



## Benchmarking financial statements

Reflections on the first year of implementation

New financial reporting law (Code of Obligations)

# Contents

Most recent analysis of the new financial reporting law	<b>01</b>
Financial statements structure and terminology	<b>02</b>
Disclosure of subsidiaries	<b>03</b>
Individual and group valuation	<b>04</b>
Reliefs due to consolidated accounts	<b>05</b>
Disclosure information about full time equivalents	<b>06</b>
Conclusion	<b>07</b>
Contacts	<b>07</b>

# Most recent analysis of the new financial reporting law

## Reflections on the first year of implementation

2015 was the first year many companies had to apply the new Swiss financial reporting law, with the vast majority applying it for the first time. Our analysis has identified significant areas where the requirements of the new Swiss financial reporting law have been interpreted in different ways by the reporting companies.

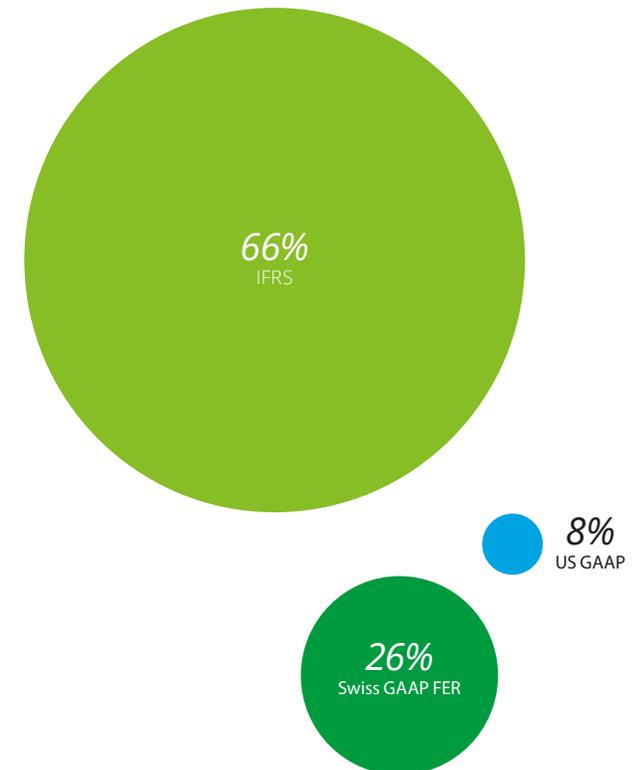
This analysis was prepared in response to the first year of application of the new financial reporting law. It comprises a review of the annual reports of 50 Swiss listed companies, representing a wide range of size, geographies and industries.

It is based on their annual reports comprising the consolidated financial statements and standalone financial statements of the holding companies, which are prepared in accordance with the Swiss Code of Obligations and thus the new financial reporting law. We focused our analysis on the standalone financial statements of the holding company therein.

66% of the consolidated financial statements were prepared in accordance with IFRS (26% Swiss GAAP FER, 8% US GAAP).

The five biggest areas of divergence between companies are presented in this publication.

### Accounting standards



# Financial statements structure and terminology

The new Swiss financial reporting law (reflected in the updated Code of Obligations) introduces a new structure and terminology for the balance sheet and income statement. It constitutes a significant change from the past where companies had more choice and flexibility. The new law sets out a structure for the order and terms of the balance sheet and income statement captions.

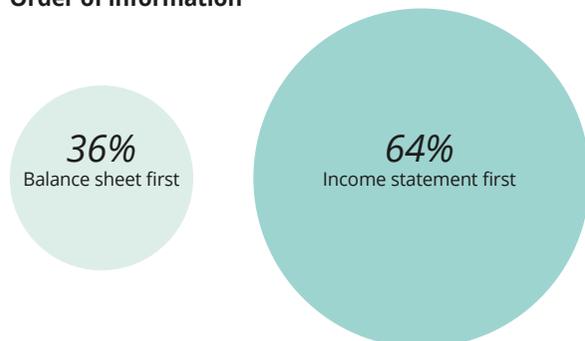
## Balance sheet – deviation from Code of Obligations



2%  
Not at all

In practice, we noted that the wording used by companies diverged from the specific terms set out in the new financial reporting law to a varying extent. Some companies used the exact wording of the law with few modifications, whereas other companies used wording which differed significantly from the legal text of the law and instead was closer to wording used in other accounting standards (mainly IFRS).

## Order of information



The graph on the left column illustrates that a total of 44% of the surveyed companies used either the exact wording of the law for balance sheet items (2%) or only minor changes (42%). 32% of companies, however, made a moderate changes and 24% made significant changes. Where there were many changes, the wording used was similar to terminology used in international accounting standards such as IFRS.

## Income statement – deviation from Code of Obligations



This gap was even larger when analysing the changes for the captions of the income statement. 38% of analysed companies showed strong changes to the wording of the Code of Obligations, whereas 34% show only few differences. Worth mentioning is also the order of the presentation of the primary statements within the financial statements: 36% of the companies analysed presented the balance sheet before the income statement, which is consistent with the order presented in the Code of Obligations, while 64% of companies presented the income statement before the balance sheet, mirroring the order within the international financial reporting standards including IFRS.

### Observation:

Companies need to strike the right balance between a strict application of the terms of the revised Code of Obligations and providing the best possible clarity and transparency for the readers of the financial statements.

### Recommendation:

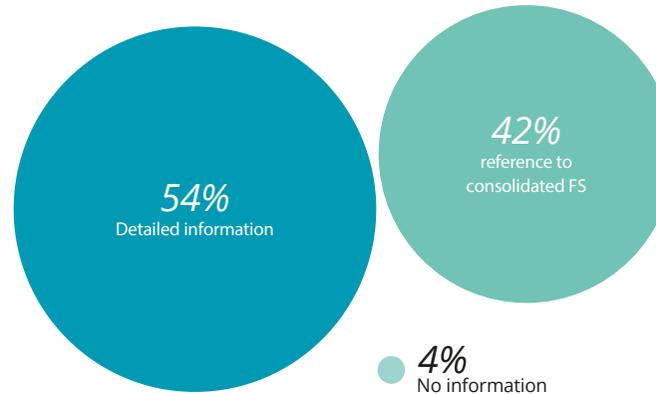
We recommend wording financial statement items according to the Code of Obligations (available in German, French and Italian). Where appropriate, the wording should be tailored to the company's circumstances in order to provide a maximum level of readability and clarity. For example, we consider the description "cash and cash equivalents" instead of "cash and cash equivalents and current assets with a stock exchange price" could be more appropriate, if the company does not have any current assets with a stock exchange price.

Additionally, we recommend to generally use the wording of the Code of Obligations if the new financial reporting law shows a different wording: for example "retained earnings" (Code of Obligations) instead of "voluntary retained earnings" (new financial reporting law).

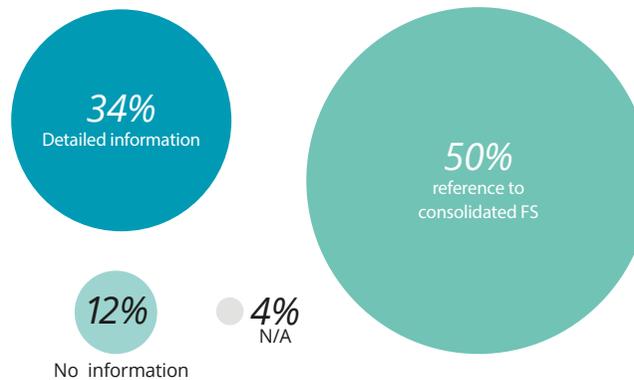
# Disclosure of subsidiaries

Art. 959c para. 2 no. 3 CO requires companies to disclose the name, legal form, registered office as well as the share capital and voting rights held in direct and substantial indirect subsidiaries. Based on our analysis however, only 54% of companies disclosed complete information regarding direct subsidiaries; and only 34% show the required information about substantial indirect subsidiaries within the notes to the standalone financial statements (i.e. the holding company). Instead, for direct subsidiaries 42% of the companies only refer to the disclosure notes to the consolidated financial statements of the group (published in the same document) which have been prepared in accordance with other financial reporting standards (mainly IFRS or US GAAP). For the disclosure of substantial indirect subsidiaries, 50% of the analysed companies only refer to the consolidated financial statements.

## Disclosure of direct subsidiaries



## Disclosure of substantial indirect subsidiaries



### Observation:

Taking this approach gives rise to a risk that the information required by the new financial reporting law are not completely provided for the reader of the statutory financial statements. This is because the financial reporting standard used to prepare the consolidated financial statements does not necessarily fulfil the same disclosure requirements with regard to subsidiaries as the new financial reporting law.

### Recommendation:

We recommend to disclose each direct and substantial indirect subsidiary separately, including information about the subsidiary's name, legal form, registered office, share capital and held voting rights in the standalone financial statements instead of referring to disclosure notes within the consolidated financial statements. This will ensure full compliance of the statutory financial statements with the new financial reporting law.

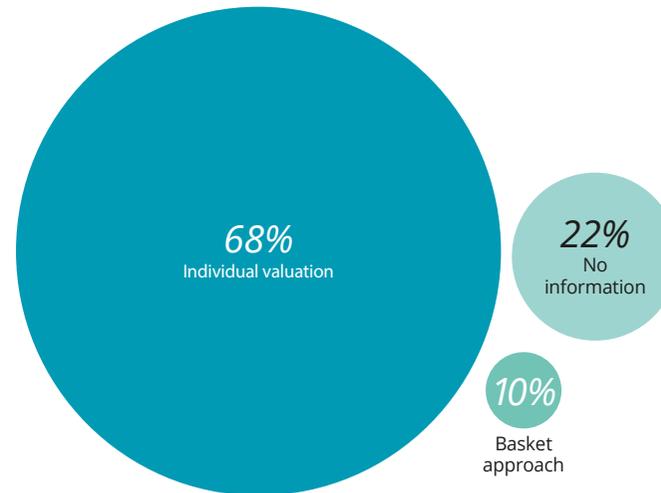
# Individual and group valuation

The new financial reporting law requires companies to value their assets and liabilities on an individual basis. This includes any value adjustments which have to be evaluated and recognised separately for each asset. This generally applies to all items in the balance sheet. In some circumstances, however, it is possible to break through this principal rule: if assets or liabilities are of similar nature and if they are usually valued on group basis. Such assets are for example account receivables with similar due dates for payments and homogeneous inventory items.

The requirement to generally value assets individually also applies to investments. Exceptions are possible but only in very rare cases such as if one or more investments are managed as economical units which cannot stand alone. For example, if an entity is responsible for production work whereas another entity manages the sales of these products. In such cases the economical success of both entities might be inseparably linked.

Our analysis shows that 68% of the analysed companies' annual reports explicitly state that they value their subsidiaries or rather investments individually. However, other companies (10%) state in the disclosure notes that they apply a group valuation (basket approach) while 22% of the companies do not provide any information about their valuation approach.

## Valuation of subsidiaries



### Observation:

Applying a group valuation for investments – and for other assets, especially investments/subsidiaries – is not expressly permitted by applicable law and therefore is only permitted in exceptional cases: only if entities represent economical units. By applying a group valuation for investments, there is a risk that individual investments may not be evaluated individually for impairment, which may result in materially misstating the financial statements.

### Recommendation:

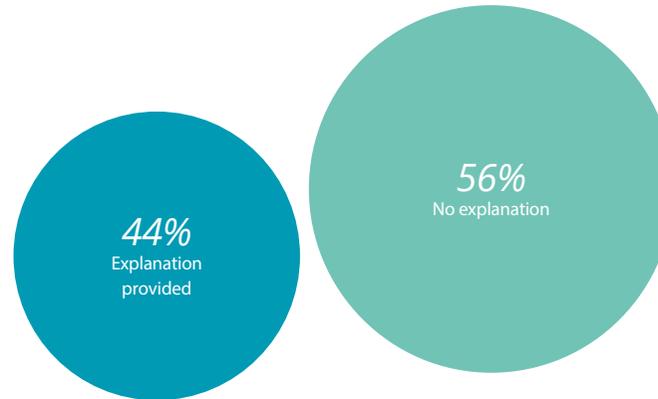
We recommend to value assets and investments in particular individually, because the hurdle for permission of group valuation is high. The group valuation method should be only used for the initial and subsequent measurement of homogeneous items such as accounts receivable and inventory.

# Reliefs due to consolidated accounts

Companies that are subject to an ordinary audit by law must disclose additional information in their financial statements. This refers to additional information in the disclosure notes, a cash flow statement and a management report. However, such additional information may be dispensed if the company itself or a legal entity that controls the company in question prepares consolidated financial statements in accordance with a financial reporting standard (IFRS as per IASB, IFRS for SMEs as per IASB, Swiss GAAP FER, US GAAP as per FASB) recognised in Switzerland (Art. 961d para. 1 CO).

This benchmark shows that all of the analysed annual reports make use of the previously mentioned relief paragraph. However, only 44% of these companies explain this dispensation in the notes by referring to the consolidated financial statements. Such a note is helpful for users of financial statements because the user is referred to the consolidated financial statements regarding the additional information.

## Information about dispensation



### Observation:

Without any explanation the users of the financial statements must “work out” the dispensation of additional information due to the preparation of consolidated financial statements in accordance with a recognised financial reporting standard. In addition, they have no support to directly find the required information in the consolidated financial statements.

### Recommendation:

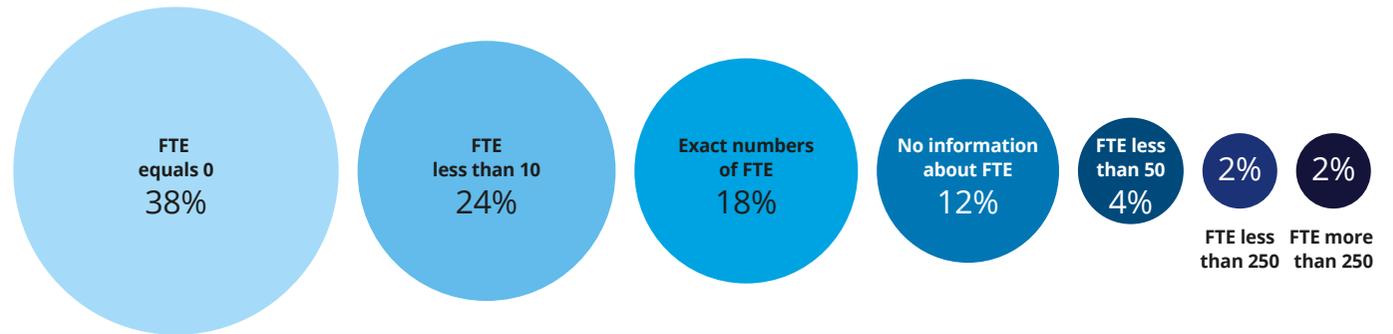
We recommend adding a paragraph to the statutory financial statements referring to the consolidated financial statements in order to explain the non-disclosure of additionally required information in accordance with the relief paragraph, if applicable. This paragraph provides clarity and transparency to the user of the financial statements. Furthermore, this is an important piece of information to any minority shareholders who may want additional information to be disclosed in the annual report (Art. 961d para. 2 CO).

# Disclosure information about full time equivalents

Disclosure notes form an integral part of the annual statutory financial statements. They play an important role in providing supplemental financial and non-financial information to the user of the financial statements which are not available from the balance sheet or the income statement. Thus, the legislator requires companies to disclose certain information as a minimum (in particular art. 959c CO). For instance, companies have to provide information on whether they employ not more than 10, 50 or 250 full-time equivalents on an annual average.

12% of the analysed companies did not present any information about the numbers of full-time equivalents.

## Information about dispensation



### Observation:

Our analysis highlights that some companies omitted to provide all of the requisite disclosures during the first year of applying the new financial reporting law.

### Recommendation:

We recommend that preparers of the financial statements ensure that all relevant and applicable information as required by law is disclosed. This includes, in this particular case, a statement whether the average annual number of full-time equivalents does not exceed 10, 50 or 250.

# Conclusion

The first year of application of the new financial reporting law shows that companies interpret the new requirements differently on certain topics. This leads to divergent applications and thus less readability and comparability. It is therefore important to be aware of common pitfalls when applying the new financial reporting law in order to ensure compliant financial statements and achieve the maximum clarity.

We trust that this benchmark of financial statements provides useful information and insights in the context of the preparation for the second year of preparation of the statutory financial statements under new Swiss law.

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