relating to the FAOA. The rulings appear in chronological order, with a short note on the subject matter dealt with and on the conclusion of the court.

- FAC Ruling No. B-2626/2015 of 19 January 2016: Notification of the opening of proceedings against a licence holder. Rejection of appeal as far as dealt with. A notification does not qualify as an ruling. Not yet legally binding.
- FAC Ruling No. 2C_860/2015 of 14 March 2016: Insufficient audit procedures in the audit of the financial statements of a pension scheme (lack of attention to legal, regulatory and professional law requirements, lack of an audit plan and insufficient professional scepticism). Licence withdrawal for five years. Confirmation of FAC Ruling No. B-1577/2015 of 17 August 2015. Rejection of appeal.
- FAC Ruling No. B-7872/2015 of 21 April 2016: Breach of independence in the audit of a company formation report. Engagement not complete at the time the auditor-in-charge accepted a place on the board of directors and subscribed for five percent of the share capital. Licence withdrawal for two years. Rejection of appeal.
- FAC Ruling No. B-6791/2015 of 27 April 2016: Breach of independence. Audit of the financial statements of two companies belonging to the same group as the auditor. Quality assurance through a member of management of a further group company. Audit services provided free. Licence withdrawal for three years. Rejection of appeal.
- FAC Ruling No. B-5317/2014 of 14 July 2016: Breach of independence. Licence holder was a member of the board of directors of the auditor and eight audited companies simultaneously over many years. Licence withdrawal for two years. Rejection of appeal.
- FAC Ruling No. B-5434/2014 of 14 July 2016: Breach of independence. Audit of seven companies (signature of 40 audit reports) over many years, during which a member of the board of directors of the auditor was simultaneously on the board of the audited companies. Licence withdrawal for two years. Rejection of appeal.
- FSC Ruling No. 2C_1026/2015 of 18 July 2016: Breach of independence. Close business relationship between the auditor-in-charge and a board member of two audited companies. Confirmation of FAC Ruling No. B-4868/2014 of 8 October 2015. Rejection of appeal.
- FSC Ruling No. 2C_29/2016 of 3 November 2016: Licence to perform audits under CISA and AMLA withdrawn by FINMA due to failure of audit firm to exercise due care and resultant lack of confidence in the audit. Proceedings transferred to FAOA as part of the bundling of oversight authority under the FAOA on 1 January 2015. Confirmation of FAC Ruling No. B-3224/2013 of 23 November 2015. Rejection of appeal.
- FSC Ruling No. 2C_121/2016 of 14 November 2016: Breach of independence. Close business relationship between the auditor-in-charge and a board member of the audited company, who simultaneously sat on the board of directors of the auditor. Licence withdrawal for two years. Confirmation of FAC Ruling No. B-2632/2014 of 15 December 2015. Dismissal of appeal.
- FSC Ruling No. 2C_528/2016 of 15 November 2016: Breach of independence. Audit of the financial statements of two companies belonging to the same group as the auditor. Quality assurance through a member of management of a further group company. Audit services provided free. Licence withdrawal for three years. Confirmation of FAC Ruling No. B-6791/2015 of 27 April 2016. Rejection of appeal.
- FSC Ruling No. 2C_487/2016 of 23 November 2016: Breach of independence in the audit of a company formation report. Engagement not complete at the time the auditor-in-charge accepted a place on the board of directors and subscribed for five percent of the share capital. The FSC overruled FAC Ruling No. B-7872/2015 of 21 April 2016 and issued a reprimand instead of a two-year licence withdrawal.

Financial statements of the FAOA

Balance sheet

(in CHF)

	Note	31.12.2016	31.12.2015
Cash at bank and in hand	4	6,206,543	6,080,801
Receivables	5	243,084	180,002
Work-in-progress	6	476,000	861,000
Prepayments	7	107,995	72,254
Current assets		7,033,622	7,194,057
Investments	8	166,074	221,058
Tangible fixed assets	9	319,526	306,246
Intangible fixed assets	10	149,659	127,424
Non-current assets		635,259	654,728
Total assets		7,668,881	7,848,785
Short term liabilities relating to services		55,969	80,470
Liabilities to state-regulated audit firms	11	323,228	84,677
Social security liabilities		104,115	123,278
Short-term provisions	12	190,000	199,809
Accruals	13	340,809	312,931
Accrued licensing fees	14	840,460	807,260
Current liabilities		1,854,581	1,608,425
Accrued licensing fees	14	814,300	1,440,360
Non-current liabilities		814,300	1,440,360
Reserves	15	5,000,000	4,800,000
Equity		5,000,000	4,800,000
Total liabilities		7,668,881	7,848,785

Income statement

(in CHF)

	Note	01.01.2016 – 31.12.2016	01.01.2015 – 31.12.2015
Oversight charges	16	3,321,620	3,515,324
Inspection fees	17	2,202,131	1,903,902
Licensing fees	18	1,136,324	1,129,428
Other income	19	67,128	120,220
Net revenue		6,727,203	6,668,874
Personnel expense	20	-5,497,979	-5,389,606
Operating expense	21	-859,746	-799,576
Depreciation and amortisation	9, 10	-168,986	-179,565
Operating profit		200,492	300,127
Financial result		-492	-127
Transfer to reserves	15	-200,000	-300,000
Profit/loss		–	–

Cash flow statement

(in CHF)

	Anhang	01.01.2016 – 31.12.2016	01.01.2015 – 31.12.2015
Transfer to reserves	15	200,000	300,000
Depreciation of fixed assets	9, 10	168,986	179,565
Increase/(decrease) in accrued licensing fees (long-term)	14	-626,060	-358,460
(Increase)/decrease in receivables	5	-63,082	64,595
(Increase)/decrease in work-in-progress	6	385,000	-610,000
(Increase)/decrease in prepayments	7	-35,741	-7,418
Increase/(decrease) in liabilities		214,050	-34,279
Increase/(decrease) in social security liabilities		-19,163	786
Increase/(decrease) in short-term provisions	12	-9,809	17,009
Increase/(decrease) in accruals	13	27,877	-12,347
Increase/(decrease) in accrued licensing fees (short-term)	14	33,200	87,000
Net cash flows from operating activities		275,258	-373,549
Acquisition of investments	8	-15	-17,019
Disposal of investments	8	55,000	55,000
Acquisition of tangible fixed assets	9	-120,344	-23,903
Acquisition of intangible fixed assets	10	-84,157	-91,232
Net cash flows from investing activities		-149,516	-77,154
Change in cash and cash in hand		125,742	-450,703
Cash and cash in hand at the start of the year	4	6,080,801	6,531,504
Cash and cash in hand at year-end	4	6,206,543	6,080,801

Change in equity

(in CHF)

	01.01.2016 – 31.12.2016	01.01.2015 – 31.12.2015
Opening balance as of 01.01.	4,800,000	4,500,000
Transfer to reserves	200,000	300,000
Balance as of 31.12.	5,000,000	4,800,000

Notes to the 2016 financial statements

1. Operating activities

The FAOA is a public-law institution of the Federal Government and has its registered office 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 AOA. Further, it oversees audit firms who provide audit services to public interest entities.

The FAOA conducts its oversight independently, organises itself, and finances itself entirely from the fees paid by licensed individuals and firms and the charges paid by state-regulated firms. The FAOA maintains its own accounts.

Since 1 September 2012 the FAOA has exercised oversight over the financial audits of listed banks, insurance companies and collective investment schemes. In addition, since 1 January 2015 the FAOA has had sole oversight authority over audit firms. This applies both to the financial and regulatory audit.

As at 31 December 2016 the FAOA employed 30 employees, representing 26 full-time equivalents (unchanged from prior year).

2. Accounting policies

a. Introduction

These financial statements of the FAOA are prepared in line with the International Public Sector Accounting Standards (IPSAS) and in accordance with Article 957 f. of the Code of Obligations (Art. 35 para. 2 AOA). The accounting policies of the FAOA differ from the IPSAS in the pensions area:

IPSAS 25 requires pension costs to be expensed in the period in which a «current obligation» arises. IPSAS also requires comprehensive disclosure of employee benefit plans in the notes. In these financial statements the employer savings and risk contributions paid to the FAOA employee benefit plans are expensed. The surplus or deficit that might arise from an actuarial valuation is not accounted for. The FAOA commissioned actuarial valuations as per 31 December 2015 and 31 December 2016. The net pension liability calculated by Aon Schweiz AG is not accounted for however, as foreseen in IPSAS 25, but rather disclosed as a contingent liability (see Note 22).

These financial statements are entity financial statements for the financial year comprising calendar year 2016 with a balance sheet date of 31 December 2016 (including comparatives). The reporting currency is Swiss francs (CHF).

Unless otherwise stated, assets and liabilities are valued at historical or production cost, which is normally the nominal value. Expenses and revenues are booked in the period in which they occur.

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

b. Cash at bank and in hand

Cash at bank and in hand comprises 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 invest excess funds with the Federal Government.

The amounts are stated at nominal value.

c. Receivables relating to services

Receivables are stated at nominal value after allowance for possible write-downs.

d. Work-in-progress

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

e. Tangible fixed assets

Tangible fixed assets are accounted for at cost less required write-downs. Depreciation is calculated on a linear basis over the expected useful life.

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 are checked at each balance sheet date and adjusted if appropriate.

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

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

f. Intangible fixed assets

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

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

The residual value, useful life and method of amortisation of an intangible fixed asset are checked at each balance sheet date and adjusted if appropriate.

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

Self-generated goodwill cannot be capitalised.

g. Investments

Investments are accounted for at market value.

h. Taxes

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

i. Provisions

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

j. Leasing

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

k. Equity

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.

l. Revenues (fees and oversight charges)

The FAOA charges fees for its orders, inspections and services and levies an oversight charge upon state-regulated audit firms to cover costs not covered by the fees (Art. 21 AOA). The fees and oversight charges are stipulated in Art. 37 f. AOO.

Fee income for the licensing of audit firms is accrued over a period of 5 years (including licence renewals). 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 in full upon invoicing.

m. Financial result

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

n. Collateral for third party liabilities

The FAOA has provided no collateral for third party liabilities (Art. 959c para. 2 section 8 CO).

o. Collateral for own liabilities

The FAOA has provided no collateral for its own liabilities (Art. 959c para. 2 section 9 CO).

3. Estimation uncertainty

The preparation of financial statements according to generally accepted accounting principles requires the use of estimates and assumptions. These affect the disclosed amounts of assets and liabilities and the disclosure of contingent assets and liabilities as at the balance sheet date, as well as disclosed revenues and expenses. Although these estimates are made to the best of the FAOA's knowledge with respect to current events and possible future FAOA measures, actual results could differ from those estimated.

Explanatory information on individual financial statement items

4. Cash and cash in hand

(in CHF)

	2016	2015
Cash in hand	837	992
Postfinance account	205,706	679,563
Investment account at Federal Finance Administration FFA	6,000,000	5,400,246
Total cash and cash in hand	6,206,543	6,080,801

5. Receivables

	2016	2015
Licence fee receivables	165,766	63,400
Yellowpay receivables	22,318	52,389
Other receivables	55,000	64,213
Total receivables relating to services	243,084	180,002

As in the prior year, no bad debt provision was established as the FAOA has only suffered insignificant bad debt losses to date.

6. Work-in-progress

	2016	2015
Work-in-progress	476,000	861,000
Total work-in-progress	476,000	861,000

Work-in-progress comprises inspection work yet to be invoiced.

7. Prepayments

	2016	2015
Prepayments	107,995	72,254
Total prepayments	107,995	72,254

Prepayments are payments made for expenses of the following year, such as rent, travel costs and Swiss Federal Railways season tickets.

8. Investments

In connection with the rent of offices, the FAOA has two tenant deposit accounts to the total amount of CHF 111,074. In addition, there is a long-term receivable of CHF 55,000 (prior year CHF 110,000) relating to the termination of an IT project in 2014.

9. Tangible fixed assets

(in CHF)

	Furniture and furnishings	Office equipment, IT equipment (hardware)	Fixtures and fittings	2016	2015
Acquisition costs					
Opening balance	408,432	190,434	336,410	935,276	911,373
Acquisitions	31,614	12,792	75,938	120,344	23,903
Disposals	–	-2,016	–	-2,016	–
Closing balance	440,046	201,210	412,348	1,053,604	935,276
Depreciation					
Opening balance	-281,078	-169,859	-178,093	-629,030	-503,260
Acquisitions	-44,005	-21,824	-41,235	-107,064	-125,770
Disposals	–	2,016	–	2,016	–
Closing balance	-325,083	-189,667	-219,328	-734,078	-629,030
Net book value	114,963	11,543	193,020	319,526	306,246

There were no indicators that tangible fixed assets were impaired at the balance sheet date.

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

10. Intangible fixed assets

	Software register and administration	Other software	2016	2015
Acquisition costs				
Opening balance		485,729	168,383	654,112
Acquisitions		78,835	5,322	84,157
Disposals		–	–	-9,961
Closing balance		564,564	173,705	738,269
Amortisation				
Opening balance		-392,568	-134,120	-526,688
Acquisitions		-43,016	-18,906	-61,922
Disposals		–	–	9,961
Closing balance		-435,584	-153,026	-588,610
Net book value		128,980	20,679	149,659

There were no indicators that tangible fixed assets were impaired at the balance sheet date.

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

11. Liabilities to state-regulated audit firms

The FAOA levies an annual oversight charge upon state-regulated audit firms (see Note 2 letter I). 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 323,228 (prior year CHF 84,677) will be credited to the state-regulated audit firms in 2017.

12. Short-term provisions

(in CHF)

	2016	2015
Personnel expense liabilities	188,000	193,809
Provision for compensation	2,000	6,000
Total short-term provisions	190,000	199,809

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 orders that have been appealed against by those affected.

13. Accruals

	2016	2015
Various accruals	340,809	312,931
Total accruals	340,809	312,931

Accruals primarily relate to personnel expense accruals and accruals for the cost of the Annual Report 2016.

14. Accrued licensing fees

	2016	2015
Accrued licensing fees (short-term)	840,460	807,260
Accrued licensing fees (long-term)	814,300	1,440,360
Total accrued licensing fees	1,654,760	2,247,620

Fee income from the licensing of audit firms is accrued over a period of 5 years.

15. Reserves

(in CHF)

	2016	2015
Reserves	5,000,000	4,800,000
Total Reserves	5,000,000	4,800,000

The FAOA accumulates a reserve for the exercise of its oversight activities up to a maximum amount of an annual budget (Art. 35 para. 3 AOA). The reserve was increased by CHF 200,000 in the reporting year

(prior year CHF 300,000) in connection with the assumption of additional responsibilities from FINMA (bundling), respectively the related general increase in the FAOA budget.

16. Oversight charges

The surplus of CHF 323,228 (prior year CHF 84,677) was offset against oversight charges. This amount will be credited to the state-regulated audit firms in 2017 (see Note 11).

17. Inspection fees

The increase in inspection fees is particularly due to one-off additional work in connection with ad-hoc inspections.

18. Licensing fees

	2016	2015
Licensing fees individuals	333,600	367,300
Licensing fees audit firms	268,000	561,000
Commission on internet payments	-26,686	-30,082
Reimbursement of licensing fees	-31,450	-40,250
Accrual of licensing fees	-214,400	-448,800
Release of accrued licensing fees from prior years	807,260	720,260
Total licensing fees	1,136,324	1,129,428

Audit firm licences are limited to a period of five years. The decrease in audit firm licence fees is due to a lower number of licence renewal applications in the reporting year.

19. Other income

Other income includes, in particular, income from an FAOA seminar in Zurich and income from FAOA proceedings (costs of proceedings and reprimands).

20. Personnel expense

(in CHF)

	2016	2015
Staff compensation and Board member fees	4,156,872	4,102,556
Employer contributions	956,750	874,156
Social security expenses	310,709	300,550
Third party personnel costs	73,648	112,344
Total personnel expense	5,497,979	5,389,606

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. They include a contribution of CHF 25,000 (prior year CHF 25,000) to the employer contribution reserve of the FAOA pension fund.

The increase in employer contributions is mainly due to the alignment of the FAOA pension plan regulations to those of the Federal Government as per 1.1.2016 (alignment of occupational pension savings contributions).

Third party personnel costs in the reporting year primarily include external translation service charges (CHF 21,748) and consultancy fees (51,900).

21. Operating expense

	2016	2015
Accommodation	226,725	196,422
Administrative expense	130,042	134,777
IT expense	309,528	301,884
Other operating expense	193,451	166,493
Total operating expense	859,746	799,576

22. Contingencies

At the balance sheet date there were no pending or threatened claims for damages.

In relation to employee pensions, the FAOA commissioned an actuarial report from Aon Schweiz AG as at 31 December 2016. The report discloses an FAOA net pension liability of CHF 6.6 million as at 31 December 2016 (prior year CHF 7.0 million).

23. Operating leases (off-balance sheet)

(in CHF)

	2016	2015
Minimum payments within one year	11,172	11,172
Minimum payments in years 2 to 6	0	11,172

Operating leases comprise off-balance sheet liabilities relating to a contract for Triumph-Adler multi-purpose equipment. The current contract has a total term of around 5 years (1.1.2013–1.1.2018).

The FAOA has not entered into any finance leases which would be on the balance sheet.

24. Related party transactions

a. Definition of term «related parties»

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

- The Federal Administration, within the meaning of Art. 6 Government and Administration Organisation Ordinance (GAOO; SR 172.010.1)
- Swisscom, Post, Swiss Federal Railways
- Members of the Board of Directors
- Members of the Executive Board

b. Particular relationship with the Federal Government

The FAOA is a public-law institution of the Federal Government with separate legal identity (Art. 28 para. 2 AOA) and part of the de-centralised Federal Administration. The Federal Government can influence the FAOA in many ways:

– The AOA is a federal law enacted by the Federal Councillors. The AOO and other regulations are enacted by the Federal Council.

– The Federal Council elects the Board of Directors, appoints the Chairman and Vice-Chairman and determines compensation. It can also dismiss the members of the Board of Directors for significant reasons (Art. 30 paras. 3, 5 and 6 AOA).

– The Federal Council approves the creation and termination of the employment contract with the Chief Executive Officer (Art. 30a letter g AOA).

– The Federal Council approves the affiliation agreement with PUBLICA (Art. 30a letter e AOA).

– The Federal Council approves the strategic goals and checks annually whether they have been met (Art. 30a letter b and Art. 38 para. 2 letter f AOA).

– The Federal Council approves the Annual Report and discharges the Board of Directors of its responsibilities (Art. 30a letter m and Art. 38 para. 2 letter g AOA).

– As auditor of the FAOA, the Swiss Federal Audit Office audits the oversight authority in accordance with the CO (Art. 32 para. 2 AOA) and the Federal Auditing Act.

– The FAOA is required to invest its excess funds with the Federal Government at market interest rates (Art. 36 para. 1 AOA).

If required for liquidity reasons, the Federal Government 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).

Remuneration of the Board of Directors and Management

In CHF thousands

Board of Directors	2016	2015
Fees of Chairman	80	75
Fees of Vice-Chairman	50	38
Fees of other members	75	52
Social security contributions ⁷⁰	12	9
Total compensation of the members of the Board of Directors	217	174
Chief Executive Officer and Executive Board	2016	2015
Salary of Chief Executive Officer	265	260
Other benefits of Chief Executive Officer ⁷¹	46	44
Salaries of other members	744	719
Other benefits of other members	78	73
Social security contributions ⁷²	272	226
Total compensation of the members of the Executive Board	1,405	1,322

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

The remuneration of the Board of Directors was newly determined by the Federal Council as per 1.1.2016.

25. Events after the balance sheet date

No events have occurred since the balance sheet date of 31 December 2016 that impact the informational value of the 2016 financial statements.

⁷⁰ Comprises pension/invalidity/income compensation insurance contribution and unemployment insurance contribution.

⁷¹ Includes additional taxable benefits such as bonuses and non-mandatory child allowances.

⁷² 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.



**Report of the statutory auditor
 on the limited statutory examination**

**to the Board of Directors of the
 Federal Audit Oversight Authority for the attention
 of the Federal Council**

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 change in equity, and notes) of the Federal Audit Oversight Authority (FAOA) for the financial year ended 31 December 2016.

These financial statements are the responsibility of the Board of Directors. 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.

Bern, 2 march 2017

SWISS FEDERAL AUDIT OFFICE

Andreas Meyer
 Auditor in Charge
 Licensed Audit Expert

Peter Küpfer
 Licensed Audit Expert

Enclosure:

Financial statements, consisting of balance sheet, income statement, cash flow statement, statement of change in equity and notes

