Media release

RUAG Statement on SFAO Report

Berne, 28th June 2019. In an audit conducted in spring 2019 of the effective profit margin achieved in the maintenance, repair and overhaul of Swiss Federal Department of Defence, Civil Protection and Sport (DDPS) systems, initiated by RUAG, the Swiss Federal Audit Office (SFAO) found no manipulation in the accounting entries and certifies that RUAG is conducting itself in accordance with its contractual obligations. A central criticism from the SFAO relates to the allocation of overheads. In line with contractual stipulations, RUAG allocates these costs equally across all customers according to the individual business units' share of sales. However, the SFAO based its audit on a new allocation formula for overheads and, on this basis, infers a higher profit margin. RUAG is prepared to consider any future adjustments with the DDPS, but is of the opinion that any changes need to be carefully thought through.

On the basis of an agreement between the DDPS and RUAG dating from 2001 and still applicable, in its audit the SFAO confirms contractually compliant billing and transparent disclosure to the customer. However, the SFAO is generally critical of the system defined in this agreement for calculating the margin. In particular, the SFAO demands a cost allocation based on the user-pays principle, i.e. that only costs that can be clearly allocated to the DDPS be charged to the DDPS. Specifically, instead of treating all customers equally with regard to overheads (e.g. administration, insurance, training, technology development, etc.) the SFAO is now placing the DDPS in a privileged position. On this basis, the SFAO estimates a profit margin of between 11.6% and 14.6%, depending on the underlying assumptions. On the basis of the applicable agreement, RUAG records a margin of between 8% and 10% on the maintenance, repair and overhaul of DDPS systems. A cost allocation as demanded by the SFAO would result in losses of sales and synergies and ultimately higher prices for the DDPS because third-party business increases fixed cost coverage and flexibility in favour of the DDPS.

Urs Breitmeier, CEO RUAG Group, comments: “I am delighted with the confirmation that RUAG is conducting itself in accordance with its contractual obligations, that it is disclosing its margins transparently and that no manipulation of any kind has taken place. I would like to underline that equal allocation of overheads across all customers is in line with contractual stipulations. However, if our owner, after 20 years of successful practice, wishes to take a look at the current position, it goes without saying that we will be happy to discuss the matter.”

Numerous price checks in past years have also been based on the applicable agreement and have identified no deficiencies. What is also clear is that, with the decision to unbundle RUAG and the associated creation of MRO Switzerland as of 1 January 2020, which will focus primarily on serving the Swiss Armed Forces, the Federal Council is among other things strengthening the transparent and cost-effective provision of services to the DDPS.

Contracts with the DDPS

RUAG and the DDPS have set down the rules governing their business relationship in contracts. Since 2013 there have been five-year contracts for maintenance, repair and overhaul of DDPS systems (e.g. military aircraft, simulators, combat vehicles, reconnaissance systems, etc.). These contracts are mostly based on fixed prices with an ongoing price reduction agreed and factored in. In this way, the DDPS shares in efficiency gains and RUAG bears the risk of achieving these efficiency gains. Over the five years examined by the SFAO, proven savings of CHF 109 million accepted by the contracting parties were realised in favour of the DDPS for the period 2013–2017. The contracts were renewed in 2018 and include price reductions of a further CHF 100 million over the next term.

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