

# Public sector asset management and accounting in France

## An overview

### 1. Definition of property assets in the public sector: the notion of “public domain”

The “public sector” in France:

- Central Government and related bodies (national public establishments, agencies, etc.);
- local Governments (municipalities, intercommunities, “départements”, regions, and related bodies);
- Social security.

That definition relies on national accounting standards (ESA 95<sup>1</sup>). Public companies, among those State-owned commercial companies, are sometimes encompassed in the public sector scope (e. g. the French Postal Service), but in management and accounting fields, the “public sector” usually refers in France to the three sectors described above.

As the Social security rarely manages significant property assets, this presentation will only deal with central and local Governments and their related bodies.

In French public law, property assets in the public sector are often<sup>2</sup> treated under the notion of “public domain”, which encompasses the possessions belonging to the State, to local authorities and to public institutions and allocated to a public utility. This public utility can result from an affectation to the direct usage of the individuals (as roads or public gardens) or to a public entity (often called “public service”), provided that the property was specially allocated to this purpose (as a university or a court).

This notion goes back up to the Ancien Régime period (before the French Revolution of 1789), but it recently evolved, with the adoption of the general code of the property of the public persons, which came into effect on July 1st, 2006.

The judge verifies these criteria when it is necessary to determine if the property is a part of the public domain. For example, in a famous decision in 1951, the French Council of State considered that a path had to be incorporated into the public domain because:

- on the one hand the State had allocated it to a public utility because of the presence in this place of an archeological site;
- on the other hand the authorities had put two posts and a chain in order to close the access to this path, what constituted a “special arrangement” realized specially with the aim of the affectation of the path to this cultural public utility.

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<sup>1</sup> European System of Accounts, 1995

<sup>2</sup> But not always : see page 3 developments on the private domain of public entities

The general code of the property of the public persons took back this notion, by specifying that the arrangement should be "indispensable" to the mission of public utility: it is a question of slowing down the evolution of the case law which tended to widen the public domain.

The status of the property belonging to the public domain can also result from a law qualification. It is the case of electro-magnetic waves, that the law of July 26<sup>th</sup>, 1996 placed in the "public domain of the radio frequencies" by entrusting the French Broadcasting Authority to allocate frequency bands.

The public domain refers to natural (maritime or river public domain) and to "artificial" assets.

1) The artificial public domain affected to the direct use of the public is constituted of:

- the road artificial public domain, constituted by ground communications, allocated to the general traffic of the public (main roads, municipal public road networks);
- the sea and river artificial public domain, constituted by seaports, works established in the interest of the sea navigation;
- the artificial public domain of the municipality, constituted by public markets, slaughterhouses, cemeteries, public washhouses, public walks, religious buildings belonging to the municipalities before the 1905 law of separation.

2) The possessions allocated to public utilities:

- the possessions specially fitted out to be adapted to the object of the service (buildings and related assets);
- works of defence (fortifications, naval and air bases);
- public works and installations of "Réseau ferré de France" (France Railroad Network);
- aerodromes allocated to the public air traffic.

The law regime of the public domain is characterized by:

- the "imprescribibility": impossibility for third parties to acquire a right on these possessions by prescription, that is by a prolonged ownership (the administration owner can claim its property at any moment even if a person is on the public domain for more than 90 years (in French private law the prescription arrives at the end of 30 years));
- and by the "inalienability" (the impossibility to resort against the public persons to the ways of execution of the private law, we can only ask to the judge for the payment of a penalty).

That is why, before being given up, the property of the public domain must be beforehand displaced, what supposes the preliminary disappearance of the affectation to the public utility or the intervention of a law.

The property belonging to the public domain cannot be given up, there is impossibility to expropriate the public domain as well as to establish right realities on those properties (subject to the administrative long lease created by the laws of January 5th, 1988 and July 25th, 1994).

We can however note real attempts of conciliations between, on the one hand, the will to protect traditionally the public domain and, on the other hand, the will today to value economically this last one. It brings even some to wonder about the utility to keep the principle of “inalienability” of the public domain. These questioning result from a variation of perception of the notion of public domain: formerly, zone to protect against the royal wastes, today, it appears as a wealth to run.

The possessions of the State, the local authorities and the public institutions which do not belong to the public domain, belong to the private domain of the public person, globally subjected to the regime of private law. The private domain of a public person is essentially constituted by three types of assets:

- the possessions which did not receive special arrangement;
- the possessions not allocated to the public utility;
- the possessions included in the private domain by legislative disposition.

## **2. Ownership**

For those items that are not mentioned above:

- primary schools (3-11 years) are owned by municipalities, “colleges” (12-16 years) are owned by the “départements” and “lycées” (16-18 years) are owned by the regions;
- universities assets are owned by the universities themselves (public persons with legal autonomy, e. g. agencies, that are controlled by the Central government);
- elderly person’s homes are private owned or, in some cases, owned by local Governments; hospitals are private or owned by dedicated public agencies;
- public libraries, water supplies waste water treatment plants and sewage systems, social housing are owned by municipalities;
- town halls , local administrative offices are owned by municipalities;
- surplus property awaiting sale, assets under construction, industry property are owned by municipalities.

## **3. Management**

Central Government property is managed by each ministry (e. g. assets of the ministry of finances are managed by the ministry of finances, assets of the ministry of foreign affairs are managed by the ministry of foreign affairs, etc.).

A coordination is being implemented through a new structure: “France Domaine”, which is a branch of the ministry of finances, without any legal personality.

“France Domaine” has for mission to estimate and sell the possessions, movable and real estate, belonging to the public domain or private domain of the public persons who decided on the transfer.

The revenues of these transfers are recovered by the governmental treasurer.

In the local public sector, assets are directly managed by local Governments.

## 4. Accounting

Following developments only concern the French Central Government. Local Governments apply French GAAP provisions, but a reflexion is under way to converge their accounting methods with Central Government’s accounting standards.

The land and buildings controlled by the Central government are very diverse in age and in nature. Their relationship to Central government property and their uses may be very different, and the same asset may have several uses.

Consequently, land and buildings are classified as specialised or non-specialised.

Non-specialised buildings are buildings that could be sold to other entities for ordinary use as offices, housing, etc., subject to limited remodelling. It is technically and economically feasible to sell these buildings. An amendment to the public property code should make the legal framework more flexible.

The following examples illustrate the notion of non-specialised buildings:

Ordinary buildings:

- Office buildings
- Residential buildings
- Warehouses
- Garages, etc.

Adaptable buildings:

- Heritage buildings housing or suitable for housing government services (e. g. the building housing the mint headquarters, government-owned buildings around the Palais Royal gardens, the Court of Auditors building, the Paris Courthouse, etc.)
- Police stations
- Technical facilities, etc.

Specialised buildings are buildings that cannot be used for ordinary purposes, such as certain historical monuments or sites.

### 1) Initial valuation

When the initial statement of financial position is drawn up, the general principle of valuation at acquisition cost can be applied to most Central government assets.

However, unlike a business, which has a precise and known start-up date, one of the special characteristics of the Central government is the permanence of its action. The time scale means that acquisition costs may be lost in the ancient past or meaningless. To overcome the lack of determinable acquisition cost, a valuation should be made and the market price can provide a recent indicator, even when it cannot be observed directly.

Once the first statement of financial position has been drawn up, the usual business accounting rules can be transposed for the initial valuation of the Central government's tangible assets, except in the case of roads, where the depreciated replacement cost is applied.

## 2) Rules for Subsequent Valuations

### 2.1) Assets with a Determinable Useful Life

The task is to determine beforehand the suitable depreciation methods and impairment tests for each asset category.

An asset is depreciated by a systematic allocation of the depreciable amount over its useful life. It should be possible to determine the useful life of the asset, which is measured by the consumption of the expected economic benefits from the asset through use that is limited over time. This makes it possible to calculate the depreciation amount as the difference between the initial value and a reliable estimate of the residual value.

This method is used for assets where the initial valuation is based on cost. It is also used for assets valued at their market value in the first statement of financial position when the market value is treated as an acquisition cost. Business accounting practices can be transposed directly to Central government accounting for certain types of assets (furniture, computer equipment, etc.), but they have to be adapted for some other assets, such as military equipment and roads.

As a general rule, assets are depreciated and impairment tests are conducted if there is evidence of a loss in value.

### 2.2) Assets with No Determinable Useful Life

When assets have a very long useful life that cannot be determined, an utilisation measurement is calculated to recognise the corresponding expense.

The measurement is called utilisation expense. It is determined on the basis of the market value of the assets and not derived from a depreciable amount. In addition to the difficulties in determining the useful life, the market value of very old assets shows that the residual value is very high in many cases.

Consequently, the depreciable amount cannot be determined, regardless of the useful life assigned to the asset.

This applies to non-specialised buildings carried at their market value.

The market value of the entire stock of old and recent buildings should be determined and recorded annually to ensure uniform treatment of the value of land and buildings and to calculate the annual utilisation expense. The valuation rules should be defined according to

the technical characteristics of the buildings (floor area, condition, etc.) and trends in the local market.

Positive and negative revaluations of land and buildings shall be recognised under the procedures set out in the relevant accounting standard, along with the annual utilisation expense.

The net selling price of an asset can be useful for the manager occupying the asset. It is a helpful tool for management knowledge, choices and discussions.

### 3) Position with regard to international and national private accounting standards

Under the terms of Article 30 of the Constitutional bylaw of 1 August 2001 on budget, the Central government's accounting standards comply with the general principles of business accounting, except for differences warranted by the specific nature of the Central government's activity.

The Standard on tangible assets is based on the French Accounting Regulation Committee Regulations and it is consistent with the French GAAP. When required by the specific nature of the Central government's activity or when they coincide with the French GAAP, the rules set out in the International Public Sector Accounting Standards (IPSAS) are applied in the cases described below.

The notion of control used in this Standard is the one recommended by the French National Accounting Council for defining assets (see survey report of 22 October 2002). This notion corresponds to the principle set out in IPSAS 17 and IAS 16 on property, plant and equipment.

The references are as follows for the specific points listed below:

The finance lease provisions refer French GAAP, and to IAS 17 and IPSAS 13 on leases, which stipulate recognition of the leased assets on the lessee's statement of financial position.

The cofinancing provisions draw their inspiration from the recognition rules for capital grants (French GAAP).

Assets covered by public service concessions are subject to the accounting measures set out in French GAAP.

The rules applying to the initial valuation for the first statement of financial position refer to the rules under French GAAP, except in the case of roads, which are valued at their depreciated replacement cost on the basis of data provided by the Highways Directorate at the Ministry of Public Works. This treatment is also used for the starting statement of financial position and for subsequent valuations.

Costs for dismantling and removing plant and equipment and costs for restoring the sites are treated with reference to the French GAAP.

The provisions on the initial valuation of assets in the starting statement of financial position comply with the general acquisition cost valuation principle set out in the French GAAP. The provisions on valuation of non-specialised land and buildings refer to IPSAS 17 (paragraph 23).

As a general rule, subsequent valuations of assets use depreciation and impairment tests in the event of a loss in value, in keeping with French GAAP.

The valuation of non-specialised land and buildings draws its inspiration from the alternative treatment allowed by IPSAS 17.

#### 4) Control criterion

The accounting standard on “tangible assets” sets out the requirements for recognising any of the property under the Central government’s control as assets. Central government assets consist of a set of rights and obligations carrying an economic value. An asset is a balance sheet item that has a positive economic value for the central government, meaning that it is a resource controlled by the government as a result of past events and that is expected to produce economic benefits in the future. Control over the benefits means that the entity has the ability to govern the benefits and that it bears some or all of the related risks.

The Central government controls a tangible asset because it controls its right to use it. For the purposes of recognition in the central government financial statements, control over the right of use is determined as follows:

- it is assessed on the basis of the existence of a right to the resource. Consequently, a tangible fixed asset is not recognised, even though the central government owns it, if it can be shown that the government can derive no economic benefit or service potential from the asset.
- obligations may arise from control over an asset, when it is certain or likely that this control will entail an outflow of resources for the entity controlling the asset. Bearing the main expenses related to ownership of the controlled asset proves the existence of an obligation, which must be considered as a presumption that control exists.

These criteria mean that the Central government recognises assets that it does not own in its financial statements, but it controls them and manages them (e.g. assets used under the terms of a finance lease).

The corollary to this is that the Central government financial statements do not recognise assets that the Central government owns, when other entities manage them and incur the risks and enjoy the benefits of ownership (e.g. conceded assets).

The control criterion is intended to make the central government’s financial situation easier to understand.

It means that assets and transactions are recognised when they have an impact on economic resources, obligations or service potential. Failing to recognise these assets would lead to understatement of the corresponding rights and obligations in the Central government’s statement of financial position.

Symmetrically, this criterion prevents recognition in the central government’s statement of financial position of assets controlled by other entities, when such recognition would lead to overstatement of the Central government’s rights and obligations.

Applying the control criterion solely to the central government could give a partial view of public assets if the criterion is not seen in a broader context. Understanding of the criterion requires a grasp of the distinction between direct control and overall or indirect control. The preliminary division of assets and liabilities between the Central government and other public

entities is made in the separate financial statements. It will be satisfactorily carried through in the steps towards consolidation.

## **5. Value added tax**

VAT is treated as an expense in the accounting books.

## **6. Resources for capital investment**

In the Central Government, the acquisition of assets, replacement buildings, refurbishments, renovations and new constructions are financed through the State's budget (appropriations). Investment and disposal are decided by the concerned ministry and the ministry of budget, and appropriations are provided in the Budget Act.

The same decision process is to be mentioned in the local public sector.