

European Program TW Project- « Improving Data Quality in public Accounts »
International Conference of March 16th 2012 in Rome
on
Accounting standards and control procedures : Tools for ensuring data quality

The French Experience in adopting IPSAS,
connecting public finance accounts with national accounting accounts (ESA 95)
and implementing a public internal control system

Danièle LAJOURMARD,
Inspecteur général des Finances



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FOREWORD



Reminder of the Context : a main Budgetary Reform

The French Central Government Accounting Reform : a part of the Constitutional Bylaw regarding budget procedures (so called L.O.L.F) of 1.8.2001



- A main reform including two components :
 - A budgetary reform : definition of a performance based State Budget
 - An accounting reform : the main provisions of the law
 - **Two types of accounts:** (Article 27) « The central government shall keep :
 - accounts of budgetary receipts and expenditures
 - and general purpose accounts for all of its transactions... The State's accounts must be lawful, faithful and give a true and fair view of its net assets and financial situation ».
 - **Two accounting systems**
 - (Article 28) : "Budgetary receipts and expenditures shall be recognised on a cash basis" at their date of payment or receipt
 - (Article 30) « General purpose accounting system is based on the accrual basis principle. Transactions are entered for the financial year to which they apply, regardless of their date of payment or receipt »
 - **The certification of the general purpose financial statements**
 - (Article 58) : General purpose financial statements are submitted to auditors' opinion. The legal auditor for this purpose is the **Court of Accounts' Auditors**
- The reform was to become effective the 1.1.2006

Evolution of the accounting system according to the Constitutional Bylaw (L.O.L.F)



• Before 1.1.2006

1 accounting system (cash basis)

- Budgetary accounts (main accounts / details in Auxiliary accounting)
- Payable and receivable accounts
- Cash accounts

Statements :

- Budgetary reporting
- Trial balance

End year restatement :

Financial Statements
(modified cash basis)

- + Recording of commitments
- For capital expenditures

• After 1.1.2006

2 separated accountings:

Budgetary accounting (cash basis)

Budgetary reporting

General purpose accounting

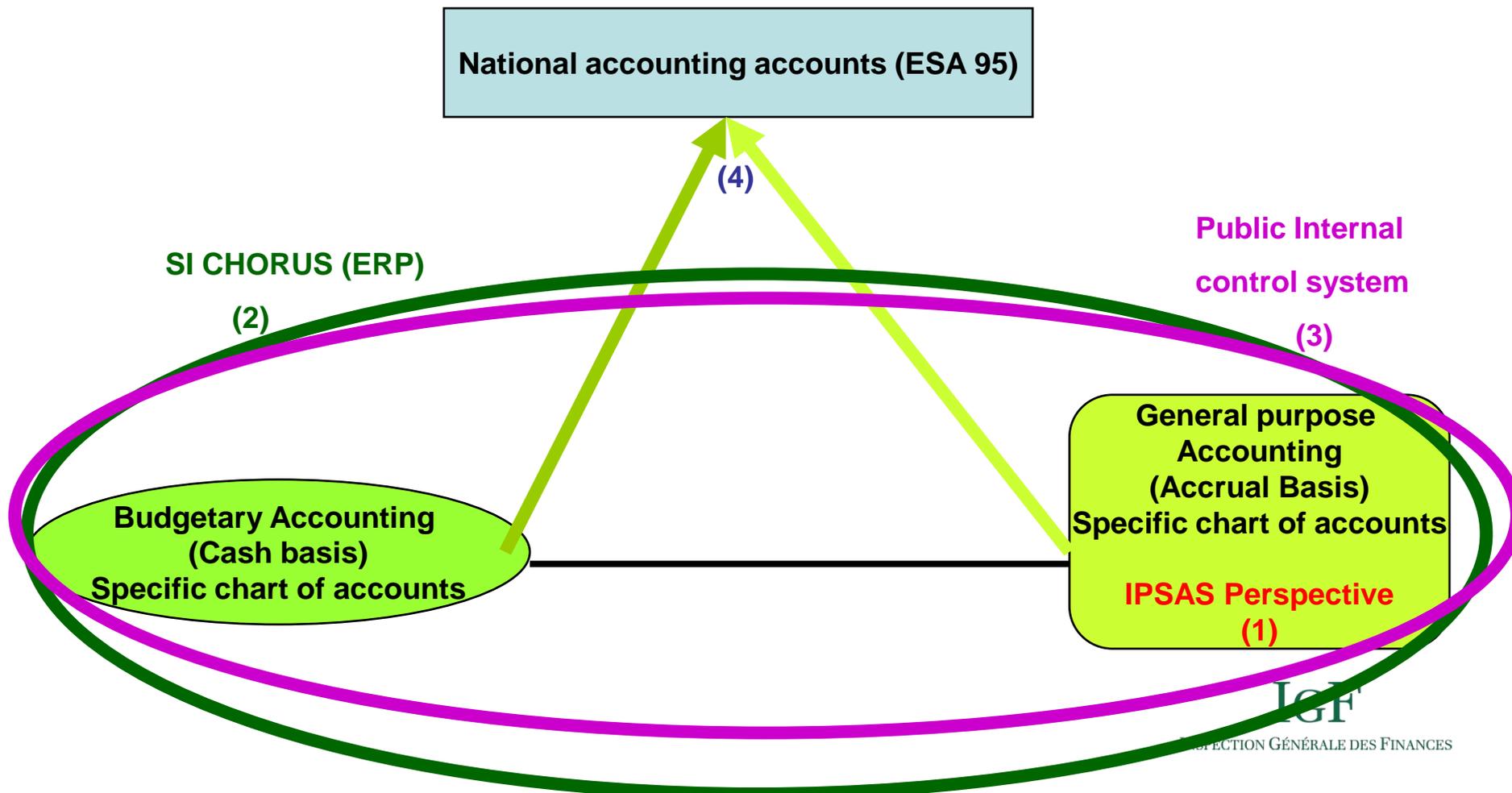
(accrual basis)

Financial statements

- + Recording of commitments
- For all expenditures

The result of the Reform :

Two complementary accounts, with specific purpose, providing data to the national accounting accounts (ESA 95)



Summary



1. The French Central Government Accounting Standards setting Process
2. The Implementation of an Accounting System compliant with the new Standards
3. The Accounting Quality Insurance System (The public internal control system)
4. Synthesis : difficulties and advantages of an accrual accounting system – The connexion with national accounting accounts (ESA95)

Part I



The French central Government Accounting Standards setting process

Legal Framework for the definition of the Accounting Standards



- The Constitutional Bylaw of 1.8.2001 (L.O.L.F) contains two requirements about Central Government Accounting Standards :

1. Requirement about Accounting Standards Setter :

- Accounting Standards Committee (Hereafter : “The Committee”) prepares the Central Government accounting standards (article 30) :
 - These rules (Standards) “are decided on following ***an opinion*** from a committee of public and private experts as provided in the budget act. *The opinion is communicated to the National Assembly and Senate Finance Committees and is published ».*
 - The Standards defined by this committee are put in force by Orders of the Minister of Budget
 - The Committee is chaired by Mr. PRADA, IGF, Former President of the Financial Market Regulation Committee (AMF), Former general director of State Treasury (DGCP)
- This Accounting Standardization Committee was set up at the end of 2002 and completed the collection of Standards in July 2004 for an implementation on 1st January 2006

2. Requirement about Accounting Standards Nature :

- According to the Article 30 of the L.O.L.F. : « The rules applicable to general public accounting only differ from those applicable to companies in terms of the specific nature of government action”. So, the standards **MUST**
 - be based on private accounting principles
 - and in the same time take into account public sector specificities
- The L.O.L.F. does not specify these standards

The approach of central Government accounting standards



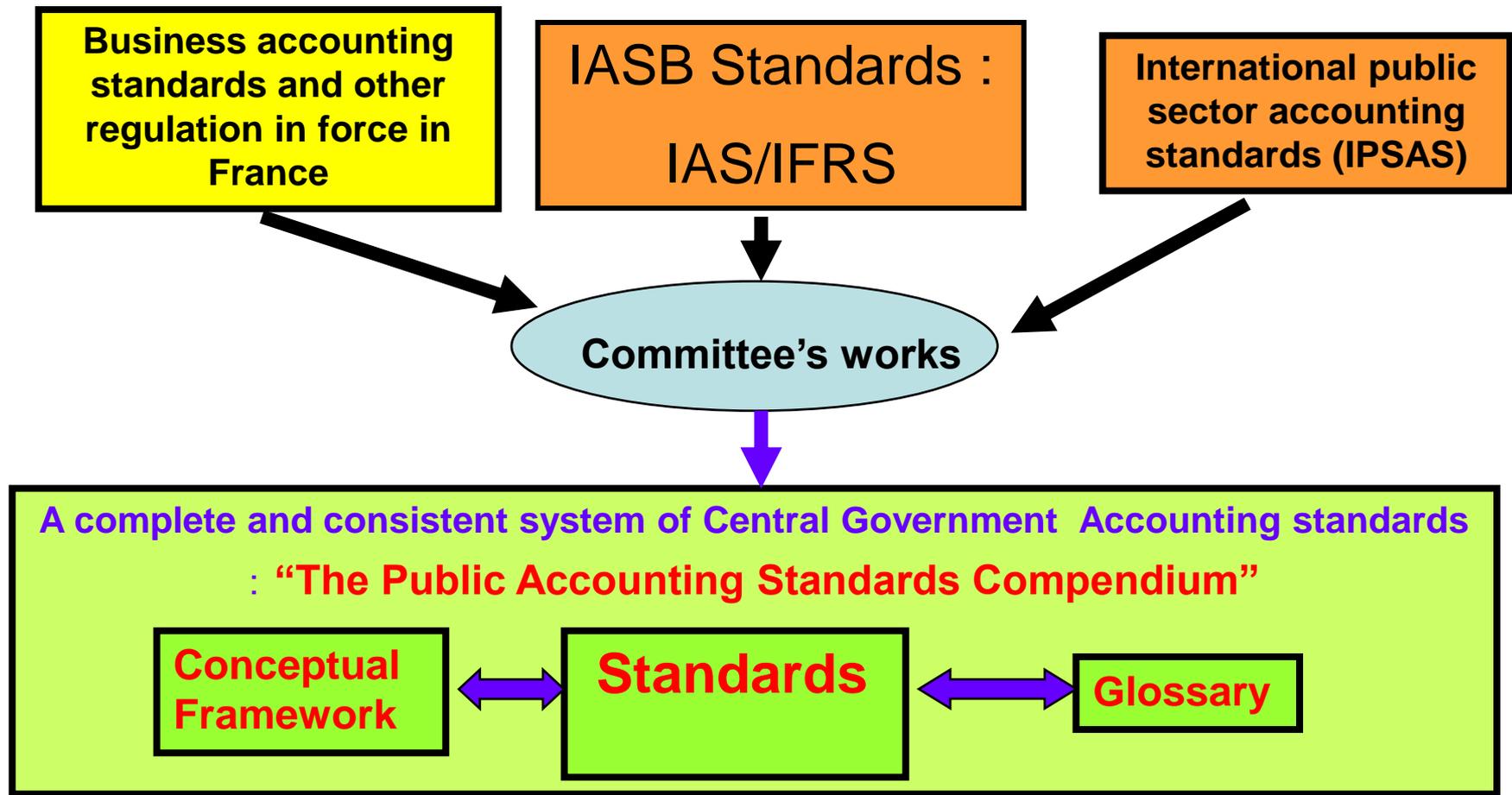
- **The committee elaborates standards with reference to three sets of standards that are converging :**
 - **The Business Accounting Standards (P.C.G) and the Accounting Regulation Committee Rules, in force in France**
 - **The IASB standards (IAS/IFRS)**
 - **The standards being developed by the IFAC Public Sector Committee international business accounting standards (IPSAS)**
- **The committee must determine :**
 - **Which accounting rules are directly applicable to Central Government**
 - **Which rules need to be adapted to specific nature of the central government's activity**
- **In fact, in each Central Government Accounting Standard designed by the Committee, there is a mix of different references**
- **The Committee must explain its choices in the introduction of each standard**

A Design of the Public Accounting Standards as a Whole



- **The body of Central Government Accounting Standards constitute a complete and consistent system**
- **All the accounting standards that apply to the Central Government accounting standards is in a same compendium**
 - These Standards were collected in a “Public Accounting Standards Compendium”
 - They were validated by an order of the Minister of Finance (Order of July 2004)
- **The consistency of the system is reflected by the structure of the compendium that has three parts :**
 - **The Conceptual Framework for Central Government Financial Statements**
 - It presents the assumptions underlying the accounting standards that apply to the Central Government
 - It defines the main concepts derived from these assumptions
 - It explains the scope and the limitations of the financial information's provided by the statements
 - **The Accounting standards with two components :**
 - An introduction that explains the standards, any specific features of the Central Government in the area under consideration, the choices made and how the standard compares to other benchmarks
 - The standards per se (*Only the standards themselves shall be regarded as setting requirements*)
 - **The Glossary**

Scheme summarizing the works of the French Standardization Committee



A new step of standardization



- **Legislation (30.12.2008) changing the composition and the structure of the committee and extending its role in order :**
 - **To improve the corpus of Central Government Accounting Standards**
 - Taking into account New Standards reflecting the IPSAS produced since 2004 (e.g. :taxes) and reflecting practices evolution (development of P.P.P...)
 - Drawing conclusions from the use of initial Standards after some year of practices
 - Writing opinions published on a site web (CNOCP), going into legal force by new orders of the Minister of Budget
 - **To extend the scope of Standardization to other Public Entities : since 2009, the Committee includes three sub-committees respectively in charge of**
 - State and National Agencies Accounting,
 - Local Governments Accounting
 - Social Security Agencies Accounting
- **To contributes to international work on accounting issues (IPSAS, OCDE, UE...)**

The IPSAS

in the 16 French Central Government Accounting standards



- Standard 1 : Financial Statements
 - Reference to **IPSAS 1** Presentation of financial statements and **IPSAS 2** Cash flow statements
- Standard 2 : Expenses (rewritten in 2011 without express reference to IPSAS, not relevant)
- Standard 3 : Sovereign Revenues
 - on going revision of the Standard 3 considering, if relevant, the IPSAS 23 Revenue from non exchange transactions (taxes and transfers), not available in 2004,
- Standard 4 : Operating Revenues, Interventions revenues and Financial revenues
 - Reference to **IPSAS 9** Revenue for exchange transactions
- Standard 5 : Intangible Assets
- Standards 6 : Tangible Assets (rewritten in 2011 to take into account IPSAS 32)
 - Reference to **IPSAS 17** Property, plant and equipment, **IPSAS 13** Lease, **IPSAS 32** Service Concession Arrangements : Grantor”
- Standard 7 : Financial Assets
 - Reference to **IPSAS 6** Consolidated and separate financial statements,
- Standard 8 : Inventories
 - Reference to **IPSAS 12** Inventories
- Standard 9 : Claims related to Current Assets
- Standard 10 : Central Government Cash Position Components
- Standard 11 : Financial Debts and Derivative Financial Instruments
 - Reference to **IPSAS 32** Service Concession Arrangements : Grantor”
- Standard 12 : Non financial liabilities
- Standard 13 : Commitments to be disclosed in Notes to the Financial Statements
- Standard 14 : Accounting Policies, Changes in accounting estimates and errors (rewritten in 2011)
 - Reference to **IPSAS 3** : Accounting policies, changes in accounting, estimates and errors
- Standard 15 : Events after the reporting date
 - Reference to **IPSAS 14** : Events after the reporting date
- Standard 16 : Segment reporting (New Standard, Order of December, 16, 2011)
 - Reference to **IPSAS 18** “Segment reporting” and **IFRS 8** “Segment reporting”

A simplified example of transposition by the Committee of an IPSAS (IPSAS 32 Service Concession Arrangements : Grantor)



- Scope of the Standard
 - types of contracts in the Scope : reference to IFRS for a part and to the IPSAS 32 for an other part
- Assets :
 - Recognition of the asset : in accordance with IPSAS 32 and compliant with the other sets of references : IFRS and PCG
 - Initial evaluation and subsequent evaluation : in accordance with IPSAS 32
- Liabilities :
 - Financial liabilities : in accordance with IPSAS 32
 - Non financial liabilities : **provision of IPSAS 32 irrelevant**, decision of the Committee : accounting in net financial position, in compliance with the Conceptual Framework for Central Government Financial Statements
- Disclosures :
 - **More developed than in IPSAS 32**

Part II

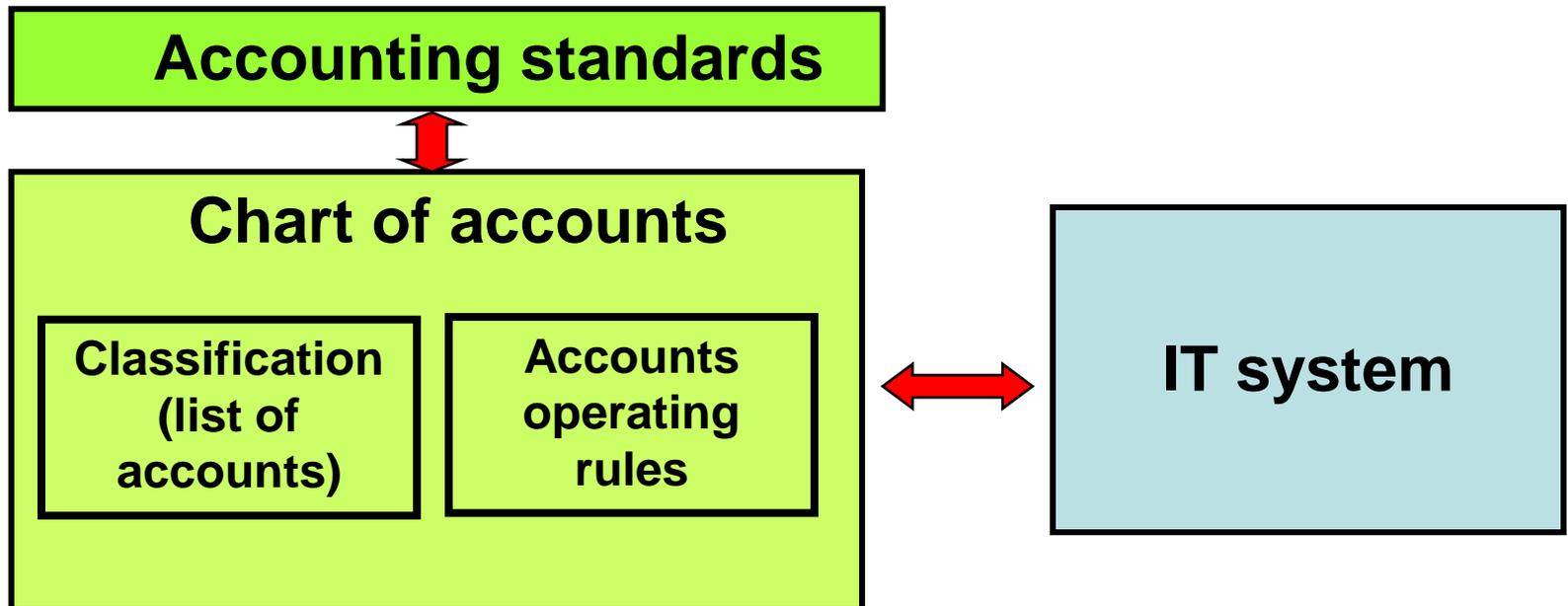


The Implementation of an Accounting System compliant with the new Standards

Definition of a new chart of accounts



- The new chart of accounts is elaborated according to :
 - the new accounting standards
 - the IT system



Adaptation of the information system



- **The IT system was temporary adapted (a transitory step) to meet the date of application of the LOLF (January, 1st, 2006)**
 - To provide the application of the accrual accounting technique
 - To separate the budgetary accounting from the general purpose accounting (general ledger)
- **A more ambitious IT modernisation project has been launched in 2006 (named « CHORUS »)**
 - using E.R.P technology allowing an integrated treatment of all budgeting and accounting data throughout the chain of expenditure and revenue (non-tax)
 - in order to:
 - collect more complete information
 - provide a better accounting traceability
 - streamline procedures and to make productivity gains
 - **End of implementation of CHORUS : 1.1.2011**
 - 20 000 Professional and permanent Users + 30 000 Occasional Users via a simplified technology Intranet
 - **Full budgetary accounting and general purpose accounting in CHORUS : 1.1.2012**
 - Interface between CHORUS and 18 specific applications (tax, pay, cash management...)
- * E.R.P = Enterprise Resource Planning

Training and new directives



- **Two main waves :**
 - During 2004 and 2005, actions were conducted to ensure quality and reliability of the new accounting
 - From 2009 to 2011 : Training for the deployment of CHORUS
- **Perimeter :**
 - Accounting Services (State Treasury),
 - Spending units (Line ministries, services and agencies)
- **Actions :**
 - Executives and staff training (approximately 50 000 people involved)
 - Elaboration of detailed methodology for executives and staff training

Organizational changes



- **At the central level of the State Treasury :**
 - **Setting up the function of Central Government financial statements production**
 - High level technical service in the hierarchy
 - In charge of the official presentation of Central Government financial statements :
 - **Accounting centralization control**
 - **Some specific accounting entries (e.g. provisions)**
 - **Relations with the Court of Accounts' Auditors (according to the constitutional bylaw LOLF)**
- **At the local level of the State Treasury (“Trésoreries générales”)**
 - **Setting up a service in charge of accounting quality**
 - Checking the right application of the new accounting standards

Preparation of starting balance sheet



- **To set up ASSETS of the statement of financial position at 1.1.2006, a census of fixed assets (tangible and intangible) and inventories was carried out in 2004-2005 :**
 - **Method: physical inventory and valuation on market value**
 - **Nota :**
 - Fixed assets were previously identified by budgetary flows reprocessing in a particular application (STGPN), for their acquisition and production cost
 - Intangible assets were not identified prior to 1.1.2006
 - Inventories were not previously registered in accounting
 - **Accounting impact of the new valuation method**
 - Fixed assets : + 209 billion Euros
 - Inventories: + 32 billion Euros

Result of preparatory works :

The objective of 1 January 2006 reached in time



- **Meeting the deadline :**
 - shifting to the new accounting system on 1 January 2006
- **Production of financial statements since the 2006 year according to the standards**
 - **Central Government Balance sheet : The Statement of Financial position**
 - Assets – Liabilities = Net position (or Financial position)
 - **Central Government Surplus/Deficit Statement : 3 statements**
 - Net Expenses Statements
 - Net Sovereign Revenues Statement
 - Operating Balance (Net expenses - Net sovereign revenues)
 - **Cash Flow Statement**
 - Inflows and outflows classified by category (operating activities, investment transactions, financing transactions)
 - **Legal annex (audited):**
 - Notes to the financial statements, commitments and disclosures
 - Reconciliation of Net Operating Surplus/Deficit and Budget Surplus/Deficit
- Budgetary reporting (Budget Surplus/deficit)
- **Accounts certified by the « certifier »** (the Court of Accounts) :
 - certification of accounts since 2006 (with observations)

Part III



The Accounting Quality Insurance System (The public internal control system)

The Accounting quality Insurance System

A comprehensive system of risk and quality management in the field of the Central Government Accounting



- **Definitions :**

- The internal accounting control aims **to ensure compliance with the accounting referential** (Standards) of the French Central Government **and thus enable reliable the financial statements**
- The internal accounting control applies **the referential of internal control recommended by AMF** (French financial market regulation authority) (referential close to COSO)

- **A comprehensive system with three components**

- **Risk analysis and monitoring** of internal accounting control of the Central Government
- **Operational organisation** of internal accounting of the Central Government
- control of the Central Government **Assessment of the whole process** of Risk management and internal accounting control of the Central Government

Risk analysis and monitoring of internal accounting control of the Central Government



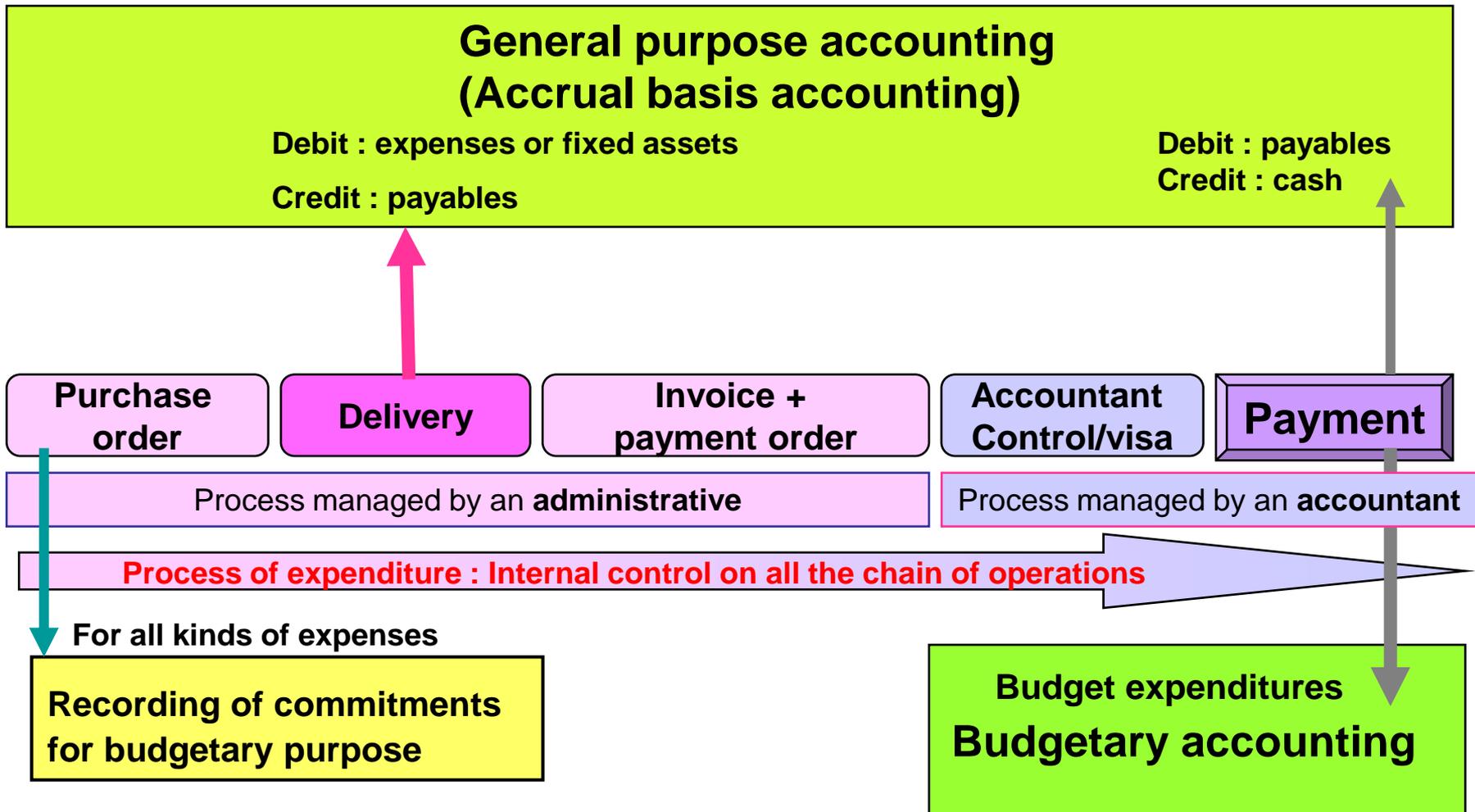
- The structure in charge of this monitoring :
 - The general directorate of public finances (**DGFIP**) of the Ministry of Budget, public accounts and State Reform)
- The process of monitoring
 - **Definition of an Accounting quality Framework with 6 objectives :**
 - completeness, accuracy, attachment to the right exercise, sincerity, consistency, correct accounting entries
 - **Risks identification through a Risks map**
 - map based on the accounting cycles (expenses, revenues, assets, inventories, liabilities, cash) and process (details of the cycles)
 - **Treatment of these Risks through accounting action plans**
 - Definition of improvement measures and schedule
 - Declination in action plans defined by Line Ministries and in action plans of the public accountants of the DGFIP
 - Monitor progress by the DGFIP in association with each Line Ministry and in link with the Court of Accounts
 - **In the ministry lines Support Risk Management by the DFIP :**
 - In each Line Ministry , appointment of an official in charge of this accounting quality subject in association with DGFIP
 - Training, documentation etc.

Operational organisation of internal accounting control of the Central Government



- **The structures in charge of this operational organisation :**
 - The general directorate of public finances (**DGFIP**) of the Ministry of Budget, public accounts and State Reform)
 - In very close association with the **line ministries**
- **The operational organisation**
 - Internal control is not a special process : it is built **into each process** of expenses, revenues, cash... and **at all level** of the accounting process and **all along the chain** of operations (from the authorizing officer to the accountant)
 - Internal control is based on documentation of risks and of financial and accounting process (accounting procedure manuals), the clear definition of responsibilities (for each department or service : a functional organization Chart)
 - It takes into accounts the new IT System CHORUS and the new process resulting

Example of internal control in the new accounting system : Internal control all along the chain of expenses



Assessment of the whole process of Risk management and internal accounting control of the Central Government



- **Development of Tools of Self-assessment of the internal accounting control :**
 - **Risk management application** (« A.G.I.R ») in the accounting offices of the DGFIP to compile the findings, difficulties, abnormalities
 - **Maturity scale of risk management** in the line ministries
- **Assessment of the internal accounting control by the internal audit**
 - Audit function structured primarily in the Ministries of Budget and of Economy (DGFIP, Customs...)
 - Development of the audit function in all the line ministries (Order of the Prime Minister of June, 28, 2011)
 - Creation of a Central Harmonization Unit of Internal Audit (CHAI) chaired by the Minister in charge of the State Reform
- **The Court of Accounts is in charge of the External Audit function (Certification of the State accounts)**
 - It relies on the internal audit if relevant, accordingly to the Standard ISA 610 (International Standard of Audit, available for external audit)

Part IV



Synthesis :
difficulties and advantages
of an accrual accounting system
The connexion with national accounting
accounts (ESA95)

Difficulties



- **Difficulties in the standardization process : lake of availability of a set of standards fully relevant for the State**
 - **IPSAS don't address the main specific issues of the State : The target of convergence with IFRS leads to minimize the specificities of the State**
 - **Some examples :**
 - There is no IPSAS on non exchange transaction expenses when they are the main part of the expenses of a Central Government and of some other public entities;
 - The IPSAS 23 on Revenue from non-exchange transactions (taxes and transfers) is not enough relevant
 - **Some exceptions reflecting a new approach ?**
 - The last standard IPSAS 32 "Service Concession Arrangements : Grantor" : abandonment of the first idea of a standard "mirror" of the private standard concerning the private operator
 - Work in progress on IPSAS Conceptual framework : consultation paper on specificities of the Public entities
- **Difficulties in the implementation of the standards : Greater complexity of the system**
 - Complexity and cost of the IT adaptation
 - Need to manage the adaptation of the staff to a new conceptual framework and a new work process
 - Heaviness of the upgrade to prepare the initial statement of financial position (inventories of fixed assets)

Advantages



- **A best information**

- Accrual accounting complements and enriches the budgetary cash basis accounting with the presentation of the assets, liabilities and commitments
 - It allows a best democratic information (Information of the Parliament, citizens...)
 - It provides national accounting accounts (ESA95) with directly relevant data (Hereafter)

- **A best financial management**

- The identification and valuation of these assets, liabilities and commitments lead to a more active management of these elements and to more informed choices
 - Examples : the identification of non tangible assets (radio frequencies, water power, prestigious names, internet domain name...) lead to a valuation of these assets (trough auctions, concessions...)
 - Accrual accounting provides data to calculate full cost (with amortization, provisions...) and to identify the real cost of public policies.

The connexion with national accounting accounts (ESA95)



National accounting accounts (ESA 95)

Accounting restatements

Accounts of the other economics actors

State accounts

Budgetary Accounting
(Cash basis)
Specific chart of accounts

General purpose
Accounting
(Accrual Basis)
Specific chart of accounts
IPSAS Perspective

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National accounting accounts (ESA95) : a specific accounting system...



- The national accounting accounts (ESA95) :
 - A specific purpose :
 - The representation of the whole **economic activities** of a Nation
 - A specific consistent framework
 - with precisely defined concepts : economic actors belong to **institutional sectors** performing **operations** traced through **accounts articulated**, summarized in **tables** showing **aggregates**
 - With a specific accounting referential :
 - It includes the same concept of **accrual basis** used in the general purpose accounting (the monetary flow is registered when the economic event occurs and not at the date of the payment)
 - **but there are special rules for some operations**
 - With specific methods : the use of the **double entries** but always with a “mirror effect” between two economic actors (M. MAGNIEZ, the French best specialist of the system call this method : “**the quadruple entries**” :

National accounting accounts (ESA95) : a specific accounting system requiring adjustments of the data provided by accrual accounting



- **Accrual basis accounting fills an important role in the process of elaboration of national accounting**
- **But elaboration of national accounting accounts requires important adjustments of the data provided by the accounts of the different economic actors**
 - Difference of concepts, for example concept of production,
 - Method of “quadruple entries” (coherence between sectors for example for tax)
 - Valuation of the non exchanges transactions
 - Valuation of assets (historic cost, other cost...)
 - Question about the perimeters (mainly for the definition of public debt)

National accounting accounts (ESA95) :

The contribution of the Central Government Accrual basis Accounting



- **The Central Government Accrual basis Accounting provides Information not included in cash basis accounting**
 - Change in Assets, Change in inventory (specially important in military scope)
 - Liabilities, some provisions...
 - Accrued interest ...
- **The French Central Government Accounting Standards take into accounts the links with the National accounting accounts :**
 - The conceptual framework establishes **the principle of the compliance** between the two accounting system
 - Some standards contains provisions to provide directly relevant specific data :
 - For example, in the Standard 2 “Expenses”, the transfers are classified by category of final recipients of the aid, according to the requirements of the national accounting accounts (Households, business sector, public sector...)
 - Some explain, when relevant, the similarity or the difference with the National accounting accounts :
 - Example Standard 3 “Sovereign Revenues” (compliance with the concept of accrual basis used in national accounting accounts)
- **In complement, the budgetary cash basis accounting provides some useful information for some specific purpose and adjustments**



Additional information

The main differences between standards applicable to companies and those applicable to Central Government



- **The Central Government financial statements cannot be interpreted in the same way as those of companies**
 - There are no Initial capital amounts, start date, initial balance sheet
 - Valuation of assets raises special problems :
 - The balance sheet does not include the main Central Government asset : « intangible asset » of sovereignty, and its corollary, the right to levy taxes
 - Tangible assets is a resource controlled by the government as a result of past events that is expected to produce economic benefits in the future : either cash flowing (in compliance with companies' standards) or potential production of services expected.
 - The very long life of a lot of assets
 - **The role of « insurer of last resort »**
 - which the Central Government has to play in some circumstances , requires a precise definition of the limits on the types of commitments to be disclosed in the notes to the financial statements
 - **Profit or loss versus surplus and deficit**
 - In business accounting expenses and revenues can be matched to measure an economic efficiency : profit or loss is the difference between revenues and accrued expenses relating to the resources consumed during the accounting period
 - For Central Government, the difference between revenues and expenses can not be interpreted as profit or loss in this manning. According to the weight of sovereign revenues and of transfers, it is better to use the words of « surplus » or « deficit »
- **To underline these differences, some Central Government financial statements are presented in a suitable form**

For more details...



- The English text of :
 - The Constitutional bylaw regarding budget procedure of 1. August 2001
 - The Central Government Accounting Standards
 - The audit opinion on the financial statements of the Central Government – Fiscal year 2007-8-9-10
 - And other documents about French reform

Are available on the French Government's site web:

www.performance-publique.gouv.fr

The Central Government Accounting Standards is directly available on CNOCP site web

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Thank you for your attention
Vi ringrazio per l'attenzione
Ilginiz için teşekkür ederiz



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