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Annual Review 2011–12

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Strategy

Moving ahead with innovative services.

PwC's strategic objective is to be the number one professional services firm. The firm defines this objective in terms of five criteria: revenues, talent, brand, quality and margins. During its 2011–12 financial year, PwC achieved successes in all five of these areas.

The growth rates PwC achieved last year outpaced those of its largest competitors. The firm's approach to its markets played a significant role here. PwC tackled a number of issues which were of particular relevance to its clients. This enabled the firm to win attractive new mandates, thus maintaining its market leadership.

PwC has tackled a number of issues which are of particular relevance to its clients.

In Switzerland, PwC has again set itself challenging targets for the financial year ahead. Attaining them will enable the firm to make further advances in all five key areas of its strategy:

- PwC Switzerland intends to develop its position as the leading provider of advisory and assurance services to small and medium-sized enterprises. SMEs often need support in financial statement preparation, succession planning and developing the international dimension of their business. Strategies for mitigating the effects of the strong Swiss franc are in particular demand.
- At the same time, PwC will further strengthen its ties to its key clients in industry and finance.
- PwC will push ahead with the transformation of its business model, standardising additional processes. Two objectives are paramount here – enhanced quality and greater efficiency.
- The firm will develop innovative advisory offerings aimed at capitalising on the trend towards digitalisation and the increasing use of social-media platforms.
- PwC Switzerland will intensify its collaboration with other firms in the PwC global network. The objective is to combine the expertise of its employees more effectively, particularly that of its specialists. This cooperation will extend to training and continuing education and will also involve the centralisation of specific services.
- In assurance, PwC is continuously raising the quality and reliability of its services. The firm is committed to a regulatory regime which is strictly focused on improving audit quality. PwC constantly strives to enhance the relevance of financial statement reporting and to narrow the gap between the expectations the public places on the assurance industry and the statutory requirements an audit must fulfil.

As before, PwC will continue to focus on its relationships with its clients and on those between its employees, thus creating value for both groups. Implementation of the PwC Experience programme, which focuses on behaviour as the key to enhancing the way in which services are delivered, will continue.

Urs Honegger, CEO, PwC Switzerland

Markus Neuhaus, Chairman of the Board of Directors of PwC Switzerland and Member of the Global Network Executive Team

Maximising market opportunities

Market segments and services with significant future potential are boosting revenues.

Whatever the sector in which they operate, all companies are confronted by the issues arising from the financial and debt crisis. From a business-policy point of view, the appreciation of the Swiss franc and new regulatory requirements are the most demanding challenges.

The main concern for the finance industry – apart from low interest rates – is the enactment of new regulations. The principal issues here are more stringent equity capital requirements, the “too big to fail” rules applying to systemically relevant institutions, the EU’s MiFID II directive and FATCA (Foreign Account Tax Compliance Act) legislation in the US. The preparatory arrangements required for FATCA not only cover tax-law issues, but also have multifaceted implications for business processes and IT. The integrated structure of PwC’s business and tax advisory services is a significant advantage in developing comprehensive solutions to the complex problems facing financial institutions as a result of the new regulatory requirements.

PwC will continue to focus on its relationships, creating value for its clients.

For the manufacturing sector, the key strategic focus is on transformation. Initiatives here are aimed at optimising business models, systematically analysing growth opportunities and reducing costs. For some companies, transformation amounts to nothing less than developing strategies for survival. Changing business conditions and cost pressures in saturated markets require new strategic initiatives. The digitalisation of business processes and communication via social-media platforms point the way forward. PwC is also seeing growing demand from companies for advisory services in the fields of human resources and risk management.

Besides the range of services it offers, another important aspect of PwC’s approach is its understanding of the various sectors which make up the market. In addition to the financial sector and the changes affecting it, a number of other Swiss industries are also experiencing a period of structural adjustment. Examples here include healthcare, energy and tourism, as well as manufacturing. From an international perspective, opportunities for providing additional advisory and assurance services are also emerging in the entertainment industry in its wider sense, including the organisation of large-scale cultural and sports events. There are also good prospects for growth in advisory work for international firms which either already have a headquarters office in Switzerland or are envisaging establishing one.

In order to assist its clients in their operations in other countries, PwC is expanding its network of country desks, which provide country-specific services in a number of locations. These are of particular benefit to small and medium-sized firms.

Expanding strategic capabilities

PwC is systematically aligning its skills with market requirements.

The continuous evolution of market conditions means that companies are constantly confronted with new issues to address. During its 2011–12 financial year, PwC made a number of targeted investments aimed at providing its employees with the expertise its clients require.

Business-transformation processes and the advent of new regulations in specific industries are placing substantial demands on consultants and auditors. That is why PwC is constantly engaged in adapting the skills profile of its employees to the changing needs of the marketplace. A particular challenge here is the search for professionals with detailed knowledge of specialised areas of business.

PwC is constantly adapting the skills profile of its employees to the changing needs of the marketplace.

Undeterred by market conditions, PwC continues to invest a good 10% of its gross service revenues in the training and education of its staff. In addition to its use of classical training programmes, the firm is increasingly deploying digital teaching methods. These enable PwC Switzerland to make greater use of training formats which have established themselves as standard across the firm's global network.

PwC Switzerland is notable for its highly developed talent-management capabilities. Its work in this area is based partly on a structured goal-setting process, derived from the firm's strategy and its business objectives, and partly on performance assessments, which combine quantitative metrics with a significant number of qualitative criteria. This is complemented by a rating of individual employees' future potential. PwC uses this forward-looking perspective in order to determine the talent-promotion initiatives appropriate to individual staff members in the context of its Key Talent programme.

Talent management is one of the four pillars on which PwC's human capital strategy is based. The strategy is designed to ensure that PwC always has sufficient sector-specific knowledge at its disposal and that its resources of technical expertise can meet the demands placed on its assurance and advisory services. PwC's human-capital strategy also guarantees that the firm always has an adequate number of potential successors for its key client-advisory and management posts. A further important objective of the firm's human-capital strategy is to ensure that PwC consistently remains the most attractive employer among professional-services firms.

Conveying the PwC Experience

PwC is the most respected brand in the professional services industry.

The PwC Experience is the most important element defining PwC's identity. It is central to the firm's corporate culture and quintessential to the PwC brand. The PwC Experience describes how PwC wishes to serve its clients. While its starting point is technical expertise, the PwC Experience is also aimed at enabling the firm to defferentiate itself through the way it interacts with its clients, its service delivery and the collaboration between its staff members.

In its 2011–12 financial year, PwC completed the implementation of its visual identity, a key component of its new brand presence. This new visual identity is expressed in the firm's new logo and corporate colour palette. This is complemented by a verbal identity which underscores the firm's brand promise. PwC intends to communicate in a clear, readily understandable fashion. That commitment to clear communication should be recognisable in every document the firm publishes and in all its correspondence.

PwC's brand strategy and its efforts to convey its corporate culture are proving successful. Within the firm, it is more and more common for employees to refer spontaneously to the PwC Experience. How well the essential message of the PwC Experience has become established is also reflected in the results of the People Engagement Index, a worldwide poll PwC conducts among its employees each year. Within the firm's global network, PwC Switzerland consistently achieves a prominent place in the employee-engagement rankings.

PwC has the strongest brand among the Big Four.

Testimony to PwC's external reputation is provided by the Brand Health Index (BHI). The BHI is an independent survey conducted every two years among existing and potential clients of professional-services firms. In the 2012 survey results for Switzerland, PwC not only came first, but also further increased its lead over its next-best-placed competitor. The worldwide results also place PwC in the number one slot, underscoring its position as the most respected of the Big Four professional-services firms.

PwC intends to be perceived as a professional-services firm whose intelligent, inspiring and helpful work in areas relevant to clients distinguishes it from the rest of the market. In order to consolidate this thought-leadership role, PwC regularly publishes work analysing topical trends. Among these publications, its *CEO Survey* and its *Economic Crime Survey* have already gained recognition as classics of their genre. At present, PwC is carrying out research on family-owned companies, the profound changes affecting the international financial-services market and the role of generations in the global workplace.

Ensuring quality

The quest for quality is an intellectual challenge.

Quality is fundamental to PwC's business. It is critical to the respect the PwC brand enjoys. There are three distinct dimensions to quality. The first is exemplified by immaculate performance, in the execution of work which is both technically correct and excellent by the standards of its particular discipline. The second lies in the application of this knowledge in the practical context of a client relationship. This can also been seen in the way PwC puts its sector-specific expertise into effect and leverages the collaborative potential of its global network.

The third dimension of quality is recognisable in the way services are delivered. It is along this axis that quality and the PwC Experience meet. Quality in this dimension means interacting with clients in such a way that they gain precisely the value they are looking for. That is the objective of the PwC Experience, and PwC staff should deliver it with pride, joy and inspiration. That is how PwC intends the quality of its work to stand out in the marketplace.

PwC is committed to a regulatory regime which is clearly focused on improving audit quality.

Quality is indispensable in the professional services market. One of the most effective ways of measuring it is in terms of client satisfaction. PwC is proud of the responses it receives from its regular client-experience surveys. Many clients have indicated that the work PwC has done for them has generated significant added value specifically for their firm. PwC is also ready to recognise scope for improvement and is grateful for suggestions which enable it continuously to improve the quality of its services. The ability to develop solutions tailored to specific client requirements is important, particularly in the current environment.

In assurance, PwC's own inspections, and those carried out by external oversight bodies, both show that the firm's work meets the highest quality standards. The principal requirements here are the independence, integrity and objectivity of the auditors themselves, as well as uniformity of audit methodology and a dialogue-based approach to reaching conclusions on matters requiring professional judgment. The key elements in PwC's decision-making culture are the professional scepticism of the individual auditor and leadership by example throughout the organisation's upper echelons.

Quality is not achieved solely by meeting standards. Indeed, it should not be viewed as something which is defined from the outside. Rather, the quest for quality is an intellectual challenge, one which can become a passion. It is a source of great pride to a consultant to know that he has achieved the best possible result for a client.

Transforming the business model

Improved margins and higher quality go hand in hand.

Industrial companies are not alone in having transformation on their agenda. It is also of strategic relevance for service firms. Nevertheless, the services industry is lagging behind the industrial sector as far as standardisation, automation and centralisation are concerned. Service firms, including PwC, have however acknowledged the need for transformation, recognising that it will help them to withstand margin pressure and ensure the level of profitability required to finance investments for the future.

Transformation is also of strategic relevance for service firms.

Efficiency gains are not the sole objective of business-model transformation, however. It also makes a vital contribution to quality assurance. Standardised, automated processes help to enhance service delivery. They allow better process monitoring, which in turn ensures quality. Business-model transformation encompasses all a company’s employees. Analysis of the individual steps in a process on the one hand and of the staff pyramid on the other makes it possible to achieve an ideal match between individual skills and specific tasks. This approach can be expected to enable firms to achieve further advances in both quality and efficiency.

The objective of transformation is to make firms more competitive. In a nutshell, this involves the firm rationalising its business model, concentrating on its core business and simplifying administrative tasks. It also means developing new products and services for customers. Indeed, business-model transformation can be a means of increasing a firm’s power to innovate. Conversely, innovation itself can drive transformation.

The challenge facing PwC’s business model is this: to fulfil client expectations with regard to pricing, while at the same time achieving the demanding quality standards which clients expect and which PwC expects of itself.

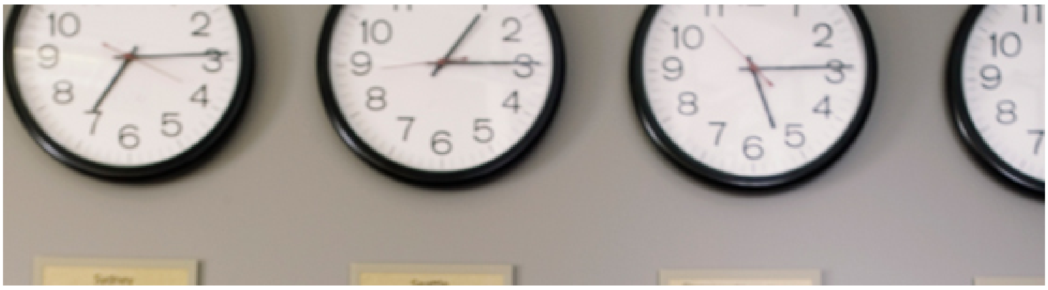
A finger on Switzerland's economic pulse

A debt crisis in Europe, diminishing purchasing power among major trading partners, dynamic growth in emerging markets and more stringent regulation throughout the world – just the sort of environment in which Switzerland needs favourable conditions for its economy. Six key issues are critical to how Switzerland positions itself as a place to do business:

- **Regulation**: the worldwide trend towards greater regulation is primarily, but not solely, directed towards the financial sector. Properly implemented, new regulation could even lend Switzerland a competitive edge.
- **Manufacturing**: Switzerland has a strong industrial base. A tradition of quality manufacturing is a hallmark of Swiss industry. The key to future success lies in research and development.
- **Innovation**: Switzerland's leading competitive position is due, first and foremost, to its ability to innovate. Innovation is not only essential to Swiss industry, it is also becoming increasingly critical to the country's service sector.
- **Finance**: the Swiss financial sector is under substantial pressure. This should not obscure the fact that Switzerland's banks are both stable and in sound financial health by international standards. Swiss insurers have even strengthened their market position.
- **Tax**: for international firms, Switzerland's tax regime is a strong argument when it comes to choosing a company domicile. Switzerland needs tax structures which maintain its attractiveness and are internationally recognised.
- **SMEs**: small and medium-sized enterprises employ two thirds of Switzerland's working population, as well as providing the majority of its apprenticeships. The most pressing challenges facing Swiss SMEs today are the strength of the Swiss franc and the scarcity of specialised staff

The pages that follow describe PwC's thinking on these key issues.

Markus Neuhaus on regulation



What is your assessment of the current wave of regulation?

After years of liberalisation, we have now entered a phase of greater regulatory stringency. There are several reasons for this. First, it reflects the currently dominant political dogma. Politicians want the electorate to see that they are actively engaged in shaping the economy. Second, regulators themselves want to exert influence on the financial markets. Of course, we should not forget that regulation is also a reaction to failure, and there has been quite a lot of that in recent years.

Has enough yet been done to regulate financial markets?

A lot has already happened, and much is still in a state of flux. I think the overall direction is correct, although one can – and indeed should – argue about individual aspects. We do, however, need to recognise that industry practice in fact already observes many of the changes that have been proposed. Banks' balance sheets, for example, are significantly less stretched than they were. Some new regulations, such as the Foreign Account Tax Compliance Act (FATCA), are however clearly going much further than is necessary.

"Industry practice already observes many of the changes proposed."

Markus Neuhaus, Chairman of the Board of Directors of PwC Switzerland

What are your views on the planned capital adequacy requirements and the regulation of systematically relevant banks?

Higher levels of required equity capital are right in principle. The development of the Basel III framework, which not only prescribes significantly more equity but also requires it to be of a higher quality, has made considerable progress internationally. These new rules should be implemented on a consistent basis worldwide. Were any of the world's important financial centres to allow any significant deviation from these standards, this would expose financial-market stability to substantial risks, because it would undermine the reliability of the entire system. Switzerland has played a pioneering role with its "too big to fail" directive for regulating systemically relevant institutions. Properly implemented, this directive could provide the Swiss financial marketplace with a significant competitive advantage, which would benefit the wider Swiss economy. While it is true that the anti-cyclical capital buffer system has not yet been put to the test, it would appear to provide appropriate, and timely, safeguards against overheating in the credit and real-estate markets.

Are the demarcations between politicians or legislators on the one hand, and regulators, supervisory authorities and other players on the other hand clearly defined?

Because of their oversight mandate, supervisory authorities can also impose regulations themselves – within the scope allowed them by legislators, of course. The scale of the financial crisis demonstrated that there were major inadequacies in the entire system. Markets failed and the state also failed. None of the players involved had a clear overview of all the risks which caused the crisis. It was caused by the risky business practices of certain banks, but it was also caused by the political decisions made at the time. Other market participants were affected by the crisis. Auditors belong to this second category. The audits they carried out were conducted in accordance with the rules. This does, however, raise the question of how relevant financial-statement reporting – and thus, by extension, audit practice – actually is, when they were unable to recognise or prevent these kinds of risks and the crisis they brought in their wake. This is an issue that the assurance industry, and PwC in particular, takes extremely seriously.

What direction should the future development of the assurance industry take in order to raise the quality of audits?

Financial statements and audits will continue to focus mainly on the past, but this perspective will be complemented by new elements. Investors and other stakeholders are demanding additional relevant information on which to base their decisions. Given this, the entire process of financial-statement reporting – including the audit process – needs to be revised. One critical aspect is the nature of the various relationships between companies, auditors, investors, regulators and other interested parties. It is also a matter of what backward-looking and forward-looking information is required by whom, and of how and in what form this information should be communicated. A further significant aspect relates to the type of external audit which is best suited to contributing to ensure the safety of the financial system. These are questions that are only beginning to be answered, and their ultimate resolution will require agreement among all stakeholders involved.

Does regulation promote structural reforms or obstruct them?

Regulation can both accelerate and slow down reform. It is a necessary means of inspiring confidence among major stakeholders. It can have a stimulative effect and it can also help to balance opposing forces. There are, however, industries in which the primary function of regulation is to preserve existing structures. From a liberal, market-economy perspective that is somewhat questionable.

Weiterführende Informationen

- PwC Global: Our points of view on audit and regulatory affairs

Urs Honegger on Swiss industry

How important is Switzerland as a manufacturing centre?

The secondary sector, industry, generates some 23% of GDP. Swiss manufacturing – especially in the field of quality products, where it has a long tradition – has helped Switzerland achieve an enviable worldwide reputation. Across the globe, the "Swiss made" label is associated with attributes such as precision, durability and technical excellence. Exports by Switzerland's pharmaceutical, machine-tool, electrical and watch industries – to cite the most obvious examples – contribute significantly to the added value generated by the Swiss economy. They are also a key element in Switzerland's positive overall image abroad.

Are Switzerland's financial and manufacturing sectors still in balance?

The financial sector is obviously in the spotlight now, yet manufacturing is the foundation of Switzerland's economy. We need both, a functioning financial sector and a strong manufacturing base. The two should not be played off against each other. Swiss manufacturing benefits from the country's sound financial system, but it is also a counterweight to the service sector. Industry attracts research, development and teaching. A weak manufacturing sector would have devastating consequences. It would deprive the economy of its foundations. Key skills would be lost. This would severely impinge on Switzerland's ability to innovate.

"Manufacturing is the foundation of Switzerland's economy."

Urs Honegger, CEO, PwC Switzerland

What are the arguments in favour of concentrating core activities – particularly research and development – in Switzerland?

Few countries in the world can match Switzerland's capacity to innovate. We have outstanding universities and universities of applied sciences which ideally support and foster those capabilities. Switzerland is also an attractive place for scientists and researchers from other countries to work. They, too, benefit from all the economic and other advantages that Switzerland has to offer. Switzerland also has a stable legal framework. This is beneficial in several ways, not least with regard to patent protection.

More and more manufacturing capacity is being moved to Eastern Europe and Asia. Can this be halted?

Although there are some outstanding Swiss firms which demonstrate that they can manufacture better in Switzerland than elsewehre, this is a trend which seems very hard to stop. At the moment, it is being exacerbated by the cost pressures that the strength of the Swiss franc is further intensifying. I am, however, convinced that there is one approach which will not work. You cannot move all your manufacturing abroad and just keep your research and development in Switzerland. If you do, sooner or later, your research and development will follow your manufacturing. That is why it is essential for Switzerland to keep key components of its manufacturing here – something it can achieve only with the right environment.

What environment does manufacturing need?

The environment Switzerland has to offer is favourable. Industrial relations are harmonious. Labour market structures are not rigid. This is illustrated by the flexible working-time models and shorter working weeks which helped to save many jobs during the crisis. Switzerland also has a stable financial system, low interest rates and a favourable tax environment for companies. There is, however, a shortage of employees with specialised skills. Action needs to be taken to address that. The prohibition of research in specific, politically sensitive fields also has a major adverse effect on manufacturing.

What can the politicians do?

Politicians should develop Switzerland's dual-pathway professional training regime and promote the apprenticeship system. Politicians and the business community need to make a career as a specialist technician or an engineer more attractive to young people. For industrial companies, a number of other important actions are needed. The main ones are reducing the burden of administrative work, keeping taxes and other charges competitive, and indirect payroll costs low. It is also essential that the existing rules on the free movement of people are maintained, so that Switzerland can continue to attract qualified specialists. Politicians should also help companies gain wider access to world markets, by, for example, establishing free-trade agreements with developing countries. In general, restrictions on entrepreneurial freedom should be avoided.

And what can the companies themselves do?

Companies should ensure that their business-model transformation processes take account of all aspects of operating in a particular country. Quality, security, stability and peaceful industrial relations are all major advantages that Switzerland offers and they help to ensure very high levels of productivity. When assessing a country as a place to do business, attention should be paid not only to its current exchange-rate and cost structures, but also, in particular, to its medium- and long-term productivity and output performance. A focus on future innovation capabilities is especially important in this regard.

Stefan Gerber on SMEs

How important are small and medium-sized enterprises (SMEs) for Switzerland's economy?

The figures alone illustrate just how important SMEs are for the Swiss economy. There are some 313 000 companies in Switzerland, more than 311 700 of which the statisticians classify as SMEs. That is over 99%. SMEs account for two thirds of all jobs in Switzerland and they provide the lion's share of the country's apprenticeships. SMEs are a fertile environment for the development of entrepreneurs, particularly those who choose not to go to university after leaving school. SMEs cannot source all the staff they need in Switzerland alone. We need to be able to recruit from abroad, particularly in specialised areas of expertise.

What are the challenges facing SMEs today?

The majority of SMEs are family-run businesses. They generally have simple management structures and flat hierarchies, but relatively undeveloped internal-control systems. The link between the personal and the work-related can be problematical. When the two are fused, it is easy for conflicts of interest to occur. Family-run companies need institutionalised conflict-resolution mechanisms, such as contracts between the shareholders which clearly state their rights and obligations to each other, particularly with regard to the sale and purchase of shares. These contracts can also govern the question of succession, a major challenge for many family-run companies. Succession arrangements serve to ensure the company's sustainability. A key issue they need to address is whether an internal or an external succession provides the better solution.

"Entrepreneurs need to incorporate scenarios into their planning."

Stefan Gerber, Swiss SME Industry leader

What issues are of most pressing concern to SMEs?

Right now, the strong Swiss franc is obviously a concern. Other issues include ensuring sustainable growth – which also requires SMEs to find sufficient numbers of qualified specialists –, internationalisation, the ever-increasing volume of regulation and the development of innovation capabilities.

Why should SMEs set their sights on the international arena?

Because that is how they can access new markets. They can also become more competitive by extending their product distribution to international markets, or shifting some of their production to locations which offer strategic advantages. Many companies have also made a conscious decision to follow their customers into new markets. Proximity to the customer is an important factor in the success of any company, irrespective of where that customer is based. Establishing local branches abroad helps a firm to operate more effectively in the markets concerned. Furthermore, internationalisation not only helps a firm to expand beyond a relatively limited customer base in Switzerland, it also helps it to diversify its risks, since it is rare for all world markets to be equally weak simultaneously. By focusing on one market, a firm is in danger of becoming too dependent on it, and that includes its dependence on suppliers. This is also a reason why it can be important to engage in purchasing in other currency areas.

What should SMEs particularly heed when they expand into other cultural environments?

Any firm wishing to expand into Asia, Latin America – or indeed even Eastern Europe – needs to acquaint itself with the business practices of the country concerned. Language barriers, inadequate logistics and the lack of contract enforceability are all potentially substantive reasons for not expanding into emerging markets.

How important are start-ups for the economy's ability to innovate?

Start-ups have an important role to play here, especially in Switzerland. Their ideas and enthusiasm are a breath of fresh air for Swiss industry.

How can SMEs best equip themselves to face the future?

The business environment is constantly evolving. That is why SMEs need to develop alternative scenarios, which they should review regularly. In order to ensure sustained business operations, companies need to consider at least three or four alternative strategic scenarios. By taking this approach, SMEs can keep on top of events, rather than being overwhelmed by them.

Wolfgang Rieder on innovation hubs

What are the hallmarks of an innovative company?

Innovation is not the result of a sudden inspiration. Of course, it can happen that insights are gained as a bolt from the blue, but that is not something a firm can count on. Rather, innovation is achieved through a conscious effort to incorporate innovative ideas and designs into a company's business processes. This enables them to fuel growth.

How would you assess Switzerland's merits as a place for innovative firms to do business?

Switzerland is the world's leading innovation hub. In 2012, it was again ranked number one in the Global Innovation Index. In that same ranking, Switzerland also achieved excellent results in all four subindices. Switzerland generates an extraordinarily large number of innovations, particularly given the country's size. This is reflected in indicators such as the number of patent applications filed or research papers published. Switzerland's leading position can also be attributed to the quality of its research institutes and the close ties between academia and business.

"Innovation fuels growth."

Wolfgang Rieder, Leader, Advisory, Member of the Management Board

Which sectors are driving innovation forward?

Traditionally, these have been companies with large research and development budgets. This is the picture we find in the pharmaceuticals and consumer-goods industries as well as in the mechanical and electrical-engineering sector, whose firms are represented by Swissmem. These are sectors which have the resources and structured processes which foster innovation, and it is to them that Switzerland owes its reputation as an innovation hub. Yet that alone is not enough. Every company that wants to get ahead needs to innovate.

And that applies to the services sector, too?

Certainly. The question here is how the processes used in manufacturing can be transferred to the services sector. There are examples from the financial sector which demonstrate that this can be done. Benchmark analysis has also been carried out indicating that innovation can help a bank raise its pre-tax earnings by between 8% and 54%, depending on how well developed its innovation processes are. The ultimate goal of innovation for a company, irrespective of the sector in which it operates, is to use new and improved services to reach its business objectives. Innovation needs to be a component of a company's strategy, its business model and its operational activities.

What conclusions should PwC draw from this?

In all our activities involving advisory services and problem solving, we need to develop innovative services. One area where this can be achieved is in our use of digital technologies in their widest sense. Platforms already exist on which companies can ask specific, targeted questions. In the UK, PwC is in fact already testing a platform of this kind, which of course is being used in a closed environment at this stage. By harnessing the expert knowledge we have in our network, this is another way in which we will help our clients meet the challenges posed by innovation. We also intend to investigate the scope for crowd-sourcing solutions. Universities and other institutions accumulating knowledge could also be granted access to a platform of this kind.

Are there not inherent security problems in the use of platforms and crowd sourcing?

IT security issues can be resolved. Indeed we have already gained considerable experience in this area through our use of internal social-media platforms. In fact, questions relating to the reliability of the solutions proposed on these platforms are much harder to resolve than technical security issues. Who, for example, is liable if an incorrect or outdated answer is posted? There are still many unresolved legal issues in this area.

Surely other industries have considered how new media should be used correctly?

Financial institutions are actively engaged in examining the issues surrounding the use of new media, particularly with regard to client access, new services and pricing. Platforms provide banks with an effective and innovative tool for improving the client-advisory process, since they also enable customers to consult investment advisors online. That does however give rise to new questions, such as the extent to which the bank has committed itself with the investment advice it has given and what compliance guidelines should govern that advice.

Peter Ochsner on Switzerland’s financial sector

What is your current assessment of Switzerland's financial sector?

The individual areas of the financial sector need to be considered separately. The circumstances affecting banks, insurers, and other financial-services providers – such as independent wealth managers or institutional investment managers – are all different and each group has a different set of challenges to face. Swiss banks, compared to those in other countries, are stable and in good financial health. The uncertain economic outlook and their clients’ diminished risk appetite have however reduced banks’ transaction volumes. There is a trend towards investment in secure, low-yield products. This is squeezing bank revenues and margins. Then there is the debate about the future of the wealth-management business in Switzerland. Insurance companies have mastered the financial crisis well and have emerged from it stronger. Over the last few years, many insurers have achieved notable success in developing their market presence, particularly beyond Switzerland’s borders.

What is the future of private banking in Switzerland?

There has been a paradigm shift in private banking. Worldwide opinion has undergone massive changes as far as transparency and tax matters are concerned. Practices which were acceptable ten years ago are no longer tolerated today. A key task now is to deal with the legacy issues. Solutions here will, however, necessarily involve an outflow of client funds, which will reduce banks’ earning capacity. This in turn will mean that business models will either have to be consolidated or redrawn from scratch.

“Tax conformity is the right strategy.”

Peter Ochsner, Leader, Assurance, Member of the Management Board

What happens then?

The next priority will be to make the most of the advantages Switzerland has to offer. This can be achieved through an emphasis on service quality, international wealth-management experience or indeed investment performance. The argument that Switzerland is a safe haven is also relevant in this context. The tax-conformity strategy that Swiss banks have now been pursuing for more than two years is right.

Will this allow Switzerland's financial sector to regain international reputation?

Switzerland still has a good name abroad. What is essential for its reputation now is that the legacy issues are resolved. Currently, Switzerland is trying to achieve this through withholding-tax agreements concluded with a number of other countries. Their purpose is to regularise the status of previously untaxed assets and to introduce a withholding tax on future income and capital gains. Agreements of this kind make it possible for national tax authorities to have their tax demands met. Unlike automatic exchange-of-information arrangements, these agreements also enable client privacy to be maintained.

What are the disadvantages of the withholding-tax agreements for the banks?

Implementation of these agreements will involve substantial administrative costs. It will also result in an outflow of assets to tax authorities abroad. The requirements placed on compliance will increase, and preparations have to be made for this, as indeed they also must to ensure adherence to US legislation, particularly FATCA. The expense involved in putting all the necessary processes and systems in place is considerable. Banks' costs will therefore rise and their margins will be further eroded. As a result, they will either resize or develop new business models

What are the challenges facing insurers?

I think it is important for the insurance industry to maintain the environment within which it currently operates, which is relatively favourable in international terms. The stability of Switzerland's financial sector and the high reputation it continues to enjoy abroad provide a sound basis for Swiss insurers to continue to operate successfully in the future. In life insurance, today's low interest rates and yields are a major challenge when it comes to acquiring new business or delivering on contractually agreed return rates. Furthermore, the insurance industry is also becoming subject to tighter regulation, as the EU's Solvency II directive or the Swiss Solvency Test demonstrate. The US FATCA legislation affects all financial institutions, including insurance companies. The resulting rise in compliance costs is contributing significantly to the upward pressure on overall costs.

Andreas Staubli on Switzerland as a tax location

What is your current assessment of Switzerland as a tax location?

Switzerland as a place for doing business is under pressure from several fronts. The strength of the currency has made it a relatively expensive location for companies to work. That is not only bad for firms setting up operations here, but also for multinationals who already have a Swiss presence. In order to operate more cost-effectively, they need to transfer specific functions back out of the country. That in turn means that there is a danger that fewer and fewer business activities will be carried out in Switzerland. It is expensive for companies to appoint expatriates to management positions here, because the strength of the Swiss franc adds to the burden of housing rental costs, which companies often pay themselves, and because of Switzerland's relatively high personal income-tax and social-security contribution rates.

Are there other adverse factors?

There is an element of uncertainty with regard to tax legislation, partly due to the tax dispute with the EU and partly as a result of domestic issues, such as those arising from the fact that the principles governing the tax treatment of capital investment, which are a key component of Switzerland's recently enacted second round of corporate-tax reform (in German, "Unternehmenssteuerreform II"), are again being called into question. When legislation is revised shortly after it comes into force, this is hardly conducive to inspiring trust in a country's institutions. That trust is a precious asset. Indeed, one of the most important arguments in the current global competition between countries as locations for doing business is that of legal certainty. Were the principles governing capital investment to be curtailed or abolished, this would be a disadvantage for Switzerland.

"Switzerland must maintain its tax sovereignty."

Andreas Staubli, Leader, Tax and Legal Services, Member of the Management Board

The tax regimes various cantons apply to corporate taxation currently favour Switzerland as a tax location. Will this change?

This is a taxation issue about which Switzerland and the EU have been arguing for years. The EU 's case is that Switzerland grants unjustified tax concessions to certain types of corporate entities, such as holdings, so-called mixed companies and domiciliary companies. The EU would like Switzerland to make itself subject to its 1997 internal Code of Conduct on Business Taxation. Were that to happen, it would mean that the EU could institute proceedings against Switzerland's tax regimes. If Switzerland wishes to maintain its tax sovereignty, it should certainly not become a signatory to this EU code. Switzerland will, however, have to alter some elements of the cantonal tax regimes currently in force, in order to ensure that domestic and foreign revenues and business activities are treated equally. Alongside this, Switzerland will need to develop new and attractive rules governing the taxation of certain group company functions and the treatment of intangible assets in their widest sense in order to remain an attractive tax location.

Switzerland is also attracting criticism for its treatment of undeclared private wealth. How do you think this can be solved?

This tax dispute is detrimental to Switzerland’s image. It would be good if the issue of untaxed wealth were resolved soon. The withholding-tax solution is a good way of regularising untaxed assets and dealing with the legacy issues they entail. Agreements like those Switzerland has negotiated with the United Kingdom, Germany and Austria maintain individual confidentiality while permitting information to be exchanged under precisely defined circumstances. These agreements also ensure that the income they cover is taxed, which makes them highly efficient for the countries that have entered into them. I believe that the Swiss government’s objective of negotiating withholding-tax agreements for individuals, not only with EU member states but with countries worldwide, is absolutely right. Automatic exchange of information would involve substantial amounts of work, generate huge, often futile, quantities of data, and ultimately benefit nobody. Switzerland’s future as a financial centre is based on managing assets which are subject to taxation. The key criteria for achieving this are quality and security.

Risk management

PwC's enterprise-wide risk management structures are designed to protect the firm from risks which could potentially jeopardise its business success or its reputation. Their objective is to prevent negative surprises and to ensure that levels of risk awareness are continuously raised throughout the entire organisation. The principal means of achieving this are:

- identifying risks and putting processes in place which prevent them from occurring;
- ensuring that everyone working at the firm complies with its risk policy, the law, regulatory requirements and the global PwC network's risk standards;
- coordinating all risk-management activities across all business areas and with other firms in the PwC network.

PwC Switzerland systematically evaluates its key risks with regard to talent, the market and the firm.

At PwC Switzerland, the Management Board and the Extended Management Board share responsibility for strategic and operational risk management. The Extended Management Board's principal task is to ensure service quality and adherence to regulatory requirements. The Risk Management Committee, chaired by the firm's Risk Management Partner, is tasked with preparatory duties. It deals with the strategic, conceptual and organisational aspects of the firm's risk policy. In addition to the Assurance Risk Management Partner and the Assurance Chief Quality Officer, this committee also comprises the Chairman of the Board of Directors, the CEO and the General Counsel.

In addition, every business unit has a designated partner responsible for risk-management activities in the business areas concerned. Working in conjunction with the head of the business unit concerned, he or she formulates directives on quality assurance and the management of individual risks. In his role as Risk Management Partner for PwC Switzerland as a whole, the General Counsel coordinates the activities of the Risk Management Partners in the individual business units.

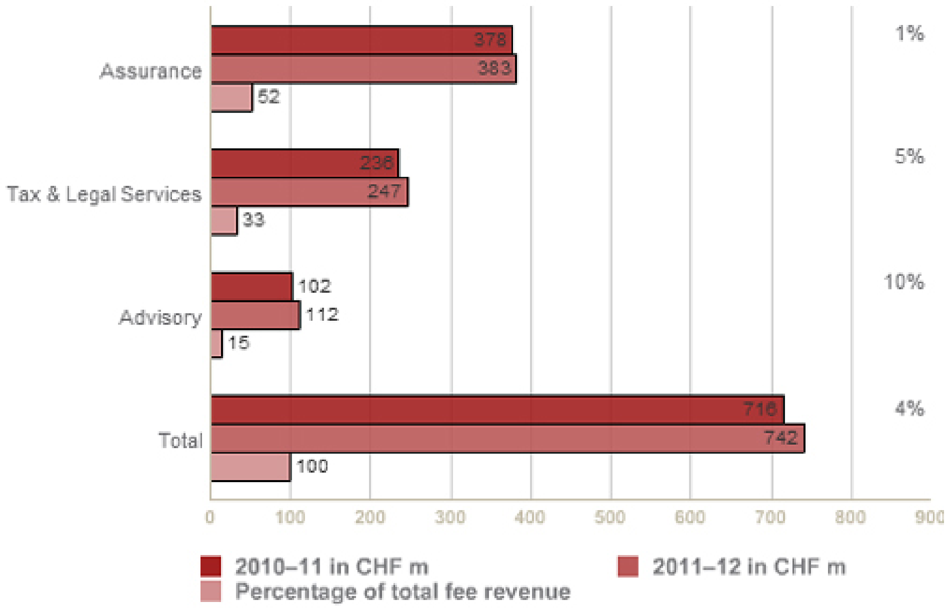
Minimum risk-management standards are defined by PwC's global network. For many years, PwC Switzerland has operated a risk-management system which goes beyond these standards. The system is regularly reviewed and is being improved continuously. PwC maintains a risk register which systematically identifies and measures some 30 key risks in the areas of talent, the market and the firm.

Performance

Economic conditions remain difficult, and market sentiment is characterised by uncertainty. Despite these challenges, PwC's strategy paid off. Gross fee revenues at PwC Switzerland were 26 million CHF higher in 2011-12 than in the previous financial year, an increase of 4%.

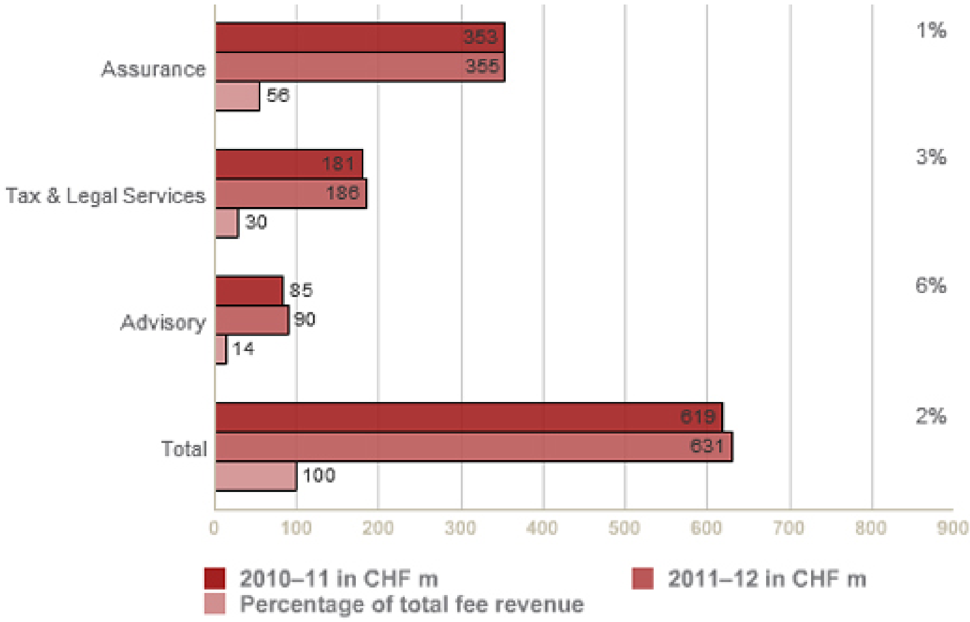
Gross fee revenues by line of service

The firm's aggregate gross fee revenues for 2011–12 amounted to 742 million CHF in 2011–12, 26 million CHF, or 4%, higher than in the previous financial year. This gross figure includes 100 million CHF (86 million CHF in 2010/11) of fees earned by partners and employees of other PwC firms from their work on PwC Switzerland mandates. Gross fee income also includes PwC expenses invoiced to clients.



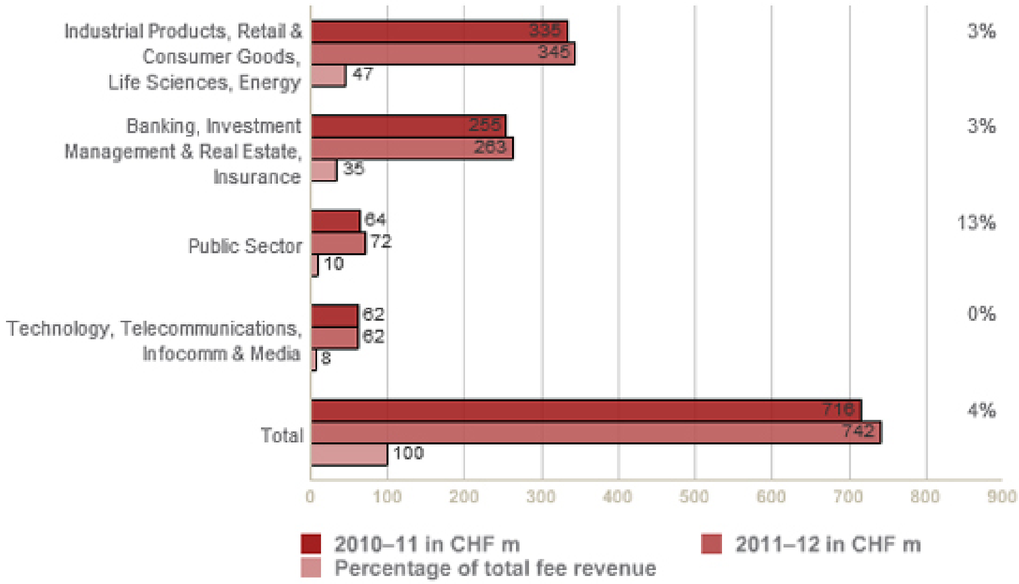
Net fee revenues by line of service

PwC Switzerland's total net fee revenues rose 12 million CHF, or 2%, to 631 million CHF. This figure represents the fees generated by PwC Switzerland itself, net of fees for services provided by other PwC firms and of expenses invoiced to clients.



Results by industry group

PwC Switzerland raised its gross fee revenues in all industry groups with the exception of the Technology, Telecommunications, Media & Entertainment sector, where they remained unchanged on their 2010/11 level. As the composition of these industry groups has been modified since last year, the prior-year figures have been adjusted to make them comparable. PwC Switzerland generates one third of its fee revenues from its work with SMEs.



Headcount

At June 30, 2012, PwC Switzerland had a total of 2,768 employees, 12 fewer than a year earlier. These figures relate to the actual number of employees. They are not stated on a full-time equivalent basis.