

**AUDIT OPINION ON THE  
FINANCIAL STATEMENTS  
OF THE CENTRAL GOVERNMENT**

**FISCAL YEAR 2008**

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	<b>Page</b>
<b>Introduction.....</b>	<b>1</b>
<b>I – Court’s opinion on the 2008 Central Government financial statements .....</b>	<b>5</b>
<b>II – Detailed observations about the Court’s opinion .....</b>	<b>9</b>
<b>A – Qualifications on the 2007 financial statements withdrawn in full or partly met .....</b>	<b>9</b>
<b>B – Qualifications expressed relative to the 2008 financial statements .....</b>	<b>13</b>
<u>B.1. Qualifications of a substantial nature</u>	13
1 – Financial and accounting information systems of the Central Government.....	13
2 – Ministerial internal control and audit systems .....	19
3 – Implementing partners.....	23
4 – Assets of the Defence Ministry .....	27
5 – Sovereign revenues .....	33
6 – Liabilities related to Programme expenditure .....	37
7 – Real estate holdings.....	43
8 – Other assets and liabilities end-of period reports .....	47
9 – Social debt redemption fund .....	51
<u>B.2. Other qualifications</u>	55
10 – Cash accounts.....	55
11 – Other Central Government participations .....	59
12 – Public service concessions .....	63
<b>III – Report on the audits of the 2008 financial statements .....</b>	<b>65</b>

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*Pursuant to the Constitutional Bylaw on Budget Acts (LOLF) of 1 August 2001, amended and in effect as at 1 January 2006, the Court of Accounts is required to prepare, each spring, three documents.*

*Pursuant to paragraphs 4 and 5 of Article 58 of the LOLF, the first two documents must be prepared before 1 June:*

*- one of the documents is a report on the Central Government results and budget management over the prior year, which analyses the implementation of budget acts in all respects, including the utilisation of appropriations by mission and by budget programme. That report is filed with Parliament together with the Central Government budget review bill for the previous year;*

*- the second document is an audit opinion “attesting that the Central Government financial statements are lawful, truthful and give a true and fair view, which is submitted together with the report on the auditing procedures performed”; the foregoing is the purpose of the document herein which is appended to the aforementioned budget review bill.*

*The third document is the report serving as a basis for the preliminary budget policy debate (“Report on the Situation and Outlook of Public Finance”), as provided by Article 58-3<sup>o</sup> of the LOLF. The latter must be filed in June along with the Government's Report on Developments in the National Economy and Public Finance Trends.*



## **Introduction**

The authors of the constitutional bylaw had recommended in 2001 that the Central Government should acquire tools enabling it to assess its financial position and its holdings, to learn about its costs and to better value its results in order to, firstly, improve its budget management.

The certification of the Central Government financial statements, entrusted with the Court of Accounts, is one of those tools.

And yet, eight years after the enactment of the LOLF, it must be said that, despite some real progress made, the Central Government financial statements are still far from being in compliance with the rules in effect. Moreover, it is hard to tell how the Central Government has used the findings of the certification of the accounts. The delays in the implementation of the accounting reform are a hindrance to the transparency of the Central Government accounts and could, in the future, have a negative impact on the confidence that citizens, international organisations and investors have in the creditworthiness of the Central Government. The lack of concrete application of those findings could contribute in the short term to decreased initiatives of the administration and is probably in part behind the delays experienced in the projects already underway.

By deciding to certify the accounts for the 2006 and 2007 fiscal years with respectively 13 and 12 qualifications, the Court wanted to underscore the fact that it would like to adopt a constructive approach. The Court is willing to continue with this approach for those matters that it considers cannot be resolved within a short timeframe.

Conversely, in relation to the other matters, it will most definitely draw conclusions from the absence of the dynamic change that it has chosen to pursue.

### **1 - Certification mission**

The permanent mandate received by the Court pursuant to Article 58, paragraph 5 of the LOLF is part of its duty to support the Parliament and the Government in its audit of the application of finance laws, set forth in Article 47-2 of the Constitution. The certification that the Central Government accounts are lawful, truthful and give a true and fair view issued by the Court is addressed to Parliament, which is charged with approving the financial statements in accordance with Section III of Article 37 of the LOLF and, more generally, to all users of the accounts. The position of the Court, which is based on a collegiate decision is handed down in *inter partes* proceedings.

### **2 - Certification purpose**

Certification is defined as a substantiated written opinion about the accounts of an entity expressed by and under the sole responsibility of an independent agency. It includes collecting the information needed to obtain reasonable assurance that the financial statements are, in all material respects, in compliance with a given set of rules and principles, including first and foremost, those according to which the accounts must be lawful, truthful and present a true and fair view.

In accordance with Article 30 of the LOLF, the Central Government general account is governed by the same accounting rules and principles as those applicable to the private sector, subject to the specific nature of Government action. These rules and principles were set out in the Central Government's accounting standards approved by the Order of 21 May 2004 and amended by the Orders of 17 April 2007 and 13 March 2008, based on the opinion issued by the Public Accounting Standards Committee.

Public accountants are responsible for keeping the accounts and preparing the financial statements of Central Government. They ensure the truthfulness of accounting records and compliance with procedures, as set forth in Article 31 of the LOLF. This quality requirement with regard to the accounts implies the implementation of effective and efficient internal control and internal audit mechanisms as well as the truthful presentation of financial statements free of material misstatements, whether the result of fraud, errors or omissions. Public accountants are also responsible for the selection and application of appropriate accounting methods and for providing reasonable for the circumstances estimates.

### **3 - Certification scope**

The annual financial statements of the Central Government reflect the transactions carried out by Government offices, establishments or institutions without legal personality including the Parliamentary Assemblies and, for the first time, the office of the President of the Republic and the Constitutional Council. On the other hand, entities with legal personality are only included for up to the capitalised amount representing the rights held therein by the Central Government.

In accordance with Government Accounting Standard 1, the Central Government general account refers to the annual financial statements which consist of a balance sheet (or statement of financial position), an income statement (including three parts : a schedule of net expenses, a schedule of net sovereign revenue, and a balance of transactions for the fiscal year), a cash flow statement and the notes to the accounts providing data and disclosures that are useful for the understanding and interpretation of accounting information. This includes, as provided for in Article 54 of the LOLF, an assessment of the Central Government's off-balance sheet commitments. The balance sheet and the income statement are derived from the Central Government trial balance, which as such is not subject to certification. The method applied in preparing the statement of cash flows, which analyses the changes in cash over the fiscal year, consists in putting together budgetary and cash flows in the same category by means of adjustments.

After the Court presented its observations based on the audit of a set of interim financial statements, the general account of the Central Government for 2008 was approved by the director general of public finances on 1 May 2009 and certified by the minister of the budget, public accounts and civil service on 20 May 2009. It was appended to the final budget review bill for 2008 budget along with this certification.

### **4 - Certification challenges**

Budgetary accounting, which was the only system prior to the LOLF, is an accounting system that reflects only the inflows and outflows for the fiscal year. Under it, it is not possible to record all the events that affect the management and the holdings of Central Government.

Accrual accounting for all the Central Government transactions which has been added to budgetary accounting since the LOLF has become effective on 1 January 2006, has a broader scope. Thus, it reflects the position of the Central Government with respect to third parties (for example in relation to its debts), the state of its holdings (end-of-period

reporting, valuation), changes in its inventory, hedging against identified risks through provisions, the matching of transactions to the fiscal year in which they have occurred, even when they do not correspond to cash inflows and outflows.

Currently, this is the system that must be used to steer the management of administrations. This is the system that must be used likewise to measure the sustainability of public finances and to ensure in a more efficient manner the preparation of the public finances planning laws, sector-based planning laws, and finances laws. This system finally represents the condition for the adequate measurement and analysis of the total cost of actions and policies implemented by the Central Government.

The retrospective restatement of financial statements following changes in method or estimates or corrections of errors, which will be done as from 2009 in accordance with Accounting Standard 14 will foster the comparability of financial statements with those from prior fiscal years and, consequently, the analysis of the changes in the financial position and the holdings of Central Government.

### **5 - The context of 2008**

The current financial and economic crisis that is compelling Central Governments to increasingly turn to the financial markets simply increases the demand for public accounts transparency. It has led the Court to pay particular attention to the accurate posting of the commitments generated over the year and made by Central Government, to the position and status of entities in which it holds an ownership interest and to the pertinence of the financial disclosures contained in the notes to the accounts.

## ***I - Court's opinion on the 2008 Central Government financial statements***

### **A - Criteria for determining the Court's opinion**

1. In accordance with International Auditing Standards applied by the Court, an auditor may not issue an unqualified opinion if material difficulties have been identified. There are two types of such difficulties:

- disagreements with the preparer of the financial statements regarding whether or not the accounting methods applied are acceptable, how those methods were applied or the relevance of the amounts and disclosures provided in the financial statements or uncertainties whose extent and scope the preparer of the financial statements may be disputing;
- limitations on the scope of the audits carried out due to circumstances out of the auditor's control and which prevented the auditor from carrying out the checks deemed necessary thereby and for which the procedures engaged to collect audit evidence regarding items available to the auditor by default in the corresponding line items of the trial balance preventing the auditor from forming an opinion in accordance with the audit criteria.

2. The degree, number and combination of disagreements and uncertainties and limitations on which the Court bases its professional judgement and decides whether to issue a qualified opinion, a disclaimer of opinion or a refusal to certify the accounts.

3. In its report on the Central Government general account as at 31 December 2007, the Court included a number of limitations, disagreements and uncertainties, which led it to issue an opinion with twelve qualifications, nine of which were labelled "substantial".

4. Compliance with the commitments made by the ministers in response to the qualifications expressed by the Court has been subjected to regular audits. The commitments made for the future do not represent in and of themselves more than a framework for action set by the administration in response to disagreements, uncertainties and limitations expressed by the auditor on the financial statements for the year ended.

5. Based on the auditing procedures performed and reported at the end of this document, the Court believes that it has collected sufficient audit evidence to support its opinion on the financial statements for fiscal year 2008.

## **B - Opinion on the Central Government general account**

### **1 - Statement of findings**

#### *a) Qualifications on the 2007 financial statements withdrawn in full or partly met*

6. At 31 December 2008, the conditions for the removal of two of the qualifications expressed on the 2007 financial statements were met. The first one, which the Court had qualified as substantial, pertained to the public procedures account managed by Coface and the section of savings funds centralised at the *Caisse des dépôts et consignations* (Finding No. 7) The second pertained to risk provisions (Finding No. 11)

7. Two other substantial qualifications on the 2007 accounts were satisfied for a portion of their components : on the one hand, in the qualification regarding sovereign revenue the disagreement on tax loss carry forwards (Finding No. 5-a); on the other hand, the disagreement on specific intangible fixed assets (Finding No. 6-b)

#### *b) Limitations*

8. Once again the Court was faced with two types of limitations in auditing the 2008 financial statements.

9. Firstly, there are structural limitations shared by all the ministries. The inadequacy of the financial and accounting information systems limits the ability of the Court to collect evidence necessary to confirm the audit criteria relative to the flow of transactions and account balances (Finding No. 1). In addition, the effectiveness and efficacy of the ministerial mechanisms for internal controlling and internal audit still remain very insufficient (Finding No. 2).

10. The audit performed by the Court thus was confronted with limitations that are specific to certain areas of the audit. The main ones concern the insufficient substantiation of the sovereign revenue accounts (Finding No. 5), the low level of auditability of the tools used for the recognition of real-estate holdings (Finding No. 7), the deficiencies in the end-of-period reports and the weak relation to the fixed-assets and inventories accounts for all the ministries (Finding No. 8) the lack of well-structured controls carried out on cash accounts (Finding No. 10).

*c) Disagreements and uncertainties*

**11.** The exceedingly low quality of the accounts of a great many implementing partners and the deficiencies in their inventories have led the Court to renew for 2008 its major disagreement regarding the capitalised for such purpose value of the financial participation of the Central Government, i.e., €54.7bn (Finding No. 3)

**12.** Most of the assets of the Ministry of Defence remain valued in accordance with methods that are contrary to the Government accounting standards based on end-of-period reports that continue to be unreliable. The end-of-year transactions generate massive adjustments, which are posted to the opening balance and whether or not they are well-founded cannot be fully confirmed. The uncertainties that remain at the completion of the Court's audit pertain to several tens of billions of euros. What emerges is a disagreement on the valuation of assets listed on the balance sheet for a total of €177bn gross, €110bn net (Finding No. 4)

**13.** Uncertainties continue to exist on the matching of sovereign revenue to the fiscal year, including that for taxes collected on behalf of third parties (Local Municipalities, Social Security, Central Government's implementing partners). There are significant deficiencies in the financial disclosures provided in the notes to the accounts regarding the taxes collected on behalf of third parties (Finding No. 5).

**14.** Numerous disagreements and uncertainties were again found regarding the inventory and recognition of Central Government liabilities related to Programme expenditure. The disagreement on the provisioning of the Central Government commitments with respect to RFF company in charge of the French railway network, by itself, pertains to close to €7bn (Finding No. 6)

**15.** The irregularities that continue to affect the end-of-period reports, the valuation and recognition of the Central Government real-estate holdings (€57.2bn) and the disagreement on the accounting treatment of the working load limits and "further" expenses have led the Court to reiterate the uncertainty expressed relative to the 2006 and 2007 accounts (Finding No. 7).

**16.** The weakness of end-of-period reporting procedures and the incorrect application of accounting standards entail a multitude of uncertainties and disagreement regarding the recognition of fixed assets and inventories of the civil ministries (close to €30bn), software produced internally by the administration (€1.1bn) and co-financing of road investments which it enjoys (€2.2bn) (Finding No. 8).

17. The Court found a disagreement related to the failure to reclassify the social debt redemption fund as a controlled entity, while duly noting the commitment of the minister of budget, public accounts and civil service, to resolve this issue during 2009. Such reclassification, which would justify a strict application of the criteria of Accounting Standard 7, would have had deteriorated the net position by approximately €80bn (Finding No. 9).

18. Uncertainties continue to exist on the reconciliation of the cash position of armed forces units with accrual accounting and on the quality of accounting records made during the year in the bank account to which are charged the accounting transactions of the financial administrations (Finding No. 10)

19. The deficiencies experienced in the recognition process applied to ownership interest in international organisations, for a capitalised amount estimated at €25bn, entail an uncertainty on the participations of the Central Government and the refusal of the administration to quantify in the notes the cost of loans granted at preferential rates and which are listed in the accounts for an outstanding amount of €10.7bn represents a disagreement (Finding No. 11)

20. Finally, the failure to recognise the underlying assets of the concession agreements prior to 1 January 2006 is at the origin of an uncertainty regarding financial stakes of several tens of billions of euros that the administration has committed to clear (Finding No. 12).

## 2 - Impact on the Court's opinion

**21. In view of the statement of findings, the Court is withdrawing in full two qualifications, one of which had been qualified as substantial, both expressed relative to the 2007 financial statements. In addition, two other substantial qualifications relative to these statements have been met for a portion of their components.**

**22. In view of the statement of findings, the Court certifies that, with regard to the applicable accounting rules and principles, the Central Government general account as at 31 December 2008 is lawful, truthful and gives a true and fair view of the financial position and holdings of the Central Government, subject to 12 qualifications detailed in Part II. The first nine qualifications are of a substantial nature.**

23. Several of these qualifications result from difficulties that the Court considers might be resolved over the short term.

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## **II - Detailed observations about the Court's opinion**

### **A - Withdrawal of the qualifications expressed on the 2007 accounts**

#### **1 - Qualifications withdrawn in full**

##### **Public procedures account managed by Coface and section for savings funds centralised at the *Caisse des dépôts et consignations***

###### *a) Public procedures account managed by Coface*

24. At 31 December 2007, the Court had maintained the disagreement noted with respect to the prior year regarding the public procedures account managed by *Compagnie française d'assurance du commerce extérieur* (Coface). It had found that the account represented an appropriation holding controlled by the Central Government and that it had to be included directly or indirectly into its financial statements.

25. The possibility to treat the public procedures accounts as a trust, a legal instrument introduced in the French Civil Code by the law of 19 February 2007, was proposed by the Court. Its interest is to gather into one autonomous and separate holding, assets or rights allocated to a specific purpose and entrusted by a "trustor" to a "trustee". The Central Government may qualify as a trustor since the Law of 4 August 2008 on the modernisation of the economy. Coface SA meets the conditions required for trustee status.

26. The accounting treatment of a trustee relationship has been specified by the National Accounting Council. It leads to registering as participations the rights of the Central Government on the trust holdings and to treat the deductions made by Central Government from the account as income allocated to a trustor.

27. Without undertaking to re-qualify as a "trust" the nature of the mechanism before the end of the agreement still in effect between the Central Government and Coface, the administration has agreed to the creation, within the accounts of the Central Government's ownership interest of the category of "special purpose vehicles". The Account for Public Procedures Managed by Coface is included among them. The initial value is measured based on the account equity as at 31 December 2007, i.e., €8.9bn. The Central Government agreed to the accounting

adjustment of the deduction from this account. The disagreement has therefore been removed as at 31 December 2008.

*b) Section for savings funds centralised at the  
Caisse des Dépôts et Consignations*

**28.** As at 31 December 2007, the Court had maintained the disagreement for the accounts of the previous year, relative to the exclusion from the scope of the ownership interest of the Central Government of the section of savings funds managed by the *Caisse des dépôts et consignations* (CDC), likewise not consolidated with the accounts of the latter.

**29.** The law of 4 August 2008 on the modernisation of the economy and the application decrees clarified that the status of savings funds and the conditions of distribution and regulated centralisation of savings passbooks. A bundle of indices makes it possible to consider that the law places the management thereof under the control of the CDC, in compliance with an already codified framework. Therefore as an entity not controlled by the Central Government, the section of savings funds must be reported in the accounts thereof.

**30.** The Court recommended adding to the acquisition cost of the Central Government's stake in the CDC that of the savings funds included in the general banking risk funds (€7.6m as at 31 December 2007, €4.6bn as at 31 December 2008). The administration has accepted to this solution. A disclosure in the notes to the Central Government general account describes the new framework for the management of savings funds. The disagreement relative to the section of the savings funds managed by the CDC has been removed as at 31 December 2008.

### **Contingency provisions**

**31.** The Court expressed on the 2007 accounts a qualification relative to the completeness and measurement of the provisions for risks inherent to the activity of the Central Government.

**32.** The actions implemented by the ministry of the interior, overseas departments and local municipalities have made it possible to cover all the litigation matters in its field and to make the end-of-period reporting procedures more uniform. The legal proceedings brought before the European Court of Human Rights were inventoried with the help of the Ministry of Foreign and European affairs. The provisioning of mass tax disputes was expanded to cover related interest on arrears. The total

amount of the provisions for risk shown in the liabilities of the Central Government balance sheet was €10bn.

33. Uncertainties remain on the provisioning of tax disputes, grouped with those that affect sovereign revenues. Conversely, the general uncertainty as to the completeness of the inventory and valuation of other risks that result in the recognition of provisions within the Central Government accounts has been reduced to an acceptable level.

## **2 - Qualifications partly met**

### **Tax loss carry forwards**

34. As part of the substantial qualification issued on sovereign revenues for fiscal year 2007, the Court had renewed its disagreement on the failure to recognise the effect of tax loss carry forwards on the liabilities side of the balance sheet. It had estimated that the right of taxpayers to carry forward such losses over time was supposed to lead taxpayers to recognise them, especially since their amount was known to the administration.

35. The provisions of Government Accounting Standards 1 and 3 relative to financial statements and to sovereign revenues were amended by Order of 11 March 2009. They make it easier to qualify the effect of ordinary tax losses and non refundable tax credits that are likely however to be carried forward. They presume greater disclosure in the notes to the accounts. The latter currently quantifies the inventory of loss carry-forwards counted at the end of the year (€245bn) as well as the estimated impact of their charge to future Central Government sovereign revenues (€36bn).

36. The Court reviewed the notes to the 2008 accounts and was able to obtain assurance based on their compliance with the requirements of the reporting standards. The portion of the qualification issued in 2007 in relation to the disagreement on the accounting treatment of tax loss carry forwards has been therefore withdrawn as at 31 December 2008.

### **Specific intangible fixed assets**

37. For fiscal year 2007, the Court had maintained a substantial qualification resulting from the failure to record in the Central Government's balance sheet assets related to its power to authorise or restrict the occupation or exploitation of the public domain.

**38.** In 2008, the preparer of the financial statements, recognised the authorisations for the exploitation of terrestrial frequencies that had resulted in transactions, notably the GSM and UMTS licenses. The assets thus included in the balance sheet total €4bn. After auditing the valuation methods, the portion of the qualification on specific fixed assets that was related to an uncertainty and a disagreement on the recognition of specific intangible assets was withdrawn as at 31 December 2008.

## **B - Qualifications expressed on the 2008 financial statements**

The qualifications of a substantial nature, followed by other qualifications are presented below.

### **B.1. – Qualifications of a substantial nature**

#### **1 - Financial and accounting information systems of the Central Government**

**39.** The Court had issued a qualification on the 2006 and the 2007 accounts based on the general limitations in the scope of the certification work imposed by the Central Governments financial and accounting information systems.

**40.** The reliability of those systems represents a fundamental challenge for the certification process. Their features must notably enable the Court to obtain reasonable assurance as to the decrease in the risk of material errors in the accounts.

**41.** At the end of fiscal year 2008, the Central Government financial and accounting information system, remain fractured with more than 350 applications referenced by the agency for the Central Government financial IT. They continue to be characterised by their inadequate ability to meet the requirements of accrual accounting. The efforts made since 2006 to increase their reliability still do not allow the Court to conclude that there has been a decrease to an acceptable level of the risks inherent to those systems or that they now present sufficient auditability.

##### *a) Increasing the reliability of existing systems*

**42.** The action plan implemented by the general directorate of public finances in 2008 made it possible to achieve certain results.

**43.** The stabilisation of the management rules supporting the preparation of financial statements and the lack of records made directly into the TCC centralisation application contributed, among other things, to increasing the reliability of *Palier LOLF IT system*. The mobilisation of the administration also contributed to reducing the risks inherent to certain applications and to improving the quality of the audit train in order to link the accounting entries to original transactions and vice versa.

**44.** These continued efforts are all the more so necessary that the roll-out calendar for the future Central Government financial and

accounting information system remains subject to significant uncertainties.

*b) Insufficient integration of the IT systems*

**45.** The work of the administration consisting in improving the audit trail between the accrual accounting application (CGL) and the applications that feed it, were not completed at the end of 2008. It remains, in addition, insufficient to enable the external auditor to ensure the correct integration of the managers' data into the accounting records. This can be seen from the following examples :

- The *Orchidée* application (used to identify accrued income and expenses) has been, since 2008, automatically interfaced with the CGL application. This technical development constitutes advancement. The methods for its realisation have however induced significant sources of discrepancies between *Orchidée* and accrual accounting, which greatly limits their scope;
- *Palier LOLF* does not specifically retrace the Central Government internal transactions. The actions undertaken to identify and inventory these transactions with a view to offsetting them are not yet exhaustive.
- The *PAY* application calculates and prints the payroll of 2.5 million civil servants. The earnings files are not sufficiently well reconciled with the data held by the managers.

*c) The inadequacy of current application for the purposes of accrual accounting*

**46.** The often antiquated and inappropriate design of applications requires data to be adjusted several times between creation and final recognition. It presents a high inherent risk and limits the ability of the auditor to audit the numerous accounting entries resulting from that.

**47.** At 31 December 2008, the database file recorded in the general ledger contained over 36 million journal entries. This volume results from the sizeable number of records transiting through clearing accounts (70% of flows recorded). The entries thus offset (and therefore without impact on the end balance) cannot be directly identified. It is not possible to link negative entries to their offsetting entries either. This situation leads the external auditor to carry out an overall audit of all the accounting records, which is incompatible with the time frame afforded thereto to conduct the audit.

**48.** Despite their decrease in 2008, the number of accounting schemes used is close to 8,700. Their instability from one fiscal year to the next one, their insufficient documentation and the lack of certain auditing tools do not enable the Court to obtain assurance about their consistency or about the perfect correspondence between accounts and the sum of records that are supposed to be used to populate them.

**49.** Designed for the purposes of logistics follow-up, the IT systems of the Ministry of Defence are not suited to the requirements of accrual accounting. They do not ensure a uniform accounting treatment of data of the same nature. The data that are extracted from them require adjustments in the electronic inventory files done in a simple office application. The volume of data and the weak controls in place are at the root of too large a number of errors identified by the Court.

*d) Lack of suppliers' auxiliary accounts*

**50.** Accrued liabilities and debts contracted by the Central Government with respect to suppliers, implementing partners, intermediary agencies and beneficiaries of transfer measures totalled €16bn at the 2008 year-end.

**51.** To verify their completeness, the auditor must be able to collect audit evidence from the interested creditors (“circularisation of third parties”). The implementation of this auditing technique requires having a balance with third parties that populates the movements for the year and the balance of the debts. In terms of completeness, a selection of third parties to be polled based on transactions should be favoured.

**52.** The expenditure applications, *Accord* and *NDL*, were not designed to meet the requirements of an accrual-basis accounting system or to keep full accrual accounting. Debts are only inventoried at the end of the period, either in the *Orchidée* application or directly in *CGL*.

**53.** The consolidation of local databases that would enable the identification for each third party the movements for the period turns out to be an impossible task due to the very large number thereof, their different designs, the absence of a single identifier for certain third parties, and the loss of the audit trail during the correction of allocation errors.

**54.** The payment of supplier debts is done in accordance with terms that do not ensure proper traceability.

**55.** The circularisation procedure that has been implemented by the preparer of the financial statements since 2006 remains limited to transactions concerning the Central Government implementing partners and the Social Security agencies.

**56.** The continued lack of third party auxiliary accounts prevents the Court from using an audit technique generally considered as being the most reliable in checking the completeness of non-financial debts. It represents as such a limitation on the scope of such audits.

**57.** The integrated management software package *Chorus* will make it possible from a technical point of view to keep an auxiliary accounting on a national basis. Such accounting will nevertheless only be operative if the administrations record an obligation when created and not at the time payment is demanded.

*e) Inadequacy of the auditing tools available to the auditor*

**58.** To successfully perform the audits, the Court must have available audit tools enabling it to ascertain the respect of audit criteria applicable to the accounting records and balances.

**59.** Despite the improvements enjoyed by the *India LOLF* data warehouse in 2008, its insufficiently broad scope and the unavailability of certain requests at the national level lead to the finding that it cannot yet fulfil this role.

**60.** To make up for the limitations of the automatic control of data in various applications, the administration has increased the number of manual controls. Their number however does not enable the Court to obtain assurance about their full effectiveness within the timeframe compatible with that afforded thereto to express an opinion on the accounts.

**61.** For example, 2.5 million manual entries were made in the accrual accounting application, CGL, during 2008 alone. The insufficient reliability of coding of entries hinders the identification of uniform categories of entries to be audited. It makes necessary the performance of manual reviews whose volume is not very conducive to collecting audit evidence. The scope of these remedial procedures is, in addition, greatly limited by the lack of precision of the entries considered.

*f) Pathway of financial and accounting information systems*

**62.** The purpose of the *Chorus* project, whose roll-out is staggered from 2008 to 2011, is to combine in an integrated management software

package the functionalities of the greatest possible number of ministerial and inter-ministerial applications for expenses, non-tax revenues and end-of-period reporting. It must enable a better integration of the accounting information while limiting the manual adjustment of data. The audit by the Court of the first version of the *Chorus* project shows strong uncertainties as to its ability to improve on the quality of keeping and follow-up on the accounts of Central Government.

**63.** Over the entire transition phase, prior to its full roll-out, *Chorus* will simply be a supplementary expenditure application, unable to remedy over the short term the limitations inherent to the accrual accounting application in place.

**64.** The extraction of data derived from old systems with a view to integrating them into *Chorus* presents a risk that will have direct impact on the scope of the audits performed by the auditor.

**65.** There are no established internal audit procedures in *Chorus*. Their precise definition will not be ready before the completion of the project roll-out.

**66.** Finally, the capacity of the software program to manage the complexity related to the keeping of the various accounting systems, the high volume of entries resulting from that, is not ensured at this stage.

**67.** Two other structuring programmes will be rolled out after 2012 ; however, the distance in time does not offer the visibility necessary to the auditor to express an opinion on the development that will result from that. This refers to the *Overhaul of the Payment System* unit of the *Copernic* programme which will ensure the management of the collection of most taxes as well as the *Opérateur national de la paye (ONP- National Payroll Operator)*.

#### *g) Conclusion*

**68.** The current features of the Central Government financial and accounting information systems and the risks pertaining to them require the implementation by the Administration of many controls, the full effectiveness of which the Court was not able to assess. It emerges from the inadequate auditability a general limitation to the scope of the Court's audits. Therefore, the substantial qualification is maintained.

**69.** The administration must continue to make efforts designed to reduce the scope of this limitation, without waiting for the completion of the large structuring IT projects, especially since their roll out calendar is distant in time. An actual taking into account of the concerns of auditability expressed by the auditor must also take place without delay.

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## **2 - Ministerial systems for internal control and internal audit**

**70.** The Court has been expressing since the audit of the 2006 financial statements a substantial qualification relative to the weaknesses of the ministerial systems for internal controlling and internal audit.

**71.** The accounting service is a service shared among the managers who initiate transactions and the accountants who confirm them and ensure their unwinding. The nature of this sharing has justified entrusting with computers, with the help of accountants, the operational implementation of the internal controlling mechanisms both at the central administration and at local offices of the Central Government.

**72.** In time, when the mechanisms for accounting risk control will have reached the maturity required and when the internal audit works will be able to provide assurance to that effect, the secretaries general of the ministries should be able to send the Court representation letters enabling them to guarantee on the effectiveness and efficiency of such mechanisms within their ministry.

### *a) Internal controlling*

**73.** Internal controlling may be defined as the set of mechanisms or organised processes which are structured and permanent, selected by the management and implemented by the Administration at every level to control the functioning of their activities so as to give reasonable assurance that their objectives have been completed. Since this involves accounting and financial procedures, the objectives are the lawfulness and truthfulness of records as well as their conformity to the facts to be described (“true and fair view”).

**74.** The Court notes the progress made in 2008 by the Administration in the design and the development of ministerial systems of internal controlling. This approach has continued to be improved according to a methodology that starts from a preliminary analysis of accounting risks and identifies specific actions gathered from the ministerial action plans.

**75.** The consolidation of the internal controlling steering around secretaries general has made it possible to combine in a more relevant manner risk analysis and the definition of actions. It has also translated into a broader coverage of accounting processes in which the managers participate:

- The “financial” ministries thus combine a high-level management, led under the direct authority of the secretary general, a close collaboration of the ministerial budget controller and accountant and significant involvement of the Central Government offices executive directors, who have dedicated governance structures in their area of competence.
- The action plan of the Ministry of Defence includes currently all the structural entity within the Ministry. The improved management of the mechanism and the extension of its scope have been conducive to this Ministry’s making up for lost time.

**76.** The extension of this approach to a growing number of local offices within all the ministries constitutes significant progress. The action plan of the Ministry of Justice is for the most part dedicated to local offices, which incur 80% of expenses. The level of commitment of managers and personnel in charge of internal controlling in the regional healthcare and social matters departments has increased greatly.

**77.** The identification and treatment of accounting risks at the local offices level represent nevertheless a project yet to be completed. This is the case at MEEDAT (Ecology and Transports Ministry), where the deployment of internal control is still limited for the most part the central administration. In a large number of Central Government offices and local government bodies of the Ministry of Culture, the approach is limited to awareness raising actions.

**78.** Generally, the deployment of the mechanism has remained partial and its degree of maturity is still inadequate to be able to guarantee an effective control of accounting risks. The consolidation of the first lessons learnt, their generalisation and exploring them in-depth constitute a major challenge for 2009.

**79.** The internal controlling organisation and documentation phase is only a first stage. It has been cleared by a significant number of ministries. The portion of effective and traceable control actions remained largely insufficient in 2008.

**80.** In the ministries where the size, organisation and degree of maturity of the mechanism justify it, the effectiveness of such first-level actions must be guaranteed by the designation of a second level of internal control. In all the cases at hand, the operational nature of the ministerial mechanisms for the control of accounting risks must be reinforced and well combined with the internal control implemented within the accounting network of the general directorate of public finances. The tests conducted on the “salaries” process illustrate the need to reinforce the combination and complementarity of the tasks pertaining to managers and

accountants. The same conclusion may be drawn about the implementation of the suppliers' auxiliary accounting.

*b) Internal Audit*

**81.** The creation within each ministry of an internal audit department in accordance with ISA 610 is a fundamental challenge. Due to its independent position with respect to the chain of command, the internal audit ensures the quality as well as effectiveness and efficiency of internal control within the ministry and provides advice for improvement. To this end, it methodically evaluates its process of risk management and control.

**82.** The coverage of Central Government offices with an internal audit mechanism at the ministerial level did not progress substantially between 2007 and 2008.

**83.** Only three ministries (the two "financial" ministries and that of agriculture and fishing) had an operational, independent system equipped with sufficient means.

**84.** Several ministries are planning to develop such a function starting from a dedicated department reporting to the highest level in the chain of command. A mission for the foreshadowing of the internal audit has thus been installed by the secretary general of the ministries in charge of social matters. At the Ministry of Defence, the ministerial committee on accounting and financial audit, created at the end of 2007, started to operate effectively in 2008. This progress is yet to be consolidated by upgrading its personnel and clarifying its role with respect to the multiple auditing mechanisms that are already in place within the ministries.

**85.** In a great number of cases, the internal audit mechanisms continue to be characterised by their scattered, incipient nature, or even their non-existence and the lack of priority given thereto. Thus, the support of reforms and the audits of universities due to become self-governing have led to postponing the creation of a Central Government audit committee within the ministries of national and higher education and research.

**86.** The accounting and financial audits in partnership with the audit mission of the Public Finance Department (DGFIP) are not sufficient to remedy this weakness.

*c) Conclusion*

**87.** The ministerial internal accounting and financial controlling and internal audit systems remains unable to provide the auditor with assurance on the control, by all the ministries, over the operations contributing to the preparation of financial statements. It results therefore in the renewal of this substantial qualification. The progress expected

concerns the traceability of actions of internal control and the structuring of the internal audit function in all the ministries.

### 3 - Implementing Partners

**88.** The Court expressed a substantial qualification concerning the valuation of the implementing partners of the Central Government policies in the 2006 and 2007 accounts.

**89.** Accounting Standard 7 defines the “implementing partners for governmental policies” as entities with legal personality exercising a public service mission under the strict control of the Central Government, which contributes a major portion of their financing. They represent participations of the Central Government and are listed as such on the assets side of its balance sheet. As at 31 December 2008, 663 implementing partners were listed for an amount of €54.7bn or close to one third of its participations.

**90.** Projects running for several years that have been implemented since 2006 by the administration to respond to this still do not allow for a remedy of the deficiencies in their inventories, of the inability of a significant number among them to file their financial statements within the timeframe compatible with the establishment of those of the Central Government and the insufficient reliability of their accounts.

#### *a) Implementing partners inventory*

**91.** The Central Government must make sure that all of its participations are listed under its assets and that the distinction is properly made, within controlled participations, between implementing partners and non-implementing partners, in accordance to the criteria defined by the accounting standard.

**92.** As in 2007, the methods for establishing the list of implementing partners alter the quality of their inventory. Proof of that are the irregularities identified at 31 December 2008 (entities responding to the regulatory criteria defining the quality of implementing partner but not listed or conversely not meeting the criteria but remaining categorised as implementing partners).

**93.** The works for increasing the reliability of the scope that have been undertaken by the preparers of the financial statements continue to be insufficient to guarantee their integrity. The movements of new additions and removals from the scope are better retraced, but the inventory that results from the works carried out in 2004 and 2005, remains insufficiently substantiated.

**94.** The shared responsibilities between the competent departments of the Central Government, even though they belong to the same ministry,

so that the preparer of the financial statements has little control over the methods and the results of the inventory carried out by the budget department.

**95.** Absent an amendment that has in fact been recommended by the Court, the current wording of Standard 7 leaves pending several ambiguities that are related to the categorisation criteria. This is the case, among other things, of the criterion of majority financing by the Central Government, whose wording is too elliptic to clear up the uncertainties that result from the diversity of contribution forms enjoyed by the implementing partners. The criteria in effect, likewise do not solve the case of joint financing, the implementing partners that are parent companies or legal forms such as public interest groups, associations, etc.

**96.** The insufficient documentation and inadequate traceability of the inventory process explain that the Administration was unable to justify maintaining several entities in the scope of the implementing partners and that it needed more than one year to start providing an analysis of the compliance of the criteria for the categorisation in response to a list of 50 entities currently not listed, but identified by the Court.

*b) The time periods for transmission of the  
Implementing Partners' financial statements*

**97.** The portion of implementing partners that are unable to transmit their financial statements within the time limits compatible with the closing of the Central Government accounts remains too high and is decreasing only slowly. More than one third (compared to close to half as at 31 December 2007), representing 37% of their total valuation (compared to 40% at 31 December 2007), were unable to produce their 2008 accounts within the required deadlines. There is no explanation for such late filings for entities whose inventory operations are theoretically completed before the end of the month of January and that are subject to the obligation to report budget and accounting data fast and feed the annual performance reports appended to the budget review bill.

**98.** The possibility to use the financial statements for the previous year, even though offered to the preparer of the Central Government financial statements by Standard 7, should continue to be applied only as an exception. This is not the case at the close of this third accounting year. Such a situation degrades the true and fair view that the balance sheet is supposed to give on Government financial holdings.

*c) Quality of the Implementing Partners' accounts*

**99.** Since 2006, the Court has found that the implementing partners' financial statements, whose quality is a condition for the reliability of their valuation in the Central Government's balance sheet, presents serious deficiencies. At 31 December 2008, the works undertaken in terms of accounting quality have not had any material impact on the accounts of the implementing partners. While a number of implementing partners and oversight administration have been put to work, the accounting adjustments made in 2008 remain modest and the accounting quality of the fixed assets line items remains very insufficient as a whole.

**100.** The implementing partners must post under assets the goods that they control and under liabilities the corresponding financings. The Central Government launched in 2006 a project aimed to increasing the reliability of its holdings, consisting of listing the goods, enhancing the corresponding data in the information systems, having them valued by France Domaine and, if applicable, proceeding to correcting the accounting records. The slow progress, including on the first wave, has led the Central Government to ask the implementing partners again to work on this objective. The results remain very modest: At the end of 2008, only 12 implementing partners (representing 8.9% of the total number) had completed the process, and 356 had not yet closed the initial phase of the inventory and so inventory taking is often deficient. To this problem are added the methodological difficulties in the valuation and recognition of assets.

**101.** A large number of implementing partners do not record in their accounts historical monuments, works of art or special assets that they control and that yet often justify the existence of these entities (*Centre des monuments nationaux, Opéra de Paris*, public establishment of the Park and of the Grande Halle de la Villette, etc.).

**102.** The accounting guidelines of 23 January 2006 relative to the recognition and impairment of assets and the recognition of provisions for risks and off-balance sheet commitments is still applied just as diversely. The implementing partners are trying hard, for most of them, to implement these complex provisions (*INRIA, Service hydrographique et océanographique de la marine, Parc national de Port-Cros*, etc.), while even tasks as simple as asset inventory and amortisation remain to be made more reliable.

**103.** In terms of debts and claims between the Central Government and its implementing partners the existence of a structured reconciliation procedure on the one hand and an operating procedure specific to the

“transparent”<sup>1</sup> mechanisms on the other hand constitutes progress in the improvement of the accounts. The weaknesses that continue to affect the former, and the late deployment in 2008 of the latter, do not however yet make it possible to reach the accounting quality objective sought.

**104.** While the implementing partners are now aware of the internal accounting control and while the tools that are available to them are getting better, few have gone beyond the stage of appropriation and roll out of efficient operational mechanisms. Under these circumstances, the overall effect on the accounts of the generalisation of internal accounting control will only become palpable in a few years.

**105.** The drivers of change that constitute the legal external audit of the financial statements and the involvement of the overseeing agencies – whose positive effect can be seen in a handful of implementing partners -- should particularly play for the universities whose financial statements are affected by serious and multiple deficiencies. While their situation is heterogeneous, none can yet really be considered as having equipped itself with a well-rounded accounting and financial management. This finding includes those that have enjoyed since 2009 greater responsibilities and competencies, while by the same token this autonomy has reinforced the stakes that are attached to the transparency of their financial situation, based on the quality of their financial statements.

*d) Conclusion*

**106.** Faced with the finding of serious deficiencies affecting the financial statements of the implementing partners and the lack of progress matching the gaps to be filled, the principle of prudence should be leading here. Therefore, the unrealised capital gains recognised by the equity method applied to the implementing partners at the year-end should not be taken into account. This result would be a decrease in the valuation of the implementing partners in the balance sheet of Central Government in the amount of €10.1bn.

**107.** All of the deficiencies found lead the Court to the same conclusion as in 2006 and 2007 of a substantial qualification resulting from a disagreement about the capitalised value of the implementing

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<sup>1</sup> A Programme expenditure mechanisms is considered transparent if: The procedure involves the Central Government, the implementing partner and the final beneficiary; the implementing partner has a limited margin of autonomy in taking the decisions; the financing of the mechanism is provided in whole or in part by transfers from the Central Government; the Central Government is bound by obligations to the final beneficiary.

partners in the Central Government financial statements as at 31 December 2008.

**108.** Over the short term, the imperfections of the inventory and the delays in reporting the accounts could be easily remedied by a revision of the criteria of categorisation of Standard 7 and a more directional management by the preparer of the financial statements.

**109.** Over the longer term, the improvement in the quality of the accounts by the implementing partners presumes, in addition to the acceleration of the multi-annual projects already underway (real estate inventory, internal controlling, etc.), a reinforcement of the action of the overseeing bodies and a broadening of the scope of external audit to include implementing partners that represent the majority of the equity stake value.

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#### **4 - Ministry of Defence assets**

**110.** The Court expressed, for fiscal years 2006 and 2007, a substantial qualification resulting primarily from a disagreement on the valuation of the assets of the Ministry of Defence, the non-completeness of the scope and the account year-end procedure.

**111.** Excluding real estate, these assets total €177bn gross on the balance sheet of the Central Government as at 31 December 2008 and €110bn net.

**112.** The Ministry of Defence undertook, in early 2007 to perform over a period of three years ending at the 2009 year-end, a set of actions intended to create an accounting reporting framework adapted to the specificities of military equipment and to improve the quality of accounting reporting. As at 31 December 2008, there was some true progress for two thirds of the pathway.

**113.** The impact of the efforts made at this stage on the quality of the accounts remains nevertheless modest considering the magnitude of the deficiencies that continue to be experienced by most of the accounting processes related to the assets of the Ministry of Defence.

##### **a) Improvements noted in 2008**

**114.** The reporting scope for the end-of-period reporting has been expanded in 2008 to include new assets for material amounts. Those include some “secret” assets and goods in storage at manufacturers for a gross amount of €5.5bn. Reordering of inventories to fixed assets have occurred for €1.1bn gross.

**115.** The accounting standards have been made clearer in relation to a dozen procedures at stake (dismantling, expenses that can be subsequently capitalised, write-downs, revisions of the amortisation schedule, general maintenance, major inspections, etc.) This clarification made it possible to experience in 2008 new accounting treatments that nevertheless affected a scope that remains limited.

**116.** The contract analysis method has been expanded to include most current weapons programmes in accordance with the commitments made. The implementation of accounting procedures aiming at improving the recognition of such transactions and that of the equipment placed in service has continued. The effect on the accounts of these new procedures will only be able to be measured with the percentage-of completion of contracts.

*b) Persistent deficiencies*

**117.** The inadequacy of the IT systems, which is reflected notably in the use of simple spreadsheets to process hundreds of items and valuations, constitutes one of the main hindrances to high-quality accounting reporting.

**118.** The works conducted to reconstitute data that are sometimes very old are also experiencing structural limitations. 16% only of the value of property, plant and equipment in service are valued in accordance with the standard. The valuation of old equipment is thus confronted with the lack of available supporting accounting documentation.

**119.** The deficiencies noted in certain departments, notably in terms of internal control and the mastery of controlling tools by the persons in charge of period-end reporting, lead to numerous major irregularities or uncertainties that do not make it possible to clear the adjustments made in the year-end.

**120.** Most controls of the finance department and of the ministerial accounting department are done after the balance sheet date and the adjustments, if any, continue to be recorded as a correction to the opening balance for the next year.

**121.** Finally, the players in the recognition of defence assets do not communicate sufficiently with one another to ensure the consistency of the entire mechanism. Thus, the dates of outflow of outstandings at the General Delegation for Armament (DGA) and inflow in service at the armies are not in line. A certain number of goods are thus excluded wrongly from the accounts for the fiscal year. In addition the absence of correspondence between the accounting nomenclatures of the DGA and the armies creates difficulties when the equipments are taken into the period-end reports. The works started in 2008 in the scope of the 12 weapons operations processed by the contract analysis method, have made it possible however to record progress in the reconciliation of goods delivered to the armies.

*c) The valuation of real-estate and inventories*

**122.** The Defence Ministry's assets include:

- Equipment in use for €9bn gross (€4.5bn net) and developments in use for €20bn gross (€10bn net);
- Equipment in production for €16bn and developments in progress for €12bn;
- Inventories for €32bn, written-down for €4bn

**123.** The valuation of the vast majority of these assets still does not meet the rules stipulated in Central Government's Standards 5 on intangible fixed assets, 6 on tangible fixed assets, and 8 on inventories.

**124.** Most equipments and developments in progress valued in accordance with the flat so-called "global" valuation method remains significant. It pertains to €4.5bn in assets as at 31 December 2008. It is not in compliance with the Government accounting standards as it values a group of undefined and not readily identifiable assets.

**125.** The application of the contract analysis method to some equipments in service has entailed important valuation differentials with the data listed in the end-of period report. For example, the eighteen ships and sub-marines analysed by the General Delegation for Armament (DGA) had their value decrease by close to 30% compared to 2007. The justification of these variations is only very partial. The IT systems of the DGA in fact did not allow reporting on data specific to each market until after 2003. In addition, the developments related to those weapon programmes are not valued and therefore not recognised.

**126.** The goods acquired directly by the services, excluding the General Delegation for Armament, are for the vast majority valued at prices derived from the logistics IT systems of the armies. These data, not justified and not auditable, do not respond to the criteria of valuation set by the accounting standards of the Central Government.

**127.** Numerous management systems do not allow to valuing the inventories according to the weighted average cost per unit method or by the FIFO method. Yet these are the only two methods allowed under Standard 8

**128.** Finally, while progress has been made to adjust the depreciation schedules over the probable useful life of equipment, the write-downs of tangible fixed assets and inventories continue to be rarely included in period-end reports or recognised. Close to 70% of the gross amounts of tangible fixed assets and over 80% of the gross amounts of inventories continue to be unreliable.

*d) Year-end transactions*

**129.** The data from the logistics IT systems of the armies feed the inventory files that constitute the auxiliary accounting of fixed assets and inventories in the financial statements of the Central Government. The reconciliation of this auxiliary accounting and accrual accounting continues to be very difficult or even impossible.

**130.** The auditor should be able to reconcile on the one hand the logistics information and the end-of-period report files and on the other hand the period-end report files and accounting. Major uncertainties and limitations continue to prevent it from doing so.

**131.** The period-end reporting data continue to be unreliable. The Court, this year again, found multiple errors in the files of the entity in charge of ensuring the maintenance in operating condition of the aeronautical defence equipment (SIMMAD), whose fixed assets and inventories are valued at €57bn. These recurrent irregularities reflect the deficiencies in the IT procedures, an incorrect implementation of the new accounting procedures as well as a deficiency characterised by the definition of procedures adapted to internal controlling. These factors bring an uncertainty on the reliability of end-of-period reporting of the main department holding fixed assets and inventories of the Central Government.

**132.** The use of files in Excel at all the stages of the closing procedure is truly unsuitable for the volume of records. The calendar of the year-end transactions does not allow the Administration to proceed with the necessary accounting controls. The General Delegation for Armament (DGA) sends its period-end data directly to the ministerial accounting department, without going through the third-level of control for its outstanding on weapons transactions (€27bn as at 31 December 2008)

**133.** The annual accounting flows do not correspond to the movements of inflow and outflow in the period-end reporting files. Many sources of disparities exist. The heterogeneous nature of the reporting standards between period-end reporting files and the charges to budget flows is thus at the root of a large portion of the differences noted.

**134.** The Court is therefore unable to express an opinion as to whether the massive adjustments charged to the opening balance in order to match the accounts as at 31 December 2008 and the period-end reports are well-founded. The amounts of these adjustments, made in reference to the provisions of Standard 14 relative to the changes in method of valuation or correction of errors totals over €3bn net for tangible fixed assets and over €1bn for inventories.

*e) Conclusion*

**135.** All of foregoing findings lead the Court to express, as in 2006 and 2007, a substantial qualification resulting from a disagreement in the recognition of the assets of the Ministry of Defence.

**136.** This disagreement can only be settled if at the end of the three-year period of building up the reliability of the accounting data for which the Ministry had made a commitment the stakes and means to allocate to the main issues are redefined and if such redefinition of priorities is expected to occur as early as in 2009.

**137.** The *Chorus* project will not thus constitute a response suitable for the difficulties noted by the Court unless it integrates the proper needs followed by the assets of the ministry and is accompanied by a suitable auditing plan.

**138.** The harmonisation of the various accounting treatments among the various players within the Ministry is a priority. It is the condition notably for increasing the reliability of new acquisitions and weapons operations.

**139.** The experiments conducted with the new procedures in 2008 must be analysed, improved and expanded to reach all the services concerned.

**140.** Finally, the internal controlling mechanism must be subjected to regular assessments by the ministerial audit committee.

## 5 - Sovereign revenues

**141.** In 2006 and 2007 the Court had expressed a substantial qualification resulting from the limitations in the scope of the audit and a significant level of uncertainty due to the lack of mastery of the preparation process of tax-related financial statements. This situation has improved to some extent in 2008. The audits conducted on the 2008 accounts led to expressing some forty audit findings, involving stakes in some cases reaching several billions of euros.

### *a) Management and controlling context*

**142.** The accounting management of sovereign revenue and their audit environment are characterised by some very integrated IT processes on significant volumes of data and the production of a limited number of reporting records at the end of the year pertaining to very high amounts.

**143.** The accounting checks and the substantiation work done by the preparer of the accounts remain insufficient to be able to guarantee the decrease of the risk of material errors to a reasonable level.

**144.** The Court still faces serious limitations that prevent it from expressing with reasonable assurance an opinion on the quality of the information provided to it for the audit. The management rules which structure the automatisms and the statements generated by the systems are not sufficiently documented. This situation limits the control ability of the preparer of the financial statements as well as that of the external auditor. The accounting works for the justification of these flows are directly affected thereby.

**145.** The functional limits and the setting of parameters for the IT applications lead to major work of inventorying and analysing data without integration in an adequate controlling mechanism. The processing of data, carried out by computers and provided to accountants, was not systematically subjected to appropriate justification works to guarantee their quality and compliance with the accounting standards in effect.

### *b) The matching principle*

**146.** The measurement of receivables continues, for a significant portion thereof, to be based on inflow records and not on the generating event as required by the accounting standards. The result is matching errors, which are themselves sources of overvaluation or incompleteness. For this reason alone, the amount of correcting entries estimated by the auditor stands at €1.6bn.

**147.** The systematic matching for the year of the cash products recognised in January of the following year is not a relevant method. The method used should, conversely, be such as to strive take into account the great diversity of the types of income in order to determine for each one of them the year to which it pertains and their recognition generating event.

**148.** With respect to taxes collected by the Central Government and whose product is transferred to third parties (social security, local authorities, implementing partners), the setting of the parameters of the IT systems does not make it possible to note, in the evaluation of the remaining balances to be collected, the portion intended for the beneficiary. That portion is therefore reported at the end of the year without using the books. But the approximations and omissions found by the auditor show the imperfections of this adjustment mechanism.

*c) Insufficient controls and substantiation as the responsibility of the preparer of the financial statements*

The assessments prior to the recognition of the end-of-period records are not analysed systematically and sufficiently in depth by the preparer of the financial statements. This control deficiency is at the root of multiple errors that were noted at the time of the audits conducted by the Court. Many of them, regarding for example the double accounting of income to be reversed, pertain to material amounts. The Administration did not carry out the necessary controls, and as a result it was unable to detect the errors that had occurred in the calculation of the provision for the write-down of fines (lack of completeness in the inventory of risks or, conversely, taking into account of risks that the Central Government is not responsible for covering).

**150.** The accrual accounting data are not sufficiently well reconciled to management data. As in 2007, the disparities between the receivables recognised and the nominal lists of the remainder to be collected in the area of taxes on individuals collected by means of tax rolls does not make it possible for the Court obtain assurance about the existence or accuracy of receivables at the balance sheet date. Likewise, the inadequate analysis of electronic statements generates uncertainty as to the valuation of the inventory of tax penalties relative to the allocated taxes and duties.

**151.** When management statements are used, the reliability of the data is not always sufficiently verified. The progress made in increasing the reliability of the database used in estimated the provision for tax litigations thus did not make it possible to completely remove the uncertainties on the valuation as at 31 December 2008.

**152.** A portion of the substantiations needed for the validation of the balances had to be asked the Authorizing Officers, or even reconstituted by the external auditor itself.

**153.** In terms of tax obligations carry forwards and tax obligations related to the VAT managed by the Customs directorate (DGDDI), in amounts on the order of €1.9bn, the information provided by the preparer of the statement does not have the probative value base to justify the balances.

**154.** The accounting methods used in 2008 are not justified in the year-end files. Nor are the provision rate of tax receivables as well as the obligations upon VAT receipt which are the result of a subtraction between VAT gross products and VAT credits allocated during the fiscal year. These insufficiencies reveal uncertainties on some very sizeable aggregates.

**155.** In a great number of cases relative to taxes of very varying nature and amounts such as VAT, corporate income tax (IS), interior taxes on petroleum products (TIPP), personal income tax and covering the entire spectrum of reporting entries, the insufficient controls are combined with the scarcity or lack of pertinent substantiations.

*d) Presentation of financial information*

**156.** The notes to the financial statements provide information relative to the taxes collected by the Central Government whose product is transferred to third parties (Social Security, Local Authorities) These are notably contributions such as local taxes, interior taxes on petroleum products, taxes on salaries, value added tax, contributions to the revenues of the national holding, excise duties on tobacco and alcohol, etc. From a total collected by the Central Government of €346.7bn the portion allocated is €136.6bn. This information presents major deficiencies.

**157.** Due to the limitations of the IT systems, the amounts of those taxes and dues allocated were reconstituted manually and inventoried solely based on cash data for 75% of contributions. The factors presented do not provide exhaustive information. In addition, the comparative data needed for understanding the changes in the taxes collected for third-party accounts are not produced. The information presented in the notes thus is still insufficient to account for, on an accrual basis, the distribution of the allocation of gross revenues between the budget of the Central Government and financing of the third-party beneficiaries.

*e) Provisions for tax litigations*

**158.** Contingency provisions recognised on the Central Government's balance sheet amounted to €10bn as at 31 December 2008, compared to €6.5bn at the end of 2007. The provisions for tax litigations, which represent a predominant part, are estimated at €6bn.

**159.** The Court has identified, in the course of its certification audit, a new tax litigation that appeared in 2008. The potentially sizeable impact of this lawsuit should have led to the booking of a provision based on the best estimate of the outflow of sources necessary to extinguish the obligation.

**160.** The uncertainty noted for the 2007 financial statements regarding the completeness and valuation of provisions for tax litigations must be maintained

*f) Conclusion*

**161.** The lack of mastery of the process of accounting production (in terms of matching, presentation and substantiation of records) does not enable the Court to consider that the accounting risks pertaining to revenues and expenses related to tax have been reduced to an acceptable level. Consequently, the substantial qualification on the recognition of government revenues from taxes must be maintained.

**162.** The Public Finance Department (DGFIP) must be able to justify all the balances in the trial balance related to government revenues from taxes. It must also increase the reliability of the entries relative to the taxes collected by the Central Government whose product is transferred to third parties (Social Security, Local Authorities) under the same conditions

## 6 - Liabilities related to Programme expenditure

**163.** For the 2006 and 2007 fiscal year, the Court had expressed a substantial qualification based on the absence of completeness and reliability of the liabilities related to Programme expenditure recognised by the Government in its mission as economic and social regulator.

**164.** As at 31 December 2008, the total transfer transactions, amounted to €161.6bn, and the amount of liabilities transfer transactions amounted to €1.6bn in loss provisions and €1.7bn in expenses payable and other non financial debts. The scope of liabilities to be recognised as at 31 December 2008 increased significantly, reflecting the efforts made by the Administration.

**165.** Nevertheless there is still a certain number of disagreements and uncertainties weighing on the completeness, the existence and valuation of transfer liabilities

**166.** Certain disagreements and uncertainties originate in issues raised by the provisions of accounting standard 2 relative to the expenses.

### *a) Risks induced by the IT systems and the weakness of internal control*

**167.** The non adaptation of the IT *Palier LOLF* applications requires an extra-bookkeeping inventory of revenues and expenses to be matched for the year in the *Orchidée* application for end-of-period reporting transactions. Despite the technical improvements of the tool in 2008, the multiplicity of end-of-period records and corrections recorded directly in accrual accounting makes the audit trail impracticable and the performance of basic auditing procedure essential for the auditor. An analysis must be conducted in the development of the Chorus project in order to solve those shortcomings due notably to the design of a specific management and recognition module especially for transfer liabilities.

**168.** The auditor cannot sufficiently rely on the procedures of internal control.

**169.** On the one hand, the proper application by all the offices managing the inventory methods defined by the central administration is not sufficiently controlled. Thus, significant deficiency in completeness and accuracy was still found by the Court in certain mechanism managed by local units (Central Government subsidies to social housing agencies, stipends and bonuses for secondary education, overall allocations of equipment to municipalities and rural development, subsidies for various work of local interest). They have led to corrections in an amount

exceeding €1bn.

**170.** On the other hand, the procedure for reconciling reciprocal debts and receivables implemented by the preparer of the financial statements in 2008 is not yet satisfactory. The differences resulting from that are neither substantiated nor usable. The reconciliation procedure further is only related to social security agencies and implementing partners with stakes which exclude some major third parties such as international agencies or beneficiaries of direct Programme expenditure (RFF, SNCF, RATP).

*b) The commitments of the Central Government to the French Railway Network Company (RFF)*

**171.** The Central Government participates through subsidies in the financing of *Réseau Ferré de France*, which owns and manages the French railway network. The commitments of the Central Government with respect to RFF, about which the Court had noted the insufficient reporting in the financial statements for the previous year, are no longer noted as at 31 December 2008, as required by the accounting standards applicable as at that date.

**172.** A contract of agreed objectives with an entity is not sufficient in and of itself to establish the existence of commitments by the Central Government that have to be provisioned in the financial statements thereof. Only a review of the clauses of the contract and of all the context elements may lead, based on a set of indicators, to a conclusion that such need exists.

**173.** The performance agreement signed in 2008 and running over several years sets for the RFF ambitious objectives for the sustainable development of railway transportation which are part of its public service mission.

**174.** The signing of this contract is accompanied by an overhaul of the intervention scope of the Central Government through a new operating subsidy instead of the various subsidies paid until then. This subsidy, which is in fact, recorded as a Programme expenditure in the accounting of budget operations, presents features of a Programme expenditure with respect to the Government accounting standards.

**175.** Indeed, the Central Government exercises in this case its mission of economic and social regulator. The payments made to RFF are intended to offset the amount that is insufficient from tolls paid by the users of the railway network to RFF. The limited amount of those tolls is set by the Central Government so as to make the level of tolls collected by the public company acceptable for the user of the network and to

foster competition in this sector.

**176.** It has not been found for the Central Government any recognised and significant counterparty of an exchange revenue to this subsidy whose indirect beneficiaries are the publicly-traded railway operators. This is therefore a transfer related to a good and a collective service in the sense of international public accounting categories which in light of Government Accounting Standards 2 and 12 must result in a provision in the case of commitments running over several years.

**177.** The industrial objectives assigned to RFF can only be achieved with the financial support of the Central Government. The latter will pay the subsidies intended to offset the insufficient exchange revenues in accordance with a business plan running over several years (commitments 20 and 21 of the performance agreement). These factors establish the existence of a commitment by the Central Government, which is reasserted, explained and outlined in aforementioned contracts and its financial schedules.

**178.** Failing to pay the subsidy by the Central Government over the coming years will most certainly affect the continuity of the operations of the public company for which trade revenues do not constitute a sufficient guarantee. The assumption of a breach in the continuity of operations of RFF is not something that the Central Government can contemplate. The likelihood of outflow of sources related to this commitment is therefore not disputable.

**179.** The amount of this outflow of sources can be estimated reliably for the next three fiscal years, as also defined within the framework of the planning law of public finances running over three years. It totals €6.8bn. Over a longer term, the opening of the competition to the transport of travellers does not make it possible to measure the commitment of the Central Government with sufficient reliability.

**180.** All the conditions necessary for provisioning the multiannual commitment of the Central Government to RFF were therefore, in this case, met as at 31 December 2008. The failure of the Administration to take into account the adjustments proposed by the Court as a correction of errors to account for the prior nature of the commitments of the Central Government results therefore in recording a disagreement.

*c) Inventory of other liabilities related to Programme expenditure*

**181.** The numerous irregularities, uncertainties and limitations noted by the Court prevent it from obtaining reasonable assurance as to the completeness, existence and accuracy of liabilities related to Programme expenditure inventoried as at 31 December 2008.

**182.** The “offsetting payment” by the Central Government to the National office of forests as part of the management of the rural districts forests is recognised as a subsidy for public service expenses. It presents however an occasional and partial nature which does not correspond to the definition of such a subsidy. The final beneficiaries are local authorities. There is no equivalent, recognisable counterparty that could indicate an exchange. This payment therefore corresponds, according to the Court, to the definition of a transfer expense. The Central Government’s commitments running over several years (€0.4bn) should have been recorded in a provision.

**183.** The payments for development and debt reduction contracts (€0.4bn) are not yet recognised in accordance with their nature.

**184.** Lastly, there remain uncertainties as to the obligations running over several years to be inventoried under payments to international bodies, a portion of which, the non-repayable aids, should be recognised as a transfer expense..

**185.** The external auditor was not in a position to collect audit evidence enabling it to obtain assurance, within the time frame necessary for its audit, regarding the proper measurement of the obligations relative to the employment support mechanisms managed by CNASEA (€0.2bn).

**186.** Certain contractual commitments of the Central Government are not recorded as off-balance sheet commitments while they correspond to the definition of potential liability. This is the case of the commitments made under the global partnership against the proliferation of weapons of mass destruction, on which the Court has brought the attention of the preparer of the financial statements for several months. The disagreement involves an amount ranging from €0.4bn to €0.6bn.

*d) Application of accounting standards*

**187.** The interpretation by the preparer of the financial statements of the provisions of Government accounting standard 2, which at this time is insufficiently stabilised, is at the root of significant disagreements or uncertainties concerning the completeness of the inventory of the transfer liabilities of Central Government. The minister in charge of public accounts further made the commitment to notify the public accounts standardisation council to address this issue.

**188.** The commitments made by certain so-called ‘transparent’ mechanisms on behalf of the Central Government must be listed in the accounts of the latter. When a transfer mechanism is qualified as “non transparent” the commitments made by the entity that is in charge of it must be recognised in its own financial statements. Yet the commitments running over several years carried by the National association for research (ANR) (€1bn) were not recognised in the financial statements thereof or in those of the Central Government. An uncertainty remains also on the accounting processing of the ANR Funds not paid to the final beneficiaries (€0.5bn)

**189.** The subsidies paid to local public learning establishments (EPLÉ) for the remuneration of education assistants are recognised at up to €1.3bn as charges related to Programme expenditure, while they are used to cover the cost of salaries and therefore should be qualified as subsidies for public service expenses. The current status of the EPLÉ, which are not Central Government implementing partners, does not allow for this.

**190.** The commitments of the Central Government relative to a large number of social aid measures managed by the Social Security agencies are not listed. Certain mechanisms (allocation to disabled adults, housing aid, special solidarity allocation, retirement pension equivalent allocation) are based on individual decisions, likely to continue over several years, subject to periodic audits. The Court considers that they should result, on a case by case basis, in the recording of provisions for charges or off-balance sheet provisions.

*e) Conclusion*

**191.** The weaknesses of the internal control and IT systems did not make it possible to note in 2008 all the improvements expected in the pathway to increased reliability of the Central Government's transfer liabilities.

**192.** For the third consecutive year, the disagreements and uncertainties noted by the Court do not allow it to express an opinion with reasonable assurance on the completeness, the existence and the measurement of transfer liabilities as at 31 December 2008. Therefore, the substantial qualification on the liabilities related to Programme expenditure must be maintained.

**193.** The actions aiming at raising the reliability of the inventory and recognition of those liabilities must be continued and reinforced. The reconciliation of reciprocal debts and receivables must be extended to all the principal third parties benefiting from transfers. The Central Government must be able to draw all the accounting consequences of the commitments to those third parties, including and particularly RFF. A correct appreciation of the roles of the Central Government and the entities managing the transfer initiatives is, in addition to that, necessary for a complete provisioning in their respective accounts of the commitments resulting from those.

## 7 - Real estate holdings

**194.** The Court had expressed a substantial qualification for the 2006 and 2007 financial statements on the real estate holdings.

**195.** The net book value of the Central Government's real estate holdings and buildings in service shown in its accounts at 31 December 2008 is €62.4bn. For the most part, this measurement is based on market values except for certain atypical properties (properties with a small or very large surface, special military facilities, etc.) due to the lack of measurement references compared to the market. Buildings classified as historical and certain special real estate properties whose use by third parties is only possible if major modifications are made are measured at a symbolic amount of €1. Other properties such as penitentiary institutions are measured at their depreciated replacement cost.

**196.** Following the uncertainties noted on the 2006 and 2007 financial statements relative to the completeness of the inventory of the real estate holdings and their measurement, the Administration had made several commitments. Those pertained among other things on defining the priorities of an inventory of properties, valuation methods, measurement of the holdings abroad and that of the penitentiary holdings, finally, clarification of the rule applicable to "further" expenses.

**197.** Real efforts have been made by the Administration with respect to clarifying the accounting instructions, the roll-out of the *Chorus* real estate module or the measurement method at the depreciated replacement cost for the penitentiary holdings, as requested by the Court. However, some of the commitments made were only partially kept and the valuation of the real estate holding still does not comply with the applicable standards.

### *a) The quality of the accounting tools for the recognition of holdings*

**198.** The inventory and valuation of the real estate holdings depends on the keeping of the General Table of Central Government's Properties (*TGPE*). The actions engaged by *France Domaine* in 2008 made it possible to continue on the road to increased reliability of the information contained therein. For all that, the previous findings, relative to the limitations inherent to this tool, are renewed in an even stronger manner in 2008.

**199.** The limited number of automated controls and the absence of an interface with the tools for expenses and accrual accounting require the implementation of multiple new adjustments and manual controls which

are very difficult to audit and result in uncertainty. The annual changes in fair value assets are recognised as a revaluation differential which increases the net position of the Central Government. The Court has not been able to validate any of the adjustments of the data issued from the STGPE to establish this revaluation differential recognised in the amount of €2.4bn.

**200.** In addition, the well-founded nature of the error corrections for previous years which were made for close to €2bn in absolute value as at 31 December 2008 was not possible to verify, due to the lack of precision of the descriptions of the entries concerned or for lack of documentation in the work-files

**201.** Without denying the progress that will represent as from 2009 the roll-out of the Chorus real estate module, RE-FX, the Court notes that this tool will remain tributary to the quality of the input of data. The need to continue on the path to increased reliability of the inventory and measurement procedures is only made even more pressing by that.

#### *b) Valuation procedures*

**202.** In accordance with the commitments made, a number of properties not valued in 2005, 2006 and 2007 underwent a valuation in 2008. The Court however notes that close to 7% of properties were yet to be measured at the end of 2008, 4% having never been subjected to any valuation since they first became part of the Central Government's holdings. The correction recorded by the preparer of the financial statements in order to reduce the scope of the uncertainties resulting from that totals €1bn. However it is only based on a flat rate and overall calculation which cannot substitute for a reliable valuation.

**203.** In addition, the accounting instructions had stipulated that the properties for which works that can be capitalised have already been checked and signed or whose surface has materially changed should be subjected to an on-site valuation. Yet, close to 3% of property concerned was valued through the discounting method which distorts their market value. In fact, discounting the market value does not take into account the surface of a property. The changes in surface not taken into account reach 96,634 m<sup>2</sup> out of a total in absolute value of 353,830 m<sup>2</sup>.

**204.** In addition, for lack of timely availability of accounting guidelines on the implementation of the new method for the valuation of the penitentiary holdings, the Court was unable to express an opinion with reasonable assurance on the correcting entries recorded for close to €1bn in absolute value or on the balance of the account of these special buildings which totals €8bn.

*c) Inventory procedures*

**205.** The completeness and the reality of the inventory of the real estate holdings are not always guaranteed. On the one hand, the reconciliation work of the land registry database and those of the STGPE should enable the external auditor to collect the evidence attesting to the completeness of the properties inventoried. Interrupted in 2007, this work has been definitively abandoned. On the other hand, the audits carried out by the Court revealed irregularities in the inventory of properties controlled by the Central Government (properties controlled by the implementing partners or valued wrongly at their market value).

**206.** The completeness of the provisions for asbestos removal which are recognised at the close of 2008 has not been shown. On the one hand, the entire Central Government real estate holding has yet to undergo “asbestos technical diagnosis” while Decree 96-97 of 7 February 1996 had required to do so prior to 31 December 2005. On the other hand, the audits conducted by the Court have not enabled it to establish the link among those documents, when they do exist, and the provisions that they are supposed to substantiate, due to the shortcomings of the audit trail.

**207.** The Ministry of Culture has carried out a valuation of the amount of the works necessary for the maintenance and the preservation of monuments classified or recorded in the inventory regardless of whether they are the property of the Central Government or whether the Central Government has the obligation to substitute itself for an owner in default. The result is a total amount of €10.7bn which is related to a significant deterioration of the state of preservation of the national heritage. The provisions booked to that effect by the preparer of the financial statements total €0.3bn. The supporting data needed were not produced for the auditor to be able to express an opinion with reasonable assurance on their completeness.

*d) Compliance with Accounting Standards*

**208.** According to Government Accounting Standard 6, “further expenses” (repairs or maintenance expenses for the purpose of restoring or maintaining the real-estate holding potential for service) must be accounted for as expenses, except if there is impairment loss associated with a reduction in the potential for service which was previously recognised. Even though the provisions of the standard call for clarification for easier application, the public accounting standards committee confirmed their applicability in 2008. The Administration does not apply the principle of recognising a charge of impairment value

related to the decreasing potential for service and as a result a significant portion of works has been wrongly capitalised in material amounts as at 31 December 2008.

**209.** Government Accounting Standard 6 stipulates annual recognition of a charge that is supposed to measure the real estate holdings use of the potential for service. This charge totals, in the Central Government financial statements, €2.2bn as at 31 December 2008. The charge is thus offset in the amount carried forward for each year contrary to the fundamental principles of the accrual-based accounting. In addition, the calculation methods used are heterogeneous. On the one hand, the utilisation charge is calculated as a holding cost (based on the Government bonds yield). When conversely the property under consideration is included in the scope of budget rents, the valuation of such rents is the method applied. The result leads to inconsistencies in the application of the standard in this respect.

*e) Conclusion*

**210.** The pathway to increasing the reliability taken in 2006 and 2007 was not properly followed. The low level of auditability of the recognition tools used for the real estate holdings, the insufficient procedures of valuation and inventory and the persistence of disagreements on the application of the accounting standards or difficulties of interpretation make again weigh an uncertainty on the completeness, the actuality and the valuation of the real estate holdings recorded on the balance sheet of the Government as at 31 December 2008. Consequently, a substantial reserve must again be expressed regarding the real-estate holdings.

**211.** Three types of progress need to be made as early as in 2009:

- The roll-out of the *Chorus* real-estate module should make it possible to meet the concerns expressed by the Court regarding the auditability of the recognition tools ;
- The valuation and inventory procedures will have to be improved and effectively applied ;
- Accounting treatments in compliance to the applicable standards will have to be defined and applied regarding the lower potential of service expected from the real estate assets and their working load

## **8 - Other end-of-period reporting of assets and liabilities**

**212.** The Court expressed on the 2007 Central Government financial statements a qualification relative to the completeness and the valuation of several assets and liabilities items listed on its balance sheet.

### *a) End-of period reporting of fixed assets and inventories of civil ministries*

**213.** Tangible and intangible fixed assets, excluding real estate holdings and roads and the inventories of civil ministries, represent €19.6bn at 31 December 2008 (€15.3bn excluding business accounts, ancillary budgets and fixed assets in progress).

**214.** The *CISIS software* application combines the electronic files of all the ministries, exclusive of the ministry of defence, for up to €4.2bn in gross amounts (€2.2bn net). It should make it possible to substantiate the balances listed in the books.

**215.** Yet, the inventory of fixed assets in CISIS is not exhaustive. Thus, none of the software acquired is listed in it. The equipment of the central unit of the judiciary police and those of the RAID are not retraced in it, while progress has been recorded for the other services of police and civil safety. The cultural properties of the ministries are not inventoried except for those of the ministry of Culture.

**216.** The scope of inventories included in the application is incomplete. Eight ministries, some of which presenting high financial stakes, do not declare any inventory. The inventory declared by the other seven ministries is not exhaustive. These gaps result from various omissions (10% of the munitions of the Home Ministry, all the replacement parts of the DGDDI, etc.) or the application of unjustified reporting thresholds.

**217.** The valuation of inventories presents multiple weaknesses and global substantiation deficiencies. No ministry, except for the Ministry of Agriculture, writes down its inventories. Contrary to the provisions of the Government Accounting Standard 6, the depreciation schedules applied do not correspond to the probable useful lives of equipment.

**218.** Neither balances nor flows recorded in the accrual accounting application CGL can be reconciled to the movements and the data inventoried in the CISIS database. The accounting flows exceed the

acquisitions partially inventoried in CISIS database. The partial sales of lots are not translated into the accounting system while they are recorded in the inventory data. The adjustments made in CGL do not generate any simultaneous correction of the end-of-period database.

**219.** The resulting differences (€0.6bn) are material for the balances considered (€4.7bn). They are not substantiated in the year-end file provided by the preparer of the financial statements.

**220.** As a result due to the irregularities noted by the Court and lack of consistency between the end-of-period reporting database and the Central Government accounting there is an uncertainty as to the completeness and the measurement of the fixed assets and inventories of the civil ministries as at 31 December 2008.

*b) Unallocated tangible assets*

**221.** Fixed assets that are not subjected to an end-of-period reporting are combined under unallocated accounts. They concern a large number of assets whose unit value is low (furniture and office equipment, computer and telecommunications equipment, certain machinery and technical equipment, etc.). They are listed on the Central Government's balance sheet as a gross amount of €10.6bn (€4.4bn net).

**222.** The uncertainty expressed about the unallocated fixed assets for 2007 referred to their low valuation and their accounting treatment. The Administration had made a commitment to expand the portion of assets subjected to an end-of period reporting, to overhaul the follow-up framework and to recognise the unallocated fixed assets and to attempt to achieve a gradual settling of the accounts pertaining thereto. As at 31 December 2008, this commitment had yet to be met.

**223.** Despite the efforts made in terms of inventorying the fixed assets of the Ministry of the Interior, the unallocated fixed assets still represent close to 63% of the gross fixed assets, Defence excluded. Their recognition is not compliant with the Government accounting standard and it is not based on an end-of-accounting-period reporting.

**224.** Certain charges to unallocated fixed assets accounts have the sole purpose to clear the differences between accounting balances and electronic end-of-period files, regardless of the nature of the assets concerned.

**225.** Consequently, the Court cannot withdraw the finding of uncertainty expressed on the valuation of the unallocated fixed assets for the previous year.

**226.** The end-of-period reporting of these fixed assets must be significantly expanded in 2009 so as to accelerate the settling of the accounts concerned. The recognition of unallocated assets, as needed, as part of a management by lots, must be specified in accordance with the provision of the accounting standards. Unless it finds a quick reliability building of their follow up, the Court considers that the accounts in question will have to be expensed.

*c) Internally produced software*

**227.** The Court had expressed an uncertainty for the 2007 accounts regarding the estimate of software produced internally on the balance sheet of the Central Government. Since then, their gross amount recognised has practically doubled and as at 31 December 2008 it totalled €1.1bn, including 0.7bn for the “financial” Ministries. This amount corresponds on the one hand to personnel expenses that can be capitalised and to indirect costs taken into account in the measurement of those assets (“capitalised external costs”).

**228.** The system for monitoring internal hourly costs are characterised by their great heterogeneity and lack of interface with the various accounting applications. There is no reasonable assurance on the completeness and consistency of the time data reported in the accounting systems. Moreover, the average cost making it possible to value those internal hours is very often determined globally without differentiating by category to which an agent belongs.

**229.** Numerous deviations have been noted between the software produced internally by each ministry, as listed in the end-of-period reporting and in the accounting balances.

**230.** The accounting processing irregularities detected by the Court concerning capitalised indirect costs reflect the persistence of a defect of distinction between charges and fixed assets.

**231.** All these factors lead the Court to maintain the findings of an uncertainty on the completeness and the valuation of the software produced internally on the Central Government’s balance sheet as at 31 December 2008.

*d) Co-Financing of fixed assets*

**232.** The co-financing of fixed assets of which benefits the Central Government refers to primarily the fund for participation in construction, equipment and operation of the national highway network. Accounting Standard 6 provides for their recognition as unearned income. Their

amount must be included in the income statement at the same rate and duration as for depreciation of fixed assets to which they pertain, if applicable, or otherwise over a ten-year period. Unearned income recognised in this manner in the liabilities of the Government's 2008 year-end balance sheet stood at €2.2bn.

**233.** In 2008, the treatment applied to these liabilities and their reversal through income remained contrary to the standard. Unearned income is recorded on a basis devoid of relation with the date of placement in service of those fixed assets. The result is a non-quantifiable undervaluation of the corresponding liabilities.

**234.** An accounting treatment in accordance with Standard 6 must lead to recording under unearned income the amount of contributions which correspond to tangible assets not entirely put into service, and for those put into service but not fully depreciated, the portion of the contribution which was not recognized in income.

**235.** Aware of the major difficulties that such treatment entails, the Court had proposed to the Administration to adopt an intermediary solution : Apply the provisions of Standard 6 to the investment operations placed in service on or after 1 January 2006; preserve for older transactions the fixed-amount method currently applied. The Administration has indicated that it would apply this solution during the 2009 fiscal year.

**236.** The Court reiterates its finding of an uncertainty as to the amounts of unearned income listed on the balance sheet under co-financing of fixed assets and regarding the balance of their inclusion on the income statement as at 31 December 2008.

|  
*e) Conclusion*

**237.** The uncertainty noted in 2007 on the inventory, valuation and accounting treatment of several material assets and liabilities has become greater. Therefore, the Court expresses a substantial reserve on the other end-of-period reported assets and liabilities.

**238.** It is important to attribute to the framework and the methods of monitoring of the fixed assets and inventories of all the ministries, as from 2009, a higher level of priority to that that had been given thereto to date.

## 9 - Social debt redemption fund

**239.** The social debt redemption fund (CADES) was created in 1996 in order to finance and extinguish the debt accumulated by the general Social Security system through resources that are allocated specifically to it. It is included with the participations of the Central Government as a non-controlled entity with a zero acquisition costs, as its liabilities are greater than its assets.

**240.** An in-depth review of the non-controlled entities justified by the financial crisis and the recent legislative measures concerning the general Social Security system leads the Court to estimate that unlike the Retirement pensions reserve fund (FRR), the old-age solidarity fund (FSV) and all the agencies that contribute to the financing of the general Social Security system, CADES, an agency for the redemption of the social debt should be reclassified as a controlled stake, but not as a Central Government's implementing partner.

### *a) The controlling criteria according to Accounting Standard 7*

**241.** Under Government Accounting Standard 7, which applies to the Central Government's participations, an entity with separate legal personality and on which the Central Government exercises its right is considered as controlled if at least one of the criteria relative to the power of control and at least one of the advantage or risk criteria are deemed met, "unless there is another factor establishing without equivoque the existence of control".

### *b) Criteria relative to the power of control*

**242.** All the criteria relative to the power of control enacted by Government Accounting Standard 7 are met, to which the administration does not object.

**243.** CADES is a national public establishment of an administrative nature, placed under the oversight of the Minister in charge of Economy and Finances and the Minister in charge of Social Security. Its board of trustees comprises six members appointed by decree, including five representing the two aforementioned ministers. This board of trustees is the governing body of CADES. In addition, its proceedings regarding the budget and the financial account are subject to the explicit approval of the aforementioned ministers.

**244.** Through its representatives, the Central Government is able to gather the majority of the voting rights at the meetings of the board of trustees.

**245.** Finally, the Central Government holds a power of control over CADES by virtue of explicit provisions. Indeed, the public establishment is placed under its oversight. Its borrowings, whose plan is decided by the board of trustees, are subject to the approval by the Minister in charge of Economy and Finances.

*c) Advantages and risks criteria*

**246.** While, for an entity such as CADES, the advantage criteria make little sense, the criteria relative to risks are met.

**247.** CADES was created in 1996 by order ratified by the Parliament and subsequently amended several times by simple law or by constitutional bylaw. Law 2004-6810 of 13 August 2004 relative to health insurance set its term: Extinguishing the missions of redemption of the debt that had been transferred to it. The legislative nature of CADES does not for that deprive the Central Government of the power to make it cease its activities. While the decision to make it discontinue its activities is not within the prerogatives of the preparers of the financial statements or of those of the Minister in charge of signing the Central Government financial statements, it is within the legislative power of Parliament, Central Government authority vested with the power to approve its financial statements.

**248.** CADES benefits from an allocated tax, the CRDS, instituted by the law on the financing of Social Security for 1997 and a tax basis equivalent to that of the CSG. The Central Government is required, in application of Article 20 of constitutional bylaw 2005-881 of 2 August 2005 relative to the law on financing Social Security, to accompany any transfer of debt to CADES of supplementary resources. This mechanism for the guarantee of resources played for the first time since the LOLF has become effective in 2008. The law on the financing of Social Security for 2009 and the decree of 19 December 2008 transferred to CADES the discharge of an amount of approximately €26.5bn of debt listed on the liabilities of the national funds of the general Social Security system and of the FSV. The Central Government had to thus allocate to CADES a portion of the generalised social contribution corresponding to 0.2 point taken from the FSV.

**249.** The debt transfers expected for 2009 and 2010 will again lead to bringing into play of the mechanism for the protection of resources. As long as the Central Government has not found the means to return the

general social security scheme to balance it will be difficult to assert that it is not responsible for generating the tax resources needed to cover the redemption of the social debt and that failing that it would cover itself a risk as a last resort.

**250.** Article 7 of the Order of 1996 places, in addition, the Central Government in a situation of having to cover any potential liquidity default of CADES: “if the forecasted annual revenues and expenses of the fund (...) show that CADES will not be able to meet all its obligations, the Central Government submits to the Parliament the measures that have to be taken to ensure the payment of the principal and interest on the dates planned”. In the event of significant contraction of the resources allocated to it, this guarantee would be called into play. In the event of insufficient cash, CADES will benefit of immediate access to liquidity from Agence France Tresor.

**251.** The Central Government finally has the obligation to ensure the solvency of CADES through the implied guarantee given to all the public institutions. This obligation is even stronger as CADES borrows on international markets.

**252.** With all these provisions it may be concluded that the Central Government is committed to CADES “provided that the latter is in business”. It is admittedly more difficult to show at a legal level that the Central Government should ensure a significant level of obligations “should the CADES activities stop”. However, it cannot be denied that, if applicable, the Central Government or one of its controlled entities would assume the obligations of CADES.

**253.** Standard 7 invites, in the event of doubt, to verify the existence of other control indicators. The most appropriate consists in verifying whether the “Central Government” has the ability to impose to the entity cooperation so as to attain its own objectives” For all the foregoing reasons combined, and principally because of the composition of the board of directors and the powers conferred to the ministers, the Central Government can impose on CADES unilateral decisions on the strategy and policy of the institutions, including its policy of issue, as did in fact show the two constitutional controls conducted by the Court since the creation of the public establishment.

#### *d) Context*

**254.** For the markets as well as for the ratings agencies, CADES is rated AAA because the Central Government is supporting it and guarantees its solvency and because it benefits from a guarantee of the tax resources allocated to it. The financial crisis enhances the responsibility

of the Central Government as a lender or an insurer or an implicit guarantor of last resort.

**255.** The author of the constitutional bylaws placed the rules of operation of CADES within the scope of the laws for the financing of Social Security, while differentiating it from the financing institutions and qualifying it as an agency for the repayment of the social debt. It did not however include it in the scope of consolidation of the branches of the general Social Security system. The inter-ministerial order of 27 November 2006 which set the rules for the combination with a view to preparing the combined financial statements of this general system excludes CADES.

*e) Conclusion*

**256.** The strict application of the accounting standards would lead to re-categorising CADES as a controlled participation. Such a re-categorisation, treated as the correction of a fundamental error, would result in a decreased total equivalent value of account 26 by €2.9bn in the opening balance of €7.4bn additional as at 31 December 2008.

**257.** Since the administration did not apply this adjustment, the Court notes a disagreement and expresses a substantial qualification.

**258.** . The resolution of this disagreement refers to considerations that go beyond the strict framework of accounting standards and concern the distribution of competencies and responsibilities of the Central Government and Social Security. A clarification of the intent of the legislator seems to impose itself in that respect, for an end to be quickly put to the current ambiguity which consists of placing CADES outside of the scope of the combination of the general system and the control of the Central Government. The Ministry for the Budget, Public Accounts and the Civil Service has made the commitment to “find a solution in agreement with the Court during fiscal year 2009”.

## **B.2. – Other qualifications**

### **10 - Cash accounts**

**259.** With regard to the certification issued on the financial statements of the Central Government for 2007, the Court made a substantial qualification based on deficient substantiation of certain balances composing the cash of the Central Government as well as the insufficient compliance with the accounting standards and quality criteria applicable to daily records.

**260.** Defined by Government Accounting Standard 10, the components of the Government liquid assets include assets items, such as bank funds and savings bank funds and liabilities items, which are composed principally of bank deposits from “Treasury Correspondents” (local governments, local public institutions, etc.). As at 31 December 2008, cash assets amounted to €46.1bn and cash and equivalent liabilities amounted to €67.5bn.

**261.** The administration implemented an ambitious action plan to respond to each of the irregularities noted by the external auditor. The progress made however is insufficient

*a) The liquid assets of local governments and local public institutions which do not have bank accounts with the Treasury*

**262.** The liquid assets of local governments and public institutions (CEPL) which do not have individualised bank accounts with the Treasury and whose cash flows are recorded in the Central Government books, stood at €32.8bn as at 31 December 2008.

**263.** In accordance with the applicable internal control systems, the centralising accounting areas must over the entire year adjust the cash assets of the CEPL with the Government accounts and ensure the audit trail for adjustments controls to be implemented.

**264.** The systematic structuring of those reconciliation statements constitutes, in fact, evidence needed to substantiate accounting balances and possible disparities found at the year-end for both the preparer and the auditor of the accounts.

**265.** The audits carried out by the Court on a representative sample of general cash accounts showed the lack of systematic structuring of audits performed and adjustments made. In the absence of a quantified and documented reconciliation statement, the ability of the auditor to express an opinion on the correspondence between the liquidities of the local authorities and the books of the Central Government is limited.

**266.** The review of the financial statements showing disparities and submitted by the accounting areas highlighted allocation errors between sub-accounts for an amount totalling as an absolute value €0.4bn. The inadequate quality of these statements and their lacking substantiation do not make it possible to identify in an exhaustive manner and within the time frame afforded the Court for its audit, the re-categorisation entries to be made as at 31 December 2008.

**267.** It emerges from these findings a limitation to the scope of the audits by the Court on the balance of the cash accounts of local authorities and local public institutions.

*b) The balances of clearing or suspense accounts  
related to operations of treasury correspondents*

**268.** Clearing or suspense accounts make it possible to follow up banking operations by Public Treasury correspondents which are pending at the fiscal year closing (mainly for technical reasons or because of insufficient funds). As at 31 December 2008, the balances of these accounts stood at €0.1bn in assets and €0.2bn in liabilities on the Government's balance sheet.

**269.** In order to substantiate the balance of accounts, it is necessary to manually consolidate, based on an interim statement of the balance as at the calendar date of 31 December 2008, all the entries made during the supplementary period (which ran from 2 January through 4 January 2009).

**270.** A significant majority of the centralising accounting areas did not produce the substantiating statements needed by the Court for expressing an opinion on the well-founded nature of the transactions recorded during the supplementary period.

**271.** Being unable to implement within the timeframe compatible with the certification mission any satisfactory alternative methods, the Court notes a limitation to the scope of the audit intended to obtain reasonable assurance on the accuracy of the balances concerned.

*c) The liquid assets of armed forces units*

**272.** The liquid assets of the armed forces units are recorded in the advance and related accounts which appear in the assets of the Central Government's balance sheet. As at 31 December 2008, the amounts recognised amounted to €bn.

**273.** The Ministry of Defence enjoys, indeed, the use of overriding budget and accounting procedures that allow it to forgo the normal circuit of performance/execution and controlling of expenses. Their reform, planned in 2008, experienced delays and their scope remained significant. In the qualification expressed in 2007, the Court had noted the absence of correspondence between the books of the Central Government and the cash position of the armed forces units and the insufficient substantiation documents produced to enable the Court to express an opinion with reasonable assurance regarding the accounts concerned.

**274.** At the completion of the audits of the 2008 accounts, these findings were reiterated, despite the efforts made by the preparer of the financial statements and the departments of the Ministry of Defence. A material unsubstantiated difference (€0.1bn, i.e., over 10% of the balance of the concerned accounts) remains at the 2008 year-end between the books of the Central Government and the cash positions of the armed forces units. This difference has even increased slightly compared to the previous fiscal year.

**275.** The administration had made the commitment, in 2007 and then in 2008, to reconcile the "cash to be reclassified" account, representative of unsubstantiated differences and opened as a clearing account under the 2006 opening balance sheet. As at 31 December 2008, this account still had a balance of €0.1bn.

**276.** The lack of adjustments between the accounting of the Central Government and the cash position of the armed forces units and the lack of substantiation for the differences found do not make it possible to remove the uncertainty on the accuracy of the balances on the advance accounts as at 31 December 2008.

*d) Daily Accounting Entries*

**277.** Major progress has been made in 2008 by the Treasury network in response to the uncertainties noted by the Court on the 2007 accounts with respect to the quality of the daily accounting entries.

**278.** Conversely, no improvement has been noted in terms of entries debited or credited to the bank account to which are posted the transactions of the accountants of the financial administrations (customs

and tax departments in charge of companies). This accounts records annually a cumulated flow in the amount of €15bn.

**279.** Contrary to the recommendations of the applicable financial reporting framework, bank statements are not systematically input in their entirety upon receipt. Accordingly, entries posted on accounting date D to the bank account retrace either the bank statement transactions of day D or the statement transactions of day D-1. They may thus involve older transactions. The sequence of operations has not been respected. Failing to take into account, on a daily basis, the events affecting the financial position of the Central Government results in a distortion, during the year, between this reality and the image provided by the books.

**280.** Certain Banque de France statements are recognised over the same day, without differentiating among the various categories of movements indicated on the statement, while the rule is to recognise them separately. In addition, the description attached to the accounting entries are too often vague. They do not make it possible to assess the nature of the transactions recorded or to identify the references in the supporting document substantiating them. The quality of the audit trail is not ensured and limits the scope of the audit performed by the external auditor.

*e) Conclusion*

**281.** The progress noted compared to fiscal year 2007 remains insufficient. The scope of the Court's audit with regard to the balances of certain cash accounts included in the Government's balance sheet remains limited. This concerns the liquidities of local public authorities and institutions that do not have an individualised bank account with the Treasury, the clearing or suspense accounts relative to transactions of the correspondents of the Treasury as well as the cash positions of the armed forces units.

**282.** This limitation is accompanied by continuing uncertainties regarding deficiencies in the quality of accounting records made during the year on the bank account to which are charged the accounting transactions of financial administrations.

**283.** Therefore, the qualification on the cash accounts cannot be removed as this year. The actions undertaken by the Administration must continue in 2009 to respond to all the insufficiencies noted by the Court over the past two years.

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## 11 - Other Central Government participations

**284.** The Central Government participations in International Organisations as at 31 December 2008 were €25bn, of which approximately half related to the IMF. The loans and advances are listed on the Central Government's balance sheet in the amount of €14.7bn, of which €10.7bn for loans granted at a preferential rate.

### *a) Review of the participations in International Organisations*

**285.** The review of allocations to International Organisations shows uncertainties relative to the absence of an audit trail. Nor the directorate general of the Treasury and economic policies nor the Ministerial accounting department ensure the monitoring of the accounting treatment of those payments, which are not subjected to an appropriate internal controlling mechanism. The result is a limited scope for the external audit.

**286.** The accounting treatments of participations held by France in International Organisations, other than the IMF, is not consistent with that of the other non-controlled entities whose acquisition value is frozen at the opening balance sheet amount, unless there is a change in the capital of the entity or as a result of an impairment test.

**287.** It perpetuates the practices preceding the establishment of the general account of the administration of the finances by cumulating budgetary flows without a preliminary analysis of their actual impact.

**288.** It does not comply with the keeping of an accounting system on an accrual basis. The payments are recognised on a cash basis while they should be recorded under liabilities corresponding to commitments made by France in the reporting of sources upon their generation.

**289.** It is not based either on a preliminary analysis of legal features of the international agency and its scope in order to verify whether the Central Government holds rights therein in light of Government Accounting Standard 7, or on a systematic review of the various types of allocations made by France.

**290.** The Treasury Department (DGTPE) acknowledges that approximately 10% (i.e., €2.5bn) of the amount capitalised can be treated as donations that should have been recognised as charges related to Programme expenditure. This incorrect allocation compromises in addition the exhaustive provisioning of Central Government's commitments running over several years with respect to International Organisations. The amount of €1.6bn "remaining to be paid" as at 31 December 2008 was not subjected to the analysis enabling it to distinguish capital allocations from non-repayable aid allocations.

*b) The weaknesses of the accounting treatment of the share of France in the IMF*

**291.** The accounting treatment of the transactions with the IMF entails an erroneous measurement of the participations held by France.

**292.** As at 31 December 2008, France's share totalled 10.7bn in DTS, i.e., €1.9bn. Banque de France carries in its account the share used by the IMF and the Treasury the unused portion in euros. Since the 2006 opening balance sheet, the claim held on the IMF has been retraced under assets as an equity investment, the debt of France in Treasury bonds being listed under liabilities in application of Standard 12.

**293.** However, the balance of the money-market transactions account is carried forward for the capitalised amount of the previous year, which is contrary to the notion of acquisition cost. This scheme overrides Government Accounting Standard 7. The latter stipulates indeed that non-controlled participations must be measured at their acquisition cost in the 2006 opening balance sheet, and then be subjected at each period-end to an impairment test. In the event in which the actual amount falls below the net asset value, impairment must be recognised. The accounting treatment applicable does not therefore lead to retracing the actual amount of France's share in the IMF.

*c) Allocated holdings*

**294.** The Central Government entrusts with intermediaries the management of missions of a general economic interest. Their transactions are combined within entities without legal personality that the Central Government outfits with initial cash, to which it subsequently contributes further. In exchange, it preserves the control over those assets. The rights available thereto under this must be posted to its accounts. A certain number of entities identified by the Court enter in its opinion in this category.

**295.** Substantial progress has been made in 2008. The Administration has made the commitment to complete the analysis, during fiscal year 2009, of all the holdings allocated to third parties (including Natixis, its subsidiary CFDI and *Crédit Foncier*) over which the Central Government has rights, with a view to ensuring their proper record in its accounts.

*d) The cost of subsidised loans*

**296.** The Central Government grants loans at subsidised rates as part of certain programmes with an international scope such as the public aid for development in favour of foreign Countries or national programmes such as the new cities programme.

**297.** Article 24 of the LOLF makes the possibility of the Central Government to grant such loans contingent on a decree by the Council of State. The author of the constitutional bylaws thus has intended to structure the agreement of this type of credit facilities.

**298.** Since 2005, the Court has been calling to the attention of the Administration the need to reflect in the financial statements of the Central Government the actual cost of subsidised interest compared to a loan extended at market rate. The Court has estimated this cost for the loans to foreign Countries alone to be between €3bn and €6bn depending on various assumptions.

**299.** Contrary to the situation prevailing in corporate accounting and for other major member countries of the OECD, the reporting standards of the Central Government do not allow for discounting the amount of the loans in the balance sheet or for recording a loss at termination. Government Accounting Standard 7 specifies however that net asset value of the loans and advances is equal to their current value. These provisions and the principle of proper disclosure should lead to reflecting in the notes to the financial statements the net asset value of those loans in order to measure their cost, which is, among other things, part of the public aid to development efforts.

**300.** The administration acknowledges the importance of such information, but the notes to the 2008 financial statements do not provide any general information as to the mechanism of subsidised loans.

*e) Conclusion*

**301.** It results from the foregoing an uncertainty and disagreement that lead the Court to expressing a qualification as to the measurement under the balance sheet assets of the equity investments that the Central Government holds in International Organisations to which the financial and economic crisis has attributed a growing role. The Treasury and Economic Policy General Department (DGTPE) has however suggested forming a working group including the Court that would make it possible to resolve within a short time frame the difficulties related to their recognition.

**302.** The refusal of the administration to quantify the cost of loans granted at a preferential rate constitutes a disagreement which could have been removed with a relevant disclosure in the notes to the financial statements.

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## 12 - Public service concessions

**303.** In the qualification regarding specific fixed assets for the 2006 and 2007 fiscal years accounts, the Court had noted a disagreement related to the lack of recognition of property built by the Central Government and placed under concessions prior to 2 January 2006.

### *a) Financial disclosure in the notes to accounts*

**304.** A table listing the concessions has been provided since 2007 in the notes to the general Account of the Central Government. It includes 464 public service concessions, including 402 in the hydroelectricity sector, 22 in the roads sector and 25 in the airport sector. For 2008, the notes present in addition an estimate of the replacement cost of the state-owned motorway network at up to €122bn.

**305.** This first valuation effort has started to improve the quality of the disclosures to the readers of financial statements. It confirms the material nature of the contracts under concession. It remains however partial and excludes among other things some material concession in the hydraulics, railway and airport sectors.

### *b) No recognition of the concession contracts under the Central Government's balance sheet*

**306.** In the Central Government financial statements, only assets recorded in the 2006 opening balance sheet or included in its holdings subsequently to that date are posted to the balance sheet (€0.1bn in 2008). As at 31 December 2008, their book value amounted to €0.3bn and pertained exclusively to road infrastructures.

**307.** The administration notes that the standards, for practical feasibility reasons, do not impose explicitly, in their current wording, the recognition of property under concession prior to the preparation of the 2006 opening balance sheet.

**308.** The method developed to value the road concessions in the notes shows however that it is possible to establish the depreciated replacement cost of highways built by the Central Government between 1971 and 2006.

**309.** The absence of recognition concerns more generally the underlying assets of the concession contracts through which the Central Government entrusts with a legal entity or an individual, the performance of a public service, at such entity's or person's risks and perils for a defined duration and, often, in consideration for the right to receive

royalties from the users.

**310.** However, the analysis of the concession contracts listed in the notes to the accounts shows a high level of control by the Central Government over the property under concession for the entire duration of the agreement.

**311.** The investment policy is decided by the Central Government. The grantee does not have practically any margin for manoeuvre in this matter. The works are fully structured by the grantor, via *ad hoc* inspections. The “essential assets” (necessary for the operation of the service) generally constitute Central Government property from the beginning to the end of the contract.

**312.** The control of Central Government over holdings under concession is expressed over the entire term of the contract, by the obligation imposed on the grantees to update and regularly report the inventory of fixed assets. The grantees are required to return in good and usable condition the assets under concession to the grantor agency at the end of the agreement, which proves the existence of a material residual interest for the Central Government.

**313.** The properties under concession present all the features of a Central Government asset whose lack of recognition on the balance sheet leads to an uncertainty and impacts negatively the “true and fair view” principle.

**314.** In the context of important developments in the international accounting standards applicable to concession service contracts linking private operators to public entities, this topic is included in the work agenda for 2009 of the public accounts standardisation agency. The Minister in charge of public accounts has made the commitment that the representatives of his department will support the principle of recognition as Central Government assets those under concession regardless of the date at which they were franchised.

|  
c) *Conclusion*

**315.** The valuation of the principal motorway concessions which is listed in the notes constitutes a first progress. For all that, it did not remove the uncertainty on the lack of recognition in the accounts themselves of the assets underlying concession contracts from before 1 January 2006. The Court nevertheless duly notes the commitment of the Minister in charge of public accounts to support in 2009 the principle of recognising on the balance sheet the assets concerned before the public accounts standardisation council.

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### **III - Report on the audits of the 2008 financial statements**

#### **1 - Scope of the audit performed by the Court**

**316.** In accordance with the provisions of Article 58-5<sup>o</sup> of the LOLF, this chapter provides a report on the audit plan and performed by the Court in the certification of the Central Government financial statements for 2008.

**317.** The audits were conducted in accordance with the Code of Financial Jurisdictions, notably procedural rules governing the certification of the Central Government and Social Security financial statements (Articles R. 137-1 to R. 137-4) which require adherence to the adversarial principle and the principle of collegiality.

**318.** The audits were also carried out in accordance with the International Accounting Standards issued by the International Federation of Accountants (IFAC). However, since the Administration had been authorised, through a decision handed down by the standards committee on 11 December 2006 amending Accounting Standard 1 on financial statements, not to prepare pro forma accounts for the first two fiscal years, the Court was unable to compare the 2007 and 2008 financial statements with those of 2006 as required by international audit standards.

**319.** The audits were planned and performed to collect evidence regarding the accounts and the disclosures made in the notes to the accounts and evaluate the accounting principles applied and material estimates used in closing the Central Government financial statements, in order to obtain reasonable assurance that they did not contain any material misstatement.

**320.** The choice of audits conducted, including the assessment of inherent and control risks, was based on the professional judgment of the Court.

**321.** The choice of focus areas and sites to be audited is made during a planning phase which is prior to both stages of due diligences. This allows the updating or, if applicable, the identification of the risks of material misstatements in the financial statements. The audit work is divided into uniform subsets of the financial statements or “audit sub-cycle” and involves description of the risks identified at that stage and checks pertaining thereto, as well as the list of sites to be audited during the interim phase.

## 2 - Audit calendar

**322.** The Court has divided its certification mission into two phases. First, it performs “interim” audits during the course of the fiscal year, then “final” audits after the accounts are closed but before the definitive closing. The certification mission is an annual responsibility which is the subject of in-depth exchanges of information with the Administration.

**323.** The calendar for the preparation of the accounts is defined in the LOLF, which sets 1 June when the budget review bill is filed as the date by which are appended the General Account of the Central Government and the certification document. In Article 28, the LOLF in addition maintains a period in excess of the calendar year limited to a maximum of twenty days.

**324.** The schedule for the preparation of the budget review bill is a major constraint imposed on the Administration as well as on the Court. The time periods for drawing the Central Government financial statements do not make it possible either for the certifying officers or the accountants to proceed with controls giving the Administration the means to make the financial statements reliable, under satisfactory security conditions, particularly adjusting entries. For its part, the Court should be able to have a longer time period so as to extend the scope of its audit on an entity as significant and complex as the Central Government.

**325.** The provision at 6 March 2009 of a first stabilised usable balance is a step forward which nevertheless remains insufficient. In fact, the Court only had 20 business days to perform its final audits, which require the implementation of difficult procedures for receipt and processing of accounting data and for providing supporting documents produced by all of the Government departments.

**326.** It is indispensable to continue to make progress along two paths of loosening constraints of the schedule already discussed by the Court. The period in excess of the calendar year must continue to be reduced, as the Government committed itself. Over time, it should even be removed. Recourse for the second year to an interim closing of the accounts helped make the accounting entries more reliable, particularly the flows for the year. Its scope however will have to be expanded to cover end-of-period reporting transactions and the methods for the preparation must include a greater involvement of computers in order to lighten the burden of final audits. The closing accounting guidelines should also be submitted earlier in the year.

### 3 - Interim audits

**327.** The interim audit missions took place from September to December 2008. Their purpose was to evaluate the risk of material misstatements in the accounts on the basis of two series of tests. The first one was related to a correct application of accounting procedures; the second one, to the effectiveness of the internal control systems.

#### *a) The content of interim missions*

**328.** The assessment of the risk of material misstatements in an accounting area makes it possible to adapt the intensity of the final audits.

**329.** The interim audits were performed in the 15 “Ministries”, according to the sense of the term given in the Budget Act for 2008. These audits included a portion that was common to the whole Administration and a portion adapted to the accounting stakes applicable to each Ministry.

**330.** The transversal part pertained to the deployment of ministerial mechanisms for the control of accounting risks. It included notably the audit of internal controlling through ministerial mapping of accounting risks and their translation into Ministerial Action Plans. It also pertained to the implementation of the internal audit department within the various Ministries.

**331.** The second part had as a purpose carrying out in-depth controls of the procedures pertaining to the various audit cycles (notably off-balance sheet commitments and contingency provisions, intangible assets, tangible assets, other fixed assets and inventories, implementing partners, staff expenditure and retirement pensions, operating and transfer expenditure). These controls were conducted on the basis of a risk analysis specific to each Ministry.

**332.** The Ministry of Economy, Industry and Employment and the Ministry for the Budget, Public Accounts and the Civil Service were, in addition, the subject of audits which were appropriate for the procedures which they are solely responsible for (financial debt, financial futures, liquid assets, participations, sovereign revenues).

**333.** As far as the relations between the Central Government and the Social Security are concerned, the verifications made with the Ministry for the Budget, Public Accounts and the Civil Service involved taxes and surcharges allocated and accounting determination procedures. Examination of internal control of operations managed by Social Security

institutions for the Government's account, included in transfer and transfer transactions, were supported by verifications carried out by the Court in connection with the external audit of the financial statements of the General System of Social Security in addition to those carried out at Central Government Directorates.

**334.** A specific study concerning the accounting and financial system and the overall quality of the accounts of 52 Central Government implementing partners was carried out, valued at the balance sheet at €6.9bn. The Court also relied on the audits carried out by the Audit Mission of the Public Finance Department (DGFIP) (55 implementing partners valued at €3.3bn) and the general inspectorate of the administration, national education and research (20 universities turning autonomous as at 1 January 2009, valued at €2.9bn), as well as on the findings of the audit mission of the General Economic and Financial Control (concerning 99 implementing partners).

**335.** IT audits were carried out to assess the risks associated with certain components of the Central Government financial and accounting IT system. Were also audited: Version 1 of the CHORUS software package providing the management of expenses, accounting and non-tax receipts of four programmes in 2008; the DDR3 and SCR3 applications that ensure the keeping of the books of the non-centralising accounting areas of the Treasury and their centralisation in the Central Government accounts; the *Farandole* application (production of budget and accounting nomenclature). A follow-up on the audits of the applications of *Palier LOLF (ACCORD, NDL, NDC, CGL, TCC and infocentre INDIA)* was carried out.

**336.** Electronic analysis was also carried out on the data of the inventory and valuation tools of the real estate holdings (STGPE and TGPE) as well as on the reconciliation of budget data, payroll (the PAY and ETR applications), pensions (PEZ) and expenses (ACCORD, NDL) and those in the accrual accounting (CGL).

*b) Impact of the audits in interim missions*

**337.** At the end of the interim audits, the Court, based on Article R. 137-2 of the Code of Financial Jurisdictions, sent the Secretary-Generals of the Ministries, the Director general of the Public Accounting and the Directors of all directorates concerned, as applicable:

- 19 summary reports of the interim audits, including 313 points needing attention matched with recommendations;

- 15 statements of provisional observations with 210 recommendations or points requiring attention, resulting after *inter partes* proceedings in an accounting valuation note per Ministry.

#### 4 - Final audits

**338.** The planning and performance of the final audits were based on the 14 audit assertions for operating flows, account balances at the end of the period as well as the presentation and information disclosed in the financial statements.

**339.** The verifications were carried out essentially by means of tests concerning the details of operations and balances; the implementation of analytical reviews which consist in comparing the data of one fiscal year with another was rendered impractical in the majority of cases due to limited information concerning the 2006 and 2007 fiscal years, the first period of application of the Government accounting standards. Lastly, in numerous cases, the justifications for the accounts necessitated repeating the accounting controls from one end to the other.

**340.** The verifications carried out for the accounts of the Senate and National Assembly by external auditors designated for that purpose by the *Conseil supérieur de l'Ordre des experts comptables* and the due diligence with regard to the accounts of the Constitutional Council under the responsibility of its financial advisor were carried out according to the auditing standards. No material irregularity was brought to the attention of the Court.

**341.** The accounts of the office of the President of the Republic, included for the first time in the accounts of the Central Government, were subjected to a limited review by the Court at the time of the audit of the departments of the President's office. No material irregularity was noted in the accounting system implemented as at 1 January 2008.

**342.** An audit of the operations carried out by the financial authorities was conducted at the request of the First President of the Court of Accounts by experts designated by the *Conseil supérieur de l'Ordre des experts comptables*. No material irregularity was brought to the attention of the external auditor.

**343.** Computerised analyses of the data derived from accrual accounting were made on all of the accounts for managing the 158 centralising Treasury local offices. The aim of this audit is to collect evidence enabling the auditor to obtain reasonable assurance as to the

quality and integrity of the information derived from the CGL application.

**344.** Furthermore, specific audits were carried out in order to verify by means of a representative sample of expense operations, the validity of the accounting entry error rate coming from by the structured expenses control system and to identify the precise weight of material errors likely to make the accounts incorrect, as defined by the Public Finances General Directorate.

**345.** Despite the lack of a unique budgetary and accounting IT system, the Court was able this year to verify the inter-relation and the consistency of the three results submitted to the approval of the Parliament. The balance of performance of the finance laws for the year, the definitive amount of resources and expenses of cash in the cash flow statement and the accounting result so that the actual financial position of the Central Government can be understood as a whole.

**346.** The Court audited the quality of the financial disclosures made in the notes to the 2008 accounts.

**347.** At the end of the final audits of the Government's accounts for the 2008 fiscal year, 283 audit observations were issued, of which 148 were related to requests for changes in the Central Government financial statements, that is 12 more than during the course of the previous fiscal year.

**348.** The impact of 86 observations that were taken into account in a satisfactory manner by the preparer of the financial statements is as follows:

In €bn	Direction of the corrected entries		Net
	Improvement	Deterioration	
Balance of transactions for the fiscal year	1,8	-7.3	<b>-5.5</b>
Net position (excluding the balance of transactions for the fiscal year)	24	-3.2	<b>20.8</b>
Off-balance sheet entries	N/A	N/A	33.3
Reclassifications in the income statement	N/A	N/A	1.1

In ₪n	Direction of the corrected entries		Net
	Improvement	Deterioration	
Reclassifications in the balance sheet	N/A	N/A	6.5

**349.** The impact of 36 observations that were subject to a disagreement with the preparer of the financial statements is as follows:

In ₪n	Amendments requested	Amendments recognised	Variance
Balance of transactions for the fiscal year	-13.0	0.1	-13.1
Net position (excluding the balance of transactions for the fiscal year)	-82.6	0.3	-82.9
Off-balance sheet entries	4.6	0.0	4.6
Reclassifications in the income statement	5.0	0.2	4.8
Reclassifications in the balance sheet	5.5	0.1	5.4

**350.** The exchanges between the Court, the Public Finance General Directorate (DGFIP) and the main Central Government administrations involved were constant and intense. Discussions took place in the Committee for Exchange and Monitoring, jointly chaired by both the president of the inter-chamber “Execution of the Government Budget and Accounts” of the Court and the Head of the Public Finances General Directorate, and also in the technical group of this Committee. All of the Secretary-Generals presented their Ministerial Action Plan before the Committee.

**351.** The certification report (introduction, statement of findings, report on the audits conducted) submitted for comment to all the Ministries with regard to the part or parts concerning them and gave rise to hearing Secretary-Generals and central Administration Directors on 4

and 6 May 2009 before the inter-chamber group “Execution of the Government Budget and Accounts”.