

Notes to the Consolidated Financial Statements

1. GENERAL

Ernst & Young Switzerland comprises ATAG Ernst & Young Holding AG, Basel (hereinafter "Holding") and its subsidiaries. The Group operates in the fields of Auditing and Advisory services. The holding company's capital is wholly owned by the Partners of Ernst & Young Switzerland through the ATAG Ernst & Young Partner pool.

2. ACCOUNTING PRINCIPLES

General

The consolidated financial statements have been prepared in conformity with all the accounting and reporting recommendations in Switzerland (Swiss GAAP ARR) and present a true and fair view of the company's financial position and results of operations. The accounts have been prepared on the basis of historic cost and the general guidelines on accounting and valuation contained in Swiss GAAP ARR. The significant accounting principles are summarized below.

Scope of consolidation

The consolidated financial statements include all companies controlled by the Holding Company through a majority of the votes or by other means.

Other companies in which the holding company has an interest of between 20% and 50% and which are not otherwise controlled are designated as associated companies and included in the consolidated accounts in proportion to the share of equity held. A list of subsidiaries and associated companies is contained in note 21. No changes to the scope of consolidation occurred during the current business year.

Consolidation method

The capital is consolidated using the purchase method, according to which the purchase price of a subsidiary is set off against the Group's share of the revalued equity capital (fair value of net assets) at the time of acquisition. The difference constitutes goodwill, which is capitalized and amortized via charges to the income statement.

Eliminations

Intra-Group receivables and liabilities, income and expenses have been eliminated. Intra-Group profits on transactions have been eliminated in the income statement.

Revenue recognition

Revenues from Audit and Advisory services are recognized at the time the services are rendered. Services not yet invoiced are carried at their estimated net realizable value. Advance payments by clients for future services are accrued as liabilities. Client-advanced expenses are shown gross, i.e. are recognized with the same amount in fee income and other operating expenses. Services performed and invoiced abroad by foreign Ernst & Young companies for clients of Ernst & Young Switzerland are not included in fee income.

Taxes

The expected current income taxes on the profits of the individual Group companies in the reporting year are fully accrued. Capital taxes are recognized under other operating expenses. Deferred income tax is calculated for all timing differences between the tax bases of assets and liabilities (in the statutory and tax balance sheets) of the individual Group companies and their carrying values in the consolidated financial statements. Full provision is made for such taxes at the current tax rate. Deferred tax assets relating to tax loss carry-forwards of individual Group companies are only recognized if these are likely to be realized.

Tax expense includes the income taxes owed for the reporting period as well as the net change in deferred income tax positions.

Cash and cash equivalents

Liquid funds, consisting of cash in hand, postal accounts, bank accounts and short-term deposits with banks with a maturity or residual maturity of less than 3 months are carried in the balance sheet at their nominal value.

The cash flow statement reconciles the change in cash and cash equivalents.

Accounts receivable

The risks in accounts receivable are provided for by means of appropriate specific and general allowances. Specific allowances are made on the basis of known or expected losses on individual receivables. General allowances are calculated on the basis of the maturity structure of outstanding receivables on the balance sheet date. The allowance rates applied are based on the experience of past years.

Work in progress

Work in progress (services not yet billed) is valued using the percentage of completion method (POC). The valuation is based on the proportion of work performed plus expected costs to complete in relation to the expected income. A proportional share of profit is recognized where it can be assumed with sufficient certainty that it will actually be realized. A general allowance for identifiable losses is made based on rates derived from past experience.

Property, plant and equipment

Property, plant and equipment is recognized in the balance sheet at cost less cumulative depreciation. Cost includes all purchase or production costs incurred until such time as the asset is ready for use. Interest expense is not capitalized. Assets under construction include planning and project expenses in connection with the construction of the new offices in Zurich. Cumulative depreciation includes straight-line depreciation of the cost value over the asset's estimated useful life plus impairment charges in exceptional circumstances.

The following useful lives are assumed:

- ▶ Fixtures and fittings in rented premises:
based on the length of the lease, max. 10 years
- ▶ Office equipment: 5 to 10 years
- ▶ IT hardware: 3 to 5 years

Intangible assets

Intangible assets are carried in the balance sheet at cost less cumulative depreciation. Cost includes all purchase or production costs incurred until such time as the asset is ready for use. Interest expense is not capitalized. Cumulative depreciation includes straight-line depreciation of the purchase value over the asset's estimated useful life plus impairment charges in exceptional circumstances. Expenses for internally generated intangible assets are capitalized if the long-term benefit to the company can be measured and the related costs clearly segregated.

The expected useful life of IT software is between 2 and 4 years.

Financial assets

Financial assets are carried in the balance sheet at cost less cumulative valuation allowances. Allowances are made on the basis of individual valuations and the expected loss in value.

Liabilities

Accounts payable and other liabilities are carried in the balance sheet at their nominal values at the date of invoice.

Accrued expenses and deferred income

Accrued expenses and deferred income serve to ensure that revenue and expense are recognized in the appropriate period. They comprise primarily accruals/deferrals for variable salaries, taxes payable and other operating expenses.

Provisions

Provisions are established where a past event triggers a legal or factual liability towards a third party in an amount that is not certain but can be estimated.

Employee Benefit Plans

Employees of Ernst & Young Switzerland are insured with the ATAG Treuhand Pension Fund (hereinafter referred to as "the Pension Fund") for old age, disability and death benefits. The pension plan is a contributory scheme to which both employees and the employer contribute specific amounts. The employer's contributions are recognized in the income statement in the period in which they became due.

An assessment is made every year as to whether an economic benefit or an economic obligation arises from the pension plan. This assessment is made on the basis of the annual financial statements of the Pension Fund, drawn up in accordance with Swiss GAAP ARR 26 as at December 31 of each year. Significant changes up to and including the June 30 balance sheet date are taken into account where necessary. Changes in the economic benefit or economic obligation versus the preceding period are recognized under personnel expense.

Related party transactions

Related parties comprise the Partner pool of ATAG Ernst & Young (shareholders), the members of the Board of Directors of the Holding company, the Management Committee and the Pension Fund. Transactions with related parties are executed at arm's length.

Derivative financial instruments

Derivative financial instruments are used to hedge currency and interest rate risks. They are valued in the same way as the underlying transaction and are recognized in profit and loss upon realization.

in CHF 1,000

3. FEE INCOME	2007/2008	2006/2007	Change (%)
Fee income by segments			
Audit Services	313,080	309,311	1.2
Advisory Services	69,604	62,701	11.0
Tax and Legal Services	159,916	134,862	18.6
Accounting Services	19,950	20,163	- 1.1
Total fee income by segments	562,550	527,037	6.7

Fee income derives principally from Switzerland.

4. PERSONNEL EXPENSE	2007/2008	2006/2007
Wages and salaries	315,900	288.172
Social insurance expense	52,628	49.636
Other personnel expense	19,829	20.778
Total personnel expense	388,357	358.586

5. OCCUPANCY EXPENSE	2007/2008	2006/2007
Rental expense for business premises	18,857	18.080
Other occupancy expense	5,173	5.217
Total occupancy expense	24,030	23.297

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6. OTHER OPERATING EXPENSE	2007/2008	2006/2007
Administrative expense	67,848	62,915
Other operating expenses	67,731	71,229
Total other services operating expenses	135,579	134,144

Administrative expense includes costs of information technology, telecommunications, marketing, travel expenses, membership fees of professional bodies, contributions to EY Global and expenses related to professional risks. Other operating expenses comprise general costs and expenses billable to clients.

7. FINANCIAL RESULT	2007/2008	2006/2007
Financial income		
Interest income	1,949	1,309
Other financial income	41	4,300
Total financial income	1,990	5,609
Financial expense		
Interest expense	227	331
Other financial expense	2,627	29
Total financial expense	2,854	360
Total financial result	-864	5,249

8. INCOME TAXES	2007/2008	2006/2007
Deferred income tax	15	15
Current income tax	1,253	938
Total income taxes	1,268	953

There are no loss carry-forwards at individual Group companies that could be capitalized.

in CHF 1,000

9. CASH AND CASH EQUIVALENTS	30.06.2008	30.06.2007
Cash, balances in bank and postal accounts	83,020	84,164
Total cash and cash equivalents	83,020	84,164

10. ACCOUNTS RECEIVABLE	30.06.2008	30.06.2007
Accounts receivable	95,170	89,816
Allowance for doubtful accounts	-2,341	-2,627
Total accounts receivable	92,829	87,189

11. OTHER RECEIVABLES	30.06.2008	30.06.2007
Receivable from related parties	3,000	1,200
Other	40,620	24,821
Total other receivables	43,620	26,021

12. WORK IN PROGRESS	30.06.2008	30.06.2007
Work in progress	29,276	32,900
Allowance for unbillable fees	-2,223	-2,255
	27,053	30,645
Less advance payments from clients	-11,554	-18,241
Total work in progress	15,499	12,404

in CHF 1,000

13. PROPERTY PLANT AND EQUIPMENT	Furniture	Fixtures and fittings	Assets under construction	IT Hardware	Total
Historical cost					
At July 1, 2007	10,547	21,426	0	12,258	44,231
Additions	47	193	2,104	3,005	5,349
Disposals ¹	-2,927	-144	0	-5,022	-8,093
At June 30, 2008	7,667	21,475	2,104	10,241	41,487
Cumulative depreciation					
At July 1, 2007	-8,539	-12,660	0	-8,025	-29,224
Additions	-878	-2,432	0	-3,477	-6,787
Disposals ¹	2,731	144	0	4,880	7,755
At June 30, 2008	-6,686	-14,948	0	-6,622	-28,256
Net book value					
At July 1, 2007	2,008	8,766	0	4,233	15,007
At June 30, 2008	981	6,527	2,104	3,619	13,231

¹ In the course of the reporting year, assets no longer used and fully written off in the amount of CHF 6,808,000 (prior year CHF 4,566,000) were eliminated from the accounts. The fire insurance value at June 30, 2008 was approx. CHF 60.3 million (prior year CHF 60.3 million).

in CHF 1,000

14. INTANGIBLE ASSETS	Software
Historical cost	
At July 1, 2007	1,722
Additions	0
Disposals ¹	-597
At June 30, 2008	1,125
Cumulative depreciation	
At July 1, 2007	-554
Additions	-1,124
Disposals ¹	597
At June 30, 2008	-1,081
Net book value	
At July 1, 2007	1,168
At June 30, 2008	44

¹ In the course of the reporting year, assets no longer used and fully written off in the amount of CHF 597,000 (prior year CHF 1,420,000) were eliminated from the accounts.

15. FINANCIAL ASSETS	30.06.2008	30.06.2007
Loans	5,000	5,000
Cumulative allowances	-5,000	-5,000
Total financial assets	0	0

The subordinated loan has been in existence since the 2002/2003 financial year, and is fully written down.

in CHF 1,000

16. FINANCIAL LIABILITIES	30.06.2008	30.06.2007
Financial liabilities	6,000	7,000

The fixed advance totaling CHF 10 million comprises four tranches of CHF 1 million each and one of CHF 6 million. CHF 1 million is due for repayment at the end of each calendar year from 2004 through 2007 and CHF 6 million at the end of June 2009 (interest rates between 1.82% and 3.4% fixed for the term of the loan).

17. PROVISIONS	Deferred income taxes	Other provisions	Provision for pension liabilities	Total
At July 1, 2007	15	16,225	1,600	17,840
Allocation to provisions	15	3,350	321	3,686
Utilization of provisions	0	-1,681	-355	-2,036
Release	0	-2,328	0	-2,328
At June 30, 2008	30	15,566	1,566	17,162
Of which short-term:				
At July 1, 2007	0	852	224	1,076
At June 30, 2008	0	825	252	1,077

Other provisions comprise liabilities arising from the premature termination of leases, provisions for staff jubilees and for coverage of ordinary business and professional risks. The cash outflows from these provisions are expected to take place over a period of approximately 10 years and are discounted to present value at a rate of 4%.

The provision for pension liabilities covers the entitlements of employees with long years of service under the terms of the employment contracts valid prior to December 31, 2001. The provision is recalculated annually, using a discount rate of 4%.

18. EMPLOYEE BENEFIT PLANS	Surplus		Economic benefit		Pension expense included in personnel expense	
	31.12.2007	31.12.2006	30.06.2008	30.06.2007	2007/2008	2006/2007
Pension fund	36,461	42,450	0	0	36,107	33,941

As the pension fund had no freely available funds within the meaning of Swiss GAAP ARR 26 either on June 30, 2008 or on June 30, 2007, no economic benefit accrued to the company on either of the two balance sheet dates. The surplus on December 31, 2007 and December 31, 2006 consisted mainly of the fluctuation reserve. Due to the volatility in the financial markets, a projected calculation as at June 30, 2008 produces a shortfall of CHF 36.1 million, corresponding to 95.5% cover.

in CHF 1,000

19. OFF-BALANCE-SHEET LONG-TERM LIABILITIES	Due within 1 year	Due in 2-5 years	Due in over 5 years	Total
Rental contracts for business premises	20,260	48,308	6,408	74,976
EDP rental and maintenance contracts	3,136	9,408	0	12,544
Vehicle leasing liabilities	658	688	0	1,346
At June 30, 2007	24,054	58,404	6,408	88,866
Leases on business premises	19,163	54,512	101,196	174,871
EDP rental and maintenance contracts	3,136	5,489	0	8,625
Vehicle leasing liabilities	665	913	0	1,578
At June 30, 2008	22,964	60,914	101,196	185,074

The company has liabilities under automobile leasing contracts for partners and directors with terms ranging from 3 to a maximum of 5 years. The leasing agreements were concluded by Ernst & Young AG. The liabilities are shown net, i.e., the actual leasing installments net of the amounts recharged to the partners and directors in question.

20. CONTINGENT LIABILITIES	30.06.2008	30.06.2007
Guarantees and warranties on behalf of third parties		
Bank guarantee	7,650	9,192
Joint and several guarantee to a bank as security for loans to partners	1,195	1,542
	8,845	10,734

Ernst & Young AG has an investment in an ordinary partnership (einfache Gesellschaft) for which it has a joint and several liability.

in CHF 1,000

21. SUBSIDIARIES AND ASSOCIATED COMPANIES

		Total Nominal Capital 30.06.2008	Equity interest (%) 30.06.2008	Voting rights (%) 30.06.2008
Subsidiaries (fully consolidated)				
ATAG Ernst&Young Holding AG, Basel		6,000	–	–
> Ernst&Young AG, Basel	o	8,000	100	100
> EY Accounting Services AG, Basel	o	500	100	100
> Ernst&Young AG, Vaduz	o	200	49	49
> Société Fiduciaire Lemano SA, Lausanne	o	500	100	100
> SRC Revisionsgesellschaft AG, Berne	o	100	100	100
> ATAG Technische Organisationen AG, Berne	i	100	100	100
> ATAG Allgemeine Treuhand AG, Zurich	i	100	100	100
> ATAG Treuhand AG, Basel	i	100	100	100
> EY Law AG, Zurich	i	200	100	100

o = operational companies

i = inactive companies

22. EVENTS AFTER THE BALANCE SHEET DATE

Between the balance sheet date and the date on which the financial statements were approved by the Board of Directors (September 24, 2008), no events occurred that had any influence on the financial statements.