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cutting through complexity

The New Law on Accounting and Financial Reporting

Accounting and financial reporting in a foreign currency

Determination of the functional currency

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Sources used / citations

The texts in this brochure are largely based on the following sources:

- Swiss Auditing Manual, volume "Accounting and Financial Reporting", chapter II.3.4.2 and chapter II.3.4.3. EXPERTsuisse (formerly Treuhand-Kammer) 2014 [hereinafter: HWP/MAS 2014].

- Selected questions and answers on the new law on accounting and financial reporting, question 7.3. EXPERTsuisse 2015 [hereinafter: Q&A 2015, question 7.3].

In the interest of readability, these sources will be quoted only in the title of each chapter, even if some passages were incorporated verbatim. KPMG has contributed significantly to these two aforementioned publications.

Terminology Used

The following terms are used in this brochure:

- Foreign currency differences: Generic term, includes exchange rate differences and translation differences.

- Exchange rate differences: Foreign currency differences arising from the recording of transactions or from the valuation of balance sheet items in a foreign currency.

- Translation differences: Foreign currency differences from the translation of financial statements in a foreign currency to Swiss francs.

1. Background and preliminary remarks

On 23 December 2011, the Swiss Parliament enacted the new law on accounting and financial reporting. It became effective as at 1 January 2013. The new provisions are applicable to financial statements for the 2015 financial year, and as of 2016 for consolidated accounts, respectively.

The legislator proved to be quite progressive when it came to the currency used for accounting and financial reporting in the stand-alone financial statements. While the previous law did not regulate the accounting currency, the new legislation explicitly allows the accounting in a foreign currency. Previously, it was mandatory to present the financial statements in Swiss francs but the new provisions allow for financial reporting in the currency relevant to the company's business activities. However, if the annual financial statements are not prepared in the national currency, the values must additionally be disclosed in Swiss francs. The relevant provisions are found in art. 957a para. 4 CO and art. 958d para. 3 CO:

B. Accounting	Art. 957a para. 4 CO [4] Accounting is carried out in the national currency or in the currency relevant for the company's business activities.
IV. Presentation, currency and language	Art. 958d para. 3 CO [3] Financial statements are presented in the national currency or in the currency relevant to the company's business activities. If the national currency is not used, the values must also be shown in the national currency. The exchange rates applied must be disclosed in the notes to the accounts and if applicable explained.

During the discussion on the accounting in a foreign currency it soon became clear that company law aspects pose an obstacle to a simple implementation of this new accounting alternative. For example, the relevant provisions of the company law for the share capital pertain to Swiss francs (art. 621 and 622 para. 4 CO). Further provisions on the equity are based on the share capital in Swiss francs (for example in regard to the allocation to reserves and the capital protection). Consequently, for assessing company law matters, the figures in Swiss francs continue to be relevant. The contradiction between the new accounting law and the still unchanged company law can be bridged in this context, albeit at the price of increased complexity.

This publication is intended as a practical tool when changing the currency of the accounting and/or financial reporting. By way of introduction, the first part discusses the criteria for determining the functional currency. The second part primarily presents the steps to implement the transition using illustrative examples. The third and last part treats the accepted methods for translating the financial statements into Swiss francs, which is an additional requirement if the company prepares its stand-alone statutory financial statements in a foreign currency.

2. Determination of the functional currency

[Basis: HWP/MAS 2014, II.3.4.2]

The accounting and financial reporting may be prepared in the currency relevant to the company's business activities (cf. art. 957a para. 4 and art. 958d para. 3 CO). Although the law does not define the term "currency relevant to the company's business activities", it can be deduced (art. 958 para. 1 CO) that it should be the currency that allows third parties to form a reliable judgment about the company's economic situation.

Taking into consideration other accounting standards, the currency relevant to the company's business activities is comparable to the concept of the functional currency. A company's functional currency is the currency of the primary economic environment in which the company operates and in which the cash flows mainly occur. In determining the functional currency, the following factors should be taken into account:

- the currency in which the sales prices of goods and services are denominated and settled;

- the currency of the country whose competitive forces and regulations mainly determine the sales prices of the company's goods and services;

- the currency that mainly influences labour, material and other costs of providing goods and services.

In addition to these primary factors, the currency in which financing activities are carried out or the currency in which receipts from operating activities are usually retained are indicators of a company's functional currency.

If a company makes use of the option to do its accounting in the currency relevant to the company's business activities, it cannot be expected to keep tracking historical cost values in Swiss francs in the long term. The cost value relevant for future valuation will then be available in the functional currency only.

As art. 957a para. 4 CO provides a choice, the accounting may always be in Swiss francs, even if the Swiss franc is not the currency relevant to the company's business activities. Only the choice of a foreign currency must be justified.

3. Changing the currency of accounting and/or financial reporting

3.1 Basic principles and overview

3.1.1 Translation of financial statements in a foreign currency under previous law (accounting in foreign currency)
[Basis: Q&A 2015, question 7.3]

Under previous law, the inventory, the income statement as well as the balance sheet had to be prepared in the national currency (art. 960 para. 1 old CO). The accounting currency was not regulated by law. In practice, accounting in a foreign currency was accepted as long as the annual financial statements were prepared in Swiss francs in accordance with company law provisions. The accounting currency underlying the annual financial statements in theory was not meant to influence the annual financial statements in Swiss francs and therefore "did not exist" conceptually.

Under previous law in the case of accounts kept in a foreign currency, there were essentially two basic options for converting foreign currency accounts into financial statements in Swiss francs authoritative under company law (cf. HWP/MAS 2009, Volume 1, chapter IV.6.1.2):

Modified current/non-current method

- Translation of current assets and current liabilities at the closing rate
- Translation of the non-monetary non-current assets at historical rates
- Translation of the monetary non-current assets at historical rates or lower closing rates, respectively
- Translation of the monetary non-current liabilities at historical rates or higher closing rates, respectively
- Translation of shareholders' equity at historical rates
- Translation of the income statement at the annual average rate
- Recognition of translation differences in the income statement, taking into account the imparity principle (provisioning of unrealized gains)

Modified closing rate method

- Translation of assets and liabilities at the closing rate
- Translation of shareholders' equity at historical rates
- Translation of the income statement at the annual average rate
- Recognition of translation differences in the income statement, taking into account the imparity principle (provisioning of unrealized gains)

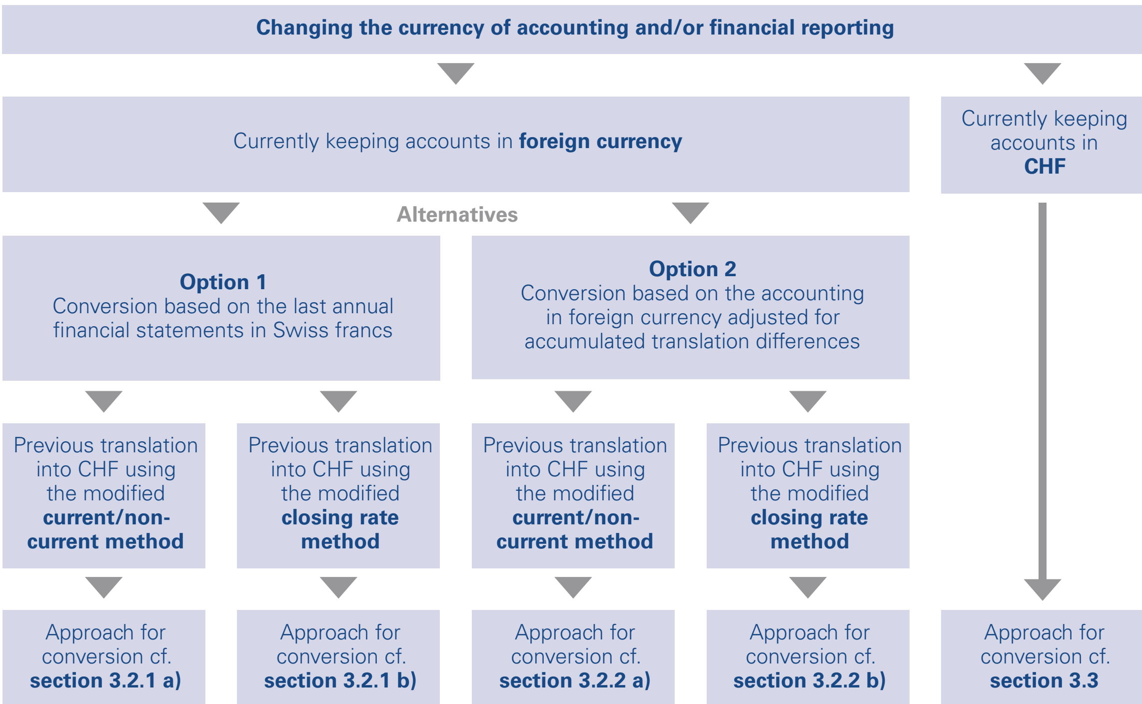
Important note:
The two methods described above remain applicable for those cases in which – in continuation of the previous practice – the accounts are kept in a foreign currency while the financial statements are prepared in Swiss francs.

3.1.2 Changing the currency of accounting and/or financial reporting – overview of alternatives

If *currently keeping accounts in a foreign currency,* a company may choose between the following two options for changing the currency used for the financial statements. Depending on the chosen option, the financial impact in the year of the transition may vary significantly. Accordingly, it is recommended to carefully assess the impact beforehand. Apart from the chosen option, the financial impact also depends on the current method used for translating the financial statements (modified current/non-current method or modified closing rate method, cf. section 3.1.1).

If *currently keeping accounts in Swiss francs,* a company has only one recognized option and accordingly no possibility to influence the translation impact.

Depending on the current accounting currency, the chosen alternative as well as the method used until now for the translation of the financial statements, the following outlines the approach to changing currencies recognized by the auditing profession, using illustrative examples (cf. figure):



3.2 Existing accounting in a foreign currency

3.2.1 Option 1: Conversion based on the last annual financial statements in Swiss francs

a) Previous translation into CHF using the modified current/non-current method
[Basis: Q&A 2015, question 7.3]

Option 1 consists of a transparent and traceable transition from the last annual financial statements in Swiss francs to the opening balance sheet in the foreign currency, the conversion date thus establishing the new historical carrying amounts and exchange rates. However, with the exception of the net working capital, these calculated foreign currency values will most probably not correspond to the underlying, already existing accounting information in the foreign currency as the latter values were translated into Swiss francs at historical rates for preparing the financial statements. As a consequence, the new foreign currency basis does not match the existing accounting information but instead establishes new values.

For the conversion it is recommended to follow a three-step approach:

Step 1: Assets and liabilities from the last financial statements in Swiss francs are translated into the foreign currency in question using the exchange rate at the date of the change. (IFRS users are familiar with this type of conversion from the change of functional currency in IAS 21.35-37.)

Step 2: Long-term monetary items are adjusted to their nominal value (less any accumulated impairment losses) through the income statement. Any translation gains realized through the income statement are justified with the change in currency.

Step 3: Existing provisions for unrealized translation gains, converted using the exchange rate at the date of the change, must be released through the income statement. Should such a provision not be released, it represents a hidden reserve going forward.

Illustrative example 1 a)

- Existing accounting in a foreign currency
- Conversion based on the last financial statements prepared in CHF (= option 1)
- Previous translation into CHF using the modified current/non-current method

2014 financial statements (=starting base, accounting in EUR/financial reporting in CHF)

Rates: Historical EUR = 1 CHF, closing date EUR = 2 CHF, average EUR = 1.50 CHF

Balance sheet	**EUR**	**Exchange rate**	**CHF**
Cash and cash equivalents	50.0	2.00	100.0
Long-term loans	200.0	1.00	200.0
Investments	80.0	1.00	80.0
Property, plant and equipment	120.0	1.00	120.0
Total assets	**450.0**		**500.0**
Long-term loans payable	150.0	2.00	300.0
Provision for unrealized translation gains			0.0
Shareholders' equity			
• Share capital	150.0	1.00	150.0
• Voluntary retained earnings			
– Results carried forward	100.0	1.00	100.0
– Net loss/profit for the year	50.0		-50.0
Total liabilities and shareholders' equity	**450.0**		**500.0**
Income statement			
Profit/loss excluding foreign currency result	50.0	1.50	75.0
Foreign currency result (as part of financial income or expenses)			-125.0
Net loss/profit for the year	*50.0*		*-50.0*

Illustrative example 1 a) – continuation

2015 financial statements (transition to accounting and financial reporting in EUR as at 1.1.2015)

	Opening balance sheet 1.1.2015			Period (adjustment of opening balance sheet)	Period (business activity)	Closing balance sheet 31.12.2015 / Income Statement 2015
Balance sheet	**CHF**	**Exchange rate**	**EUR**	**EUR**	**EUR**	**EUR**
Cash and cash equivalents	100.0	2.00	50.0		100.0	150.0
Long-term loans	200.0	2.00	100.0	100.0		200.0
Investments	80.0	2.00	40.0			40.0
Property, plant and equipment	120.0	2.00	60.0			60.0
Total assets	**500.0**		**250.0**			**450.0**
Long-term loans payable	300.0	2.00	150.0			150.0
Provision for unrealized translation gains	0.0	2.00	0.0	0.0		0.0
Shareholders' equity						
• Share capital	150.0	2.00	75.0			75.0
• Voluntary retained earnings						
– Results carried forward	50.0	2.00	25.0			25.0
– Net loss/profit for the year				100.0	100.0	200.0
Total liabilities and shareholders' equity	**500.0**		**250.0**			**450.0**
Income statement						
Profit/loss excluding foreign currency result					100.0	100.0
Foreign currency result (as part of financial income or expenses)				100.0		100.0
Net loss/profit for the year				*100.0*	*100.0*	*200.0*

Step 1: Translation of the last CHF financial statements using the exchange rate at the date of the change

Step 2: Adjustment of long-term monetary positions to their nominal values in the foreign currency through the income statement

Step 3: Release of the provision for unrealized translation gains through the income statement

Note:
The balance sheets / income statements presented in the illustrative examples are limited to information relevant for illustrating the steps and therefore do not represent the new accounting legislation's requirements on minimum structure.

b) Previous translation into CHF using the modified closing rate method

With the modified closing rate method, all assets and liabilities were already translated at the closing rate for the last annual financial statements. In contrast to the procedure described in the preceding section, where the previous financial statements have been translated using the modified current/non-current method, the second step can be dispensed with if previously the modified closing rate method was used. The other steps remain the same.

Accordingly, the approach with the following steps is recommended:

Step 1: Assets and liabilities from the last financial statements in Swiss francs are translated into the foreign currency in question using the exchange rate at the date of the change.

Step 2: Existing provisions for unrealized translation gains, converted using the exchange rate at the date of the change, must be released through the income statement. Should such a provision not be released, it represents a hidden reserve going forward.

Illustrative example 1 b)

- Existing accounting in a foreign currency
- Conversion based on the last financial statements prepared in CHF (= option 1)
- Previous translation into CHF using the modified closing rate method

2014 financial statements (=starting base, accounting in EUR/financial reporting in CHF)

Rates: Historical EUR = 1 CHF, closing date EUR = 2 CHF, average EUR = 1.50 CHF

Balance sheet	EUR	Exchange rate	CHF
Cash and cash equivalents	50.0	2.00	100.0
Long-term loans	200.0	2.00	400.0
Investments	80.0	2.00	160.0
Property, plant and equipment	120.0	2.00	240.0
Total assets	**450.0**		**900.0**
Long-term loans payable	150.0	2.00	300.0
Provision for unrealized translation gains			275.0
Shareholders' equity			
• Share capital	150.0	1.00	150.0
• Voluntary retained earnings			
– Results carried forward	100.0	1.00	100.0
– Net loss/profit for the year	50.0		75.0
Total liabilities and shareholders' equity	**450.0**		**900.0**

Income statement	EUR	Exchange rate	CHF
Profit/loss excluding foreign currency result	50.0	1.50	75.0
Foreign currency result (as part of financial income or expenses)			0.0
Net loss/profit for the year	*50.0*		*75.0*

Illustrative example 1 b) – continuation

2015 financial statements (transition to accounting and financial reporting in EUR as at 1.1.2015)

	Opening balance sheet 1.1.2015			Period (adjustment of opening balance sheet)	Period (business activity)	Closing balance sheet 31.12.2015 / Income Statement 2015
Balance sheet	**CHF**	**Exchange rate**	**EUR**	**EUR**	**EUR**	**EUR**
Cash and cash equivalents	100.0	2.00	50.0		100.0	150.0
Long-term loans	400.0	2.00	200.0			200.0
Investments	160.0	2.00	80.0			80.0
Property, plant and equipment	240.0	2.00	120.0			120.0
Total assets	**900.0**		**450.0**			**550.0**
Long-term loans payable	300.0	2.00	150.0			150.0
Provision for unrealized translation gains	275.0	2.00	137.5	-137.5		0.0
Shareholders' equity						
• Share capital	150.0	2.00	75.0			75.0
• Voluntary retained earnings						
– Results carried forward	175.0	2.00	87.5			87.5
– Net loss/profit for the year				137.5	100.0	237.5
Total liabilities and shareholders' equity	**900.0**		**450.0**			**550.0**
Income statement						
Profit/loss excluding foreign currency result					100.0	100.0
Foreign currency result (as part of financial income or expenses)				137.5		137.5
Net loss/profit for the year				*137.5*	*100.0*	*237.5*

Step 1: Translation of the last CHF financial statements using the exchange rate at the date of the change

Step 2: Release of the provision for unrealized translation gains through the income statement

3.2.2 Option 2: Conversion based on the accounting in foreign currency adjusted for accumulated translation differences

a) Previous translation into CHF using the modified current/non-current method [Basis: Q&A 2015, question 7.3]

In contrast to option 1 shown in section 3.2.1 a), in *option 2* in the result also the non-monetary long-term positions (non-current assets and long-term liabilities) are adjusted to their previous value according to the foreign currency accounting records. But just as for option 1, there must be a transparent transition from the last financial statements in Swiss francs to the new opening balances in the foreign currency, since under CO accounting principles, changes to equity must be recorded in the income statement (unless they are a direct capital contribution or a repayment to the shareholders).

In the light of this, the following approach for the conversion is recommended:

Step 1: Assets and liabilities from the last financial statements in Swiss francs are translated into the foreign currency in question using the exchange rate at the date of the change.

Step 2: The non-current assets and non-current liabilities are adjusted to their historical acquisition costs in the foreign currency (if applicable less accumulated depreciation and impairment losses) through the income statement. This means that accumulated translation gains or losses are recognized in the income statement. Any gains realized through the income statement are justified with the change in the accounting currency. This step also restores long-term monetary positions to their nominal value in the foreign currency (if applicable less accumulated impairment losses).

Step 3: Existing provisions for unrealized translation gains, converted using the exchange rate at the date of the change, must be released through the income statement. Should such a provision not be released, it represents a hidden reserve going forward.

Future annual financial statements in the foreign currency are based on the existing historical accounting records. In addition, the shareholders' equity in the first financial statements in foreign currency corresponds to the equity of the last annual financial statements in Swiss francs, converted at historical exchange rates and increased/decreased by the transparently disclosed net profit or loss of the financial statements in the foreign currency.

With this option the accumulated translation differences are realized through the income statement, which may have a major impact on the transition year's income statement. The transition to a new accounting currency, however, is a "normal" transaction in the statutory financial statements that must be recognized according to the principles of orderly accounting and reporting. Recognizing the conversion gain or loss directly in equity is therefore not permissible.

Illustrative example 2 a)

- Existing accounting in a foreign currency
- Conversion based on the accounting in foreign currency adjusted for accumulated translation differences (= option 2)
- Previous translation into CHF using the modified current/non-current method

2014 financial statements (=starting base, accounting in EUR/financial reporting in CHF)

Rates: Historical EUR = 1 CHF, closing date EUR = 2 CHF, average EUR = 1.50 CHF

Balance sheet	**EUR**	**Exchange rate**	**CHF**
Cash and cash equivalents	50.0	2.00	100.0
Long-term loans	200.0	1.00	200.0
Investments	80.0	1.00	80.0
Property, plant and equipment	120.0	1.00	120.0
Total assets	**450.0**		**500.0**
Long-term loans payable	150.0	2.00	300.0
Provision for unrealized translation gains			0.0
Shareholders' equity			
• Share capital	150.0	1.00	150.0
• Voluntary retained earnings			
– Results carried forward	100.0	1.00	100.0
– Net loss/profit for the year	50.0		-50.0
Total liabilities and shareholders' equity	**450.0**		**500.0**

Income statement			
Profit/loss excluding foreign currency result	50.0	1.50	75.0
Foreign currency result (as part of financial income or expenses)			-125.0
Net loss/profit for the year	*50.0*		*-50.0*

Illustrative example 2 a) – continuation

2015 financial statements (transition to accounting and financial reporting in EUR as at 1.1.2015)

	Opening balance sheet 1.1.2015			Period (adjustment of opening balance sheet)	Period (business activity)	Closing balance sheet 31.12.2015 / Income Statement 2015
Balance sheet	**CHF**	**Ex-change rate**	**EUR**	**EUR**	**EUR**	**EUR**
Cash and cash equivalents	100.0	2.00	50.0		100.0	150.0
Long-term loans	200.0	2.00	100.0	100.0		200.0
Investments	80.0	2.00	40.0	40.0		80.0
Property, plant and equipment	120.0	2.00	60.0	60.0		120.0
Total assets	**500.0**		**250.0**			**550.0**
Long-term loans payable	300.0	2.00	150.0			150.0
Provision for unrealized translation gains	0.0	2.00	0.0	0.0		0.0
Shareholders' equity						
• Share capital	150.0	2.00	75.0			75.0
• Voluntary retained earnings						
– Results carried forward	50.0	2.00	25.0			25.0
– Net loss/profit for the year				200.0	100.0	300.0
Total liabilities and shareholders' equity	**500.0**		**250.0**			**550.0**
Income statement						
Profit/loss excluding foreign currency result					100.0	100.0
Foreign currency result (as part of financial income or expenses)				200.0		200.0
Net loss/profit for the year				*200.0*	*100.0*	*300.0*

Step 1: Translation of the last CHF financial statements using the exchange rate at the date of the change

Step 2: Adjustment of non-current positions to their historical values in the foreign currency recognized through the income statement

Step 3: Release of the provision for unrealized translation gains through the income statement

b) Previous translation into CHF using the modified closing rate method

With the previous translation of the foreign currency accounts using the modified closing rate method, option 2 leads to the exact same result as option 1. For this reason, please refer to the explanations and the illustrative example 1 b) in section 3.2.1 b).

3.2.3 Side note: Continuation of accounting data in the foreign currency (without any further adjustments) is not a permissible option

[Basis: Q&A 2015, question 7.3]

If accounting data were to be continued in the foreign currency, the existing carrying amounts in the foreign currency would serve as a basis for the opening balance sheet in the foreign currency. The previous reporting was based on the historical data in the foreign currency and basically already existed in this form. Neither these values as such nor the "values in the national currency" derived from these (cf. the explanations in section 4) would have a directly traceable connection to the last statutory financial statements in Swiss francs that were approved by the Annual General Meeting. A reconciliation of the equity from the last statutory financial statements in Swiss francs to the opening balance sheet in foreign currency would not be possible. Therefore, this particular version as-is is not permissible. As a possible workaround, cf. option 2 in section 3.2.2.

Illustrative example 3

- Existing accounting in a foreign currency
- Continuation of accounting data in the foreign currency
- Previous translation into CHF using the modified current/non-current method

Important note:
As explained in the text above, the transition option shown in the following is not permissible. Illustrative example 3 is only to illustrate the conceptual differences compared to option 2 presented in section 3.2.2, which represents the permissible option to continue the existing accounting data in a foreign currency.

2014 financial statements (=starting base, accounting in EUR/financial reporting in CHF)

Rates: Historical EUR = 1 CHF, closing date EUR = 2 CHF, average EUR = 1.50 CHF

Balance sheet	EUR	Exchange rate	CHF
Cash and cash equivalents	50.0	2.00	100.0
Long-term loans	200.0	1.00	200.0
Investments	80.0	1.00	80.0
Property, plant and equipment	120.0	1.00	120.0
Total assets	**450.0**		**500.0**
Long-term loans payable	150.0	2.00	300.0
Provision for unrealized translation gains			0.0
Shareholders' equity			
• Share capital	150.0	1.00	150.0
• Voluntary retained earnings			
– Results carried forward	100.0	1.00	100.0
– Net loss/profit for the year	50.0		-50.0
Total liabilities and shareholders' equity	**450.0**		**500.0**

Income statement			
Profit/loss excluding foreign currency result	50.0	1.50	75.0
Foreign currency result (as part of financial income or expenses)			-125.0
Net loss/profit for the year	*50.0*		*-50.0*

Illustrative example 3 – continuation

2015 financial statements (transition to accounting and financial reporting in EUR as at 1.1.2015)

	Opening balance sheet 1.1.2015			Period (adjustment of opening balance sheet)	Period (business activity)	Closing balance sheet 31.12.2015 / Income Statement 2015
Balance sheet	**CHF**	**Ex-change rate**	**EUR**	**EUR**	**EUR**	**EUR**
Cash and cash equivalents			50.0		100.0	150.0
Long-term loans			200.0			200.0
Investments			80.0			80.0
Property, plant and equipment			120.0			120.0
Total assets			**450.0**			**550.0**
Long-term loans payable			150.0			150.0
Shareholders' equity						
• Share capital			150.0			150.0
• Voluntary retained earnings						
– Results carried forward			150.0			150.0
– Net loss/profit for the year					100.0	100.0
Total liabilities and shareholders' equity			**450.0**			**550.0**
Income statement						
Profit/loss excluding foreign currency result					100.0	100.0
Foreign currency result (as part of financial income or expenses)						0.0
Net loss/profit for the year					*100.0*	*100.0*

Compared to the permissible transition option 2 according to the illustrative example 2 a), the net profit for the year would be lower by EUR 200 since no conversion adjustments were recognized in the income statement. Assets and liabilities would be identical, just as the total equity. However, there would be significant differences in the individual positions within equity compared to option 2. On the one hand, this would be due to the missing translation from the last financial statements in Swiss francs and on the other hand due to the differing net profit.

3.3 Existing accounting in Swiss francs

[Basis: Q&A 2015, question 7.3]

To a company currently accounting in Swiss francs, no historical accounting data in a foreign currency is available. The values that are now determined in the foreign currency for the first time for the opening balance sheet will then constitute the historical carrying values (if applicable less accumulated depreciation and impairment losses), and the applicable exchange rate (closing rate of conversion) will be the historical exchange rate.

For this purpose, the following approach is recommended:

Step 1: Assets and liabilities from the last financial statements in Swiss francs are translated into the foreign currency in question using the exchange rate at the date of the change.

Step 2: Long-term monetary items are adjusted to their nominal value (less any accumulated impairment losses) through the income statement. Any gains realized through the income statement are justified with the change in currency.

Step 3: Existing provisions for unrealized exchange rate gains, converted using the exchange rate at the date of the change, must be released through the income statement (with the exception of any unrealized translation gains related to a third currency). Should such a provision not be released, it represents a hidden reserve going forward.

Illustrative example 4

- Existing accounting in Swiss francs

2014 financial statements (=starting base, accounting/financial reporting in CHF; only monetary items denominated in a foreign currency are subject to translation)

Rates: Historical EUR = 1 CHF, closing date EUR = 2 CHF, average EUR = 1.50 CHF

Balance sheet	**EUR**	**Exchange rate**	**CHF**
Cash and cash equivalents	50.0	2.00	100.0
Long-term loans	200.0	1.00	200.0
Investments			80.0
Property, plant and equipment			120.0
Total assets			**500.0**
Long-term loans payable	150.0	2.00	300.0
Shareholders' equity			
• Share capital			150.0
• Voluntary retained earnings			
– Results carried forward			100.0
– Net loss/profit for the year			-50.0
Total liabilities and shareholders' equity			**500.0**
Income statement			
Profit/loss excluding foreign currency result			75.0
Foreign currency result (as part of financial income or expenses)			-125.0
Net loss/profit for the year			*-50.0*

Illustrative example 4 – continuation

2015 financial statements (transition to accounting and financial reporting in EUR as at 1.1.2015)

	Opening balance sheet 1.1.2015			Period (adjustment of opening balance sheet)	Period (business activity)	Closing balance sheet 31.12.2015 / Income Statement 2015
Balance sheet	**CHF**	**Exchange rate**	**EUR**	**EUR**	**EUR**	**EUR**
Cash and cash equivalents	100.0	2.00	50.0		100.0	150.0
Long-term loans	200.0	2.00	100.0	100.0		200.0
Investments	80.0	2.00	40.0			40.0
Property, plant and equipment	120.0	2.00	60.0			60.0
Total assets	**500.0**		**250.0**			**450.0**
Long-term loans payable	300.0	2.00	150.0			150.0
Shareholders' equity						
• Share capital	150.0	2.00	75.0			75.0
• Voluntary retained earnings						
– Results carried forward	50.0	2.00	25.0			25.0
– Net loss/profit for the year				100.0	100.0	200.0
Total liabilities and shareholders' equity	**500.0**		**250.0**			**450.0**
Income statement						
Profit/loss excluding foreign currency result					100.0	100.0
Foreign currency result (as part of financial income or expenses)				100.0		100.0
Net loss/profit for the year				*100.0*	*100.0*	*200.0*

Step 1: Translation of the last CHF financial statements using the exchange rate at the date of the change

Step 2: Adjustment of long-term monetary positions to their nominal values in the foreign currency through the income statement

Step 3: Release of the provision for unrealized exchange rate gains through the income statement [n/a in the present example, cf. *)]

*) When accounting in Swiss francs a provision for unrealized exchange rate gains may only arise from the valuation of long-term monetary positions. The lowest value principle requires that unrealized exchange rate gains are not recognized in the income statement. This does not mean, however, that they cannot be presented separately in the balance sheet. For example, long-term loans may be valued at the closing rate despite a lower historical rate if at the same time a provision for unrealized exchange rate gains in the amount of the corresponding difference is recorded. So in the above illustrative example, it would be possible as an alternative to value the loans of EUR 200 in the 2014 financial statements at the higher closing rate (i.e. CHF 400) and record the difference between closing rate and lower historical rate of CHF 200 as a provision for unrealized exchange rate gains. This would not change the transition result.

3.4 Summary of the principles for changing the accounting and/or financial reporting currency

[Basis: Q&A 2015, question 7.3]

The following principles should be taken into account when changing the accounting and/or financial reporting currency:

1. The starting value are the last annual financial statements in Swiss francs approved by the Annual General Meeting.

2. Translation differences arising from the conversion are recognized in the income statement as extraordinary positions, irrespective of a potentially different tax treatment. It is not permitted to recognize any translation differences resulting from the change of currency directly in shareholders' equity.

3. After a change of the accounting or financial reporting currency, a brief description of the change and a reconciliation of the equity are required in the notes to the annual financial statements (art. 959c para. 1 no. 1 and 2 CO). A possible disclosure of the reconciliation of equity items can be found in the illustrative example 6.

4. For legal reasons, the positions within equity in Swiss francs according to the last financial statements in Swiss francs must be reconcilable to the "values in the national currency" which are to be presented in the financial statements at the end of the year (cf. section 4 as well as the illustrative example 6).

4. Disclosure of the values in Swiss francs

4.1 Basic principles

[Basis: HWP/MAS 2014, II.3.4.3.1]

If the financial reporting is in a different currency than the national currency, the values must also be stated in the national currency (art. 958d para. 3 CO). Consequently, for all the elements of the financial statements (balance sheet, income statement, notes and potentially also cash flow statement) the values must be disclosed in Swiss francs as well.

The CO rules on accounting and financial reporting (in particular the rules applicable to recognition and valuation) must in this case be applied to the values in the functional currency.

The purpose of financial reporting, to present the company's economic situation so as to allow third parties to form a reliable judgment, can only be fulfilled by the annual financial statements in the currency relevant to the company's business activities (art. 958 para. 1 CO), but not by the values in the national currency that must be indicated as well. The values in Swiss francs are intended for information purpose only and should not be used to form a "reliable judgment". In particular as there are no historical exchange rates, it cannot be expected that the indicated values in the national currency convey the same result as if the company had always had its accounting in Swiss francs.

4.2 Translation methods for the disclosure of the values in Swiss francs

[Basis: HWP/MAS 2014, II.3.4.3.1]

Neither the law nor the corresponding dispatch address how the values for the additional disclosure in Swiss francs must be determined. The suitability of a translation method must, however, be assessed not only from a reporting perspective, but also in more detail from the perspectives of the tax and company legislation. The disclosure of the values in the national currency for themselves may in many cases not completely fulfill the accounting rules prescribed in the CO, as fundamental information such as historical acquisition costs are no longer available in Swiss francs (and do no longer have to be available when accounting and financial reporting are carried out in the functional currency). However, in combination with the other elements of the financial statements in the functional currency, they nonetheless fulfill the requirements of the law.

Below are two appropriate methods of translation:
- Method 1: Closing rate method, equity at historical rates
- Method 2: Translation at closing rate, equity valued in the foreign-currency balance sheet

4.2.1 Method 1: Closing rate method, equity at historical rates

a) Translation
[Basis: HWP/MAS 2014, II.3.4.3.2]

With this method the equity items are carried forward at historical exchange rates. The remaining balance sheet items are translated at the closing rate; income statement items and, if applicable, the cash flow statement are translated at the average rate for the period (alternative: also at the closing rate). The resulting translation difference is recognized directly in equity, in the position "translation difference" within retained earnings.

Disclosures in the notes that are directly related to a position in the financial statements are translated using the same exchange rate as for this position. Other disclosures unrelated to financial statement positions are translated either at closing rate or average rate, whichever is more appropriate.

b) Legal aspects
[Basis: HWP/MAS 2014, II.3.4.3.2]

Due to applying historical rates, the changes in the equity items in the national currency, with the exception of the translation difference, can be easily reconciled. The equity item "translation differences" forms part of the retained earnings. The individual equity items in the functional currency and in Swiss francs can deviate significantly over the course of time.

c) Illustrative example: Disclosure of values in Swiss francs (method 1)

Illustrative example 5

- Disclosure of values in Swiss francs
- Method 1: Closing rate method, equity at historical rates [figures from illustrative example 2 a)]

Rates: Historical EUR = 2 CHF, closing date EUR = 3 CHF, average EUR = 2.50 CHF

	Closing balance sheet 31.12.2015 / Income Statement 2015		Values in CHF
Balance sheet	**EUR**	**Ex-change rate**	**CHF**
Cash and cash equivalents	150.0	3.00	450.0
Long-term loans	200.0	3.00	600.0
Investments	80.0	3.00	240.0
Property, plant and equipment	120.0	3.00	360.0
Total assets	**550.0**		**1,650.0**
Long-term loans payable	150.0	3.00	450.0
Shareholders' equity			
• Share capital	75.0	2.00	150.0
• Voluntary retained earnings			
– Results carried forward	25.0	2.00	50.0
– Retained earnings carried forward (translation difference)			250.0
– Net loss/profit for the year	300.0		750.0
Total liabilities and shareholders' equity	**550.0**		**1,650.0**
Income statement			
Profit/loss excluding foreign currency result	100.0	2.50	250.0
Foreign currency result (as part of financial income or expenses)	200.0	2.50	500.0
Net loss/profit for the year	*300.0*		*750.0*

The translation difference presented in retained earnings is composed as follows:

	EUR	**Ex-change rate**	**CHF**
Shareholders' equity in EUR as at 1.1.2015 translated at the exchange rate as at 31.12.2015	100.0	3.00	300.0
./. Shareholders' equity in EUR as at 1.1.2015 translated at the exchange rate as at 1.1.2015	-100.0	2.00	-200.0
Profit 2015, translated at the exchange rate as at 31.12.2015	300.0	3.00	900.0
./. Profit 2015, translated at the 2015 average exchange rate	-300.0	2.50	-750.0
Total translation difference			**250.0**

d) Illustrative example: Reconciliation of equity items in the notes to the financial statements

Illustrative example 6

- Presentation of the reconciliation of the equity items in the notes to the financial statements [figures from illustrative examples 2 a) and 5]

Based on the figures from the illustrative example 2 a) and the resulting data in Swiss francs according to the illustrative example 5, the reconciliation of equity items in the notes to the annual financial statements could be presented as follows:

	EUR			Values in CHF		
Reconciliation of equity items	**Share capital**	**Voluntary retained earnings**	**Total equity**	**Share capital**	**Voluntary retained earnings**	**Total equity**
Amounts in CHF according to Financial Statements 31.12.2014	n/a	n/a	n/a	150.0	50.0	200.0
Amounts in CHF according to Financial Statements 31.12.2014, translated to EUR at the closing rate	75.0	25.0	100.0	n/a	n/a	n/a
Foreign currency result from the change in reporting currency to EUR (recorded in the income statement)		200.0	200.0		500.0	500.0
Net profit for the year 2015 (excluding foreign currency result from the change in reporting currency to EUR)		100.0	100.0		250.0	250.0
Translation difference from the translation of the financial statements to CHF values	n/a	n/a	n/a		250.0	250.0
Total	**75.0**	**325.0**	**400.0**	**150.0**	**1'050.0**	**1'200.0**

4.2.2 Method 2: Translation at closing rate, equity valued in the foreign-currency balance sheet

a) Translation
[Basis: HWP/MAS 2014, II.3.4.3.3]

In this method equity items are carried in Swiss francs and valued in the balance sheet in the foreign currency at the closing rate; unrealized translation losses are recognized through the income statement, whereas unrealized translation gains are recorded in the balance sheet in the functional currency as an accrual item. The adherence to the imparity principle is based on the consideration that the resulting foreign currency difference as per this method represents a valuation difference and therefore any unrealized translation gains may not be recorded in the income statement.

The translation of the entire financial statements (including income statement and cash flow statement, if any) is carried out at the closing rate.

Alternatively, an average exchange rate may be used for the income statement (and the cash flow statement, if any); in this case, the resulting difference to the net profit according to the balance sheet must be recognized in the income statement.

b) Legal aspects
[Basis: HWP/MAS 2014, II.3.4.3.3]

If the translation is performed using the closing rates throughout this method results in a simple carry forward of equity items without additional translation differences in the financial statements in Swiss francs. The positions within equity in the functional currency and in Swiss francs run parallel.

c) Illustrative example: Disclosure of values in Swiss francs (method 2)

The practical application of method 2 is relatively complex. It remains to be seen how often this method will be used in practice. For an illustrative example over the course of six business periods, cf. the following publication (in German):

Buchmann, René / Duss, Fabian / Handschin, Lukas (2013): Rechnungslegung in Fremdwährung. Probleme und Lösungsansätze aus buchhalterischer, handelsrechtlicher und steuerlicher Sicht. (Financial reporting in a foreign currency: issues and solutions from the accounting, commercial law and tax perspective.) In: EXPERT FOCUS (formerly Der Schweizer Treuhänder), 11/2013, p. 823-835.

4.2.3 Overall considerations
[Basis: HWP/MAS 2014, II.3.4.3.4]

The method chosen should be applied consistently and explained transparently in the notes (art. 958d para. 3 CO).

For assessing company law matters, the national currency continues to be relevant. The corresponding provisions in the company law either mention Swiss Francs or do not contain any comments on currency. The legal provisions on equity are orientated towards the capital in Swiss francs. This fact for instance rules out a uniform translation of the entire financial statements (in particular the individual equity items) as at the closing rate, because this would not satisfy the requirements for a proper financial reporting.

Depending on the translation method applied the equity items in the functional currency can deviate from those in Swiss francs, due to (accumulated) translation differences. This has ramifications in particular for the proposed appropriation of retained earnings as well as for the determination of the relevant reference values for capital loss and a repayment of share capital:

Proposed appropriation of retained earnings	Capital loss	Repayment of share capital
• The Board of Directors' proposal on the appropriation of retained earnings must be presented not only in Swiss francs but also in the functional currency; for the maximum distribution, the information in Swiss francs remains decisive. The proposed appropriation of retained earnings in Swiss francs, however, may not exceed the distributable equity items in the functional currency. Furthermore, the development of exchange rates up to the date of the dividend resolution must be observed closely so as to avoid that retained earnings are distributed which are already used up by unfavorable foreign currency developments.	• The provision relating to capital loss (art. 725 para. 1 CO) must for reasons of prudence be adhered to in Swiss francs and in the functional currency, i.e. the corresponding duties requiring action are triggered by the currency that first oversteps the critical threshold value.	• The provision concerning a repayment of share capital (art. 680 para. 2 CO) must for reasons of prudence be adhered to in Swiss francs and in the functional currency, i.e. a violation is triggered by the currency that first oversteps the critical threshold value.

A consistent financial reporting in a foreign currency would also lead to a tax assessment on this basis; however, this is currently still an exception. If the tax authorities make an assessment based on the disclosure of values in Swiss francs, it knowingly accepts that this basis alone hardly corresponds to the valuation provisions prescribed by the Swiss Code of Obligations, cf. the following publication:

Dell'Anna, Fabio / de Haller, Thibaut / Schneider, Laurenz (2015): Funktionale Währung und Darstellungswährung aus steuerlicher Sicht (functional currency and presentation currency from a tax perspective). In: EXPERT FOCUS, 8/2015, p. 619-624.

If for tax purposes effects from the translation are to be eliminated, this must be done outside of the financial statements.

Illustrative example 7

- Presentation of the proposed appropriation of retained earnings when accounting and financial reporting are done in a foreign currency [figures from illustrative example 5]

Proposed Appropriation of Available Earnings 2015

	EUR	CHF
Retained earnings brought forward	25.0	300.0
Net profit for the year	300.0	750.0
Available earnings	**325.0**	**1'050.0**

The Board of Directors proposes to the annual general meeting the following appropriation of retained earnings:

	EUR	CHF
Payment of a dividend in the amount of	100.0	300.0
Allocation to the general legal retained earnings	24.6	59.3
Balance to be carried forward	200.4	690.7
Total	**325.0**	**1'050.0**

The Board of Directors proposes a dividend payment of EUR 100.0, but not exceeding CHF 300.0. At the time of the General Meeting's resolution, the maximum amount of CHF 300.0 is translated to EUR using the applicable exchange rate at that date. If the resulting amount is below the EUR 100.0 proposed for distribution, the distribution will only be of this lower amount. The proposed allocation to the general legal retained earnings remains unchanged even if the dividend amounts are adjusted due to the exchange rate.

Possible alternative wording concerning procedure for allocation to reserves:
(...) The proposed allocation to the general legal retained earnings is reduced to the legally required minimum if the dividend amounts are adjusted due to the exchange rate (allocation in the amount of 5% of the net profit for the year [unchanged] plus 10% of the dividend amount that exceeds 5% of the share capital).

In the present example, the allocation to the general legal retained earnings is calculated as follows:

Required allocation to reserves	EUR	CHF
5% of the net profit for the year up to 20% of the share capital	15.0	30.0
10% on surplus dividend (dividend that exceeds 5% of the share capital) up to 50% of the share capital	9.6	29.3
Total allocation to general legal retained earnings	**24.6**	**59.3**

Note: In the above example with a planned dividend payment of EUR 100.0, the proposed dividend in the CHF column could be increased to a maximum of CHF 975.0 (net profit of CHF 1,050.0 less minimum allocation to reserves of CHF 75.0 up to the threshold of 50% of the share capital) to build a maximum buffer for any exchange rate fluctuations until the resolution by the annual general meeting.

4.3 Disclosure

4.3.1 Disclosure of the values in Swiss francs

As mentioned in section 4.1, the disclosure in Swiss francs is required for all components of the financial statements. This is also specifically applicable to the disclosures in the notes.

The presentation may for instance be in columns, as follows:

	Reporting year		Previous year	
Balance sheet item	EUR	CHF	EUR	CHF

Other presentation forms are possible as well (for example, the complete reproduction of the annual financial statements translated to Swiss francs as a separate disclosure in the notes).

All values (i.e. every individual position) of the annual financial statements must also be disclosed in the national currency.

4.3.2 Disclosure of the applied translation method and the exchange rates used

If the financial reporting is in the currency relevant to the company's business activities (functional currency), the exchange rates used for the translation into the national currency must be disclosed in the notes to the financial statements and explained, if necessary (art. 958d para. 3 CO). In addition to the mere disclosure of the exchange rates used, also the translation method used should be described, for instance closing rates for amounts relating to a certain point in time and average rates for amounts relating to a period.

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