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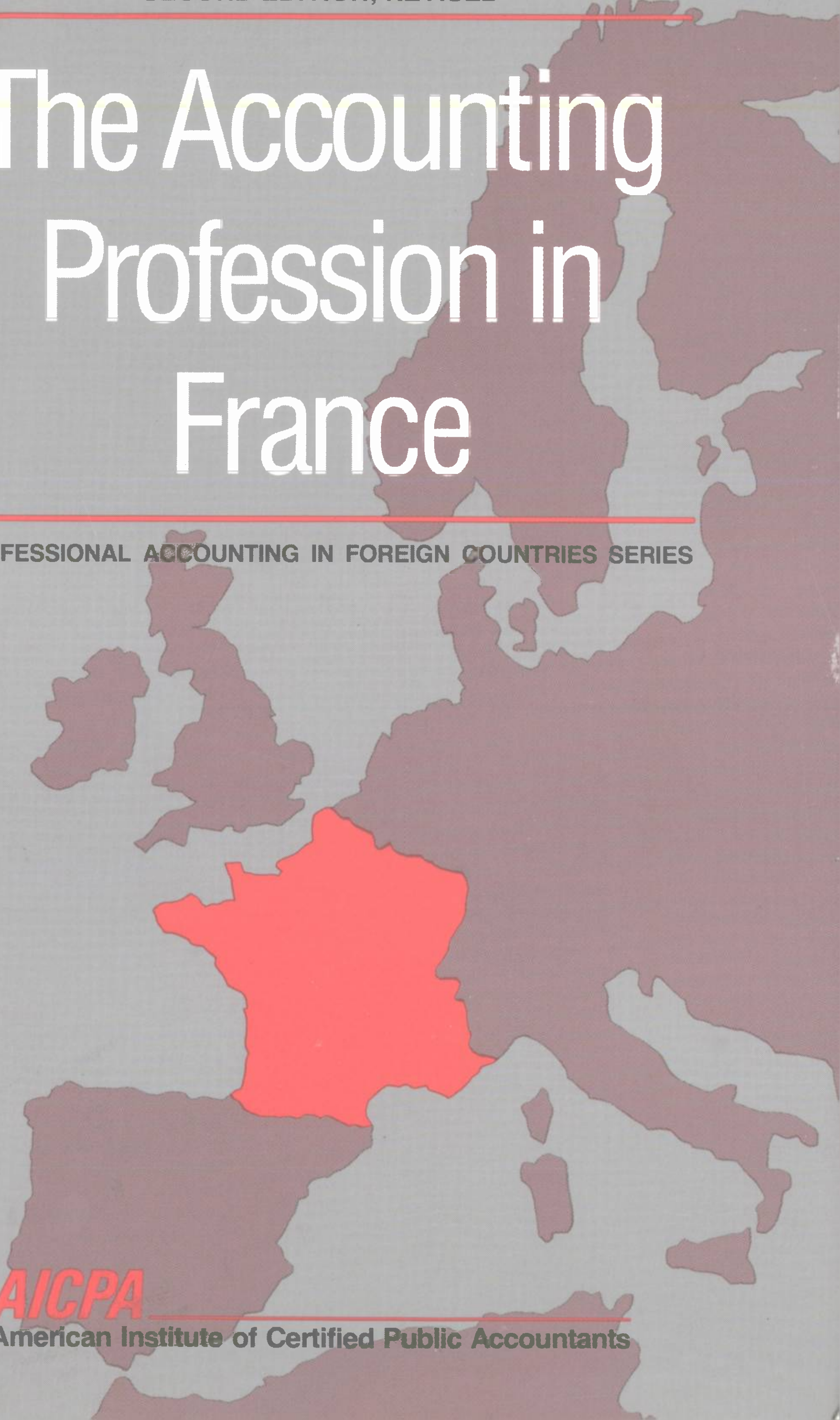
Accounting Profession in France, Second Edition Revised; Professional Accounting in Foreign Country Series

Guy Barbier & Associes

SECOND EDITION, REVISED

The Accounting Profession in France

PROFESSIONAL ACCOUNTING IN FOREIGN COUNTRIES SERIES



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American Institute of Certified Public Accountants

The Accounting Profession in France Second Edition, Revised
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NOTICE TO READERS

The Professional Accounting in Foreign Countries series is designed to be educational and used as reference material for the members of the Institute and others interested in the subject. It is not intended to establish standards.

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The Accounting Profession in France

PROFESSIONAL ACCOUNTING IN FOREIGN COUNTRIES SERIES

Prepared by

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Member Firm of Arthur Andersen Worldwide Organization

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Preface

This booklet is one of a series on professional accounting in foreign countries. The material is current as of March 1992. Changes after this date in the standards of either the United States or France may alter the comparisons and references detailed in this publication.

Included are descriptions of the accounting profession, auditing standards, and accounting principles in France. The booklet also presents brief descriptions of the various forms of business organizations, taxes, and requirements for stock exchange listings and securities offerings. Checklists comparing French auditing standards and accounting principles with those generally accepted in the United States are appendixes to the text.

This booklet is not intended to be a comprehensive discussion of auditing standards and accounting principles in France but is designed instead to focus primarily on differences from those of the United States.

John F. Hudson
Vice President
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Contents

1

The Accounting Profession

REQUIREMENTS FOR ENTRY INTO THE PROFESSION

Domestic Functions and Licensing Requirements

1. The accounting profession's position in France is notable because of its legal organization into the following two main bodies:

- The *Compagnie Nationale des Commissaires aux Comptes*, or CNCC (National Institute of Statutory Auditors), is the professional body of official statutory auditors and is under the authority of the *Garde des Sceaux* (Ministry of Justice).
- The *Ordre des Experts-Comptables et des Comptables Agréés*, or OECCA (Order of Accounting Experts and Qualified Accountants), includes all qualified independent accountants. The OECCA has both regional chapters and a national committee and is organized under the Ministry of Economics and Finance. Members of the OECCA are *experts-comptables* or *comptables agréés*. Presently, however, the qualification of *comptable agréé* is being phased out. Accountants working in industry cannot practice as *experts-comptables*.

These two organizations can be reached at the following addresses:

Compagnie Nationale des Commissaires aux Comptes
6 rue de l'Amiral-de-Coligny
75001 Paris

Ordre des Experts-Comptables et des Comptables Agréés
109 Boulevard Malesherbes
75008 Paris

2. The primary responsibility of *commissaires aux comptes* (statutory auditors) is to certify the regularity and fairness of the financial statements. Their duties are defined by law (*la Loi Sur les Sociétés Commerciales* of July 24, 1966, as amended), and they are appointed for a six-year period by a general meeting of shareholders. Although most *commissaires aux comptes* are *experts-comptables*, individuals cannot serve in both capacities for the same company.

3. A statutory auditor is generally an individual, but it can also be a firm. The latter may be any type of company: a *société anonyme*, or SA; a *société à responsabilité limitée*, or SaRL; or a professional civil company. For a firm to qualify as a statutory auditor, three-fourths of its capital and three-fourths of its shareholders and functions must be controlled by statutory auditors. In addition to *experts-comptables*, statutory auditors may include members of other professions, such as lawyers and engineers.

4. All statutory auditors are registered on the official list of each Court of Appeal. A statutory auditor may practice anywhere within French territory.

5. An *expert-comptable* (the equivalent of a certified public accountant, with the notable exception that he or she cannot perform a statutory audit unless qualified as a *commissaire aux comptes*) provides accounting, special auditing (for example, acquisition audits), taxation, financial, and general business services (including legal). His or her duties are based on a contractual agreement with the client. The *expert-comptable* may also act as a statutory auditor when listed as a *commissaire aux comptes.* Members of the OECCA generally are individuals, but may also be accounting firms in which the majority of the shares are held by *experts-comptables* acting in their own name or as a corporate body. *Experts-comptables* are licensed by the OECCA.

Foreign Reciprocity

6. Accountants qualified in foreign countries may be authorized to practice in France, as described in paragraphs 7 and 8.

*Admission to the List (*Tableau de l'Ordre*) of* Experts-Comptables

7. The following countries have signed a reciprocity agreement with France: Switzerland, Laos, and some French-speaking African countries (Congo, Senegal, Gabon, Republic of Centrafric, Chad,

Togo, and Algeria). Nationals of a European Community (EC) member country may be registered, provided they have a sufficient knowledge of French law, rules of ethics, and the French language, as determined by a special committee in France.

8. Other accountants may be granted an extraordinary revocable authorization to practice in France by the OECCA, without admission to the list of *experts-comptables*, provided that they demonstrate sufficient knowledge of French law, rules of ethics, and French language.

Admission to the Official List of Commissaires aux Comptes

9. Nationals of an EC member country or any other foreign country that allows French nationals to carry out the functions of *commissaires aux comptes* on its territory may be registered, provided they meet the minimum age requirement (twenty-five years), are of good moral character, reside in a region of jurisdiction that enables them to be registered on the official list of *commissaires aux comptes*, and have—

a. A foreign diploma considered to be equivalent to that of *commissaire aux comptes* or *expert-comptable*.

b. At least two years of auditing practice in which knowledge of French law and auditing regulations was required.

ROLES AND RESPONSIBILITIES OF STANDARD-SETTING BODIES

Professional Standards Promulgated by Each Body

10. The main bodies responsible for issuing standards are described in paragraphs 11 through 15.

Conseil National de la Comptabilité, or CNC (National Accounting Board)

11. The CNC is responsible for proposing solutions to theoretical or practical accounting problems. In addition to designing and updating the French general Chart of Accounts (*Plan comptable général*, or PCG) and professional Charts of Accounts (*Plans comptables professionnels*), the CNC advises on proposed accounting rules and recommendations made by the OECCA and other international accounting committees.

Commission des Operations de Bourse (COB)

12. The COB, comparable to the SEC in the United States, supervises the public issuance and trading of securities and the operations of the stock exchange.

13. The OECCA and the CNCC represent the French accounting profession in dealing with other international accounting bodies, such as the International Accounting Standards Committee (IASC), the International Federation of Accountants (IFAC), and the *Fédération des Experts-Comptables Européens.*

14. The OECCA issues recommendations on accounting and disclosure matters. The ethical rules and the organization of the OECCA are defined in the members' handbook (*Encyclopédie permanente*). Recommendations issued by the OECCA can be found in appendix B.

15. The CNCC issues standards (*normes*) and guidelines on auditing matters. A list of publications of the CNCC can be found in appendix A. Its main publications are the following:

a. *Normes et commentaires des normes*—includes all relevant information related to statutory audit requirements

b. *Encyclopédie des controles comptables*—reports on more detailed and practical auditing matters (specialized guides by activities)

c. *Notes d'information*—booklets that deal with particular aspects of auditing: reporting (*rapport général* and *rapport spécial*), evaluation of internal control, direct confirmation, physical inventory observation, analytical review, procedures for detecting whether a company may soon be in financial difficulty, going-concern problems, subsequent events, etc.

d. *Etudes juridiques*—deals with legal aspects of the statutory audit of the *commissaire aux comptes*

e. *Bulletin des commissaires aux comptes*—provides practical advice on actual accounting and auditing problems and solutions, as well as notification of disciplinary action taken against statutory auditors.

Ethics Requirements

16. The French accounting profession's ethical standards include principles established by law and the professional bodies. Ethical

standards that apply to *experts-comptables* require that members of the OECCA—

- Consult with the previous *expert-comptable* before accepting a new client.
- Do not engage in other business transactions beyond the scope of their professional duties.
- Do not advertise their services.
- Do not perform any salaried work, except—
  —In a professional teaching capacity.
  —For another *commissaire aux comptes* or *expert-comptable*.
- Ensure against liability for professional negligence.
- Do not charge fees contingent on financial results.

17. In addition, some ethics requirements specifically apply to both *commissaires aux comptes* and *experts-comptables*. For example, they may not—

- Be a director or an officer of a client.
- Receive any money from an audit client except for audit work.
- Have any family connections with the directors of a client.

18. The *commissaire aux comptes* and *expert-comptable* should not be in a position that is likely to impair his or her judgment or independence; for example, an *expert-comptable* giving management advice to a company may not be its *commissaire aux comptes*.

PROFESSIONAL PUBLIC ACCOUNTING ORGANIZATIONS

Requirements for Membership

19. Qualifying as an *expert-comptable* is the most common way of entering the profession. Apart from basic requirements of personal integrity and age, the requirements include the following:

a. A graduate degree
b. Four or five years of study and completion of a number of examinations in all relevant subjects
c. Three years of training
d. Passing the final examination

20. To become a listed *commissaire aux comptes,* the candidate must be—

a. At least twenty-five years of age.

b. An *expert-comptable,* or pass the *commissaire aux comptes* examination after having completed training for at least two years with a practitioner approved by the Regional Council. Persons with fifteen years of relevant experience are exempt from this training period.

c. Domiciled within the Regional Council's jurisdiction.

d. Of high moral standards and possess character references deemed sufficient by the Regional Council.

e. Of French nationality (refer to the discussion of foreign reciprocity in paragraph 6).

Rights of Membership

21. Membership in the OECCA is restricted to *experts-comptables* or *comptables agréés* in public practice. Membership is lost when a member enters industry.

Number of Members

22. The following is the approximate number of members in each of the major public accounting organizations as of March 1992:

Members of the *Ordre des experts-comptables:*	
Experts-comptables	11,317
Comptables agréés	1,516
Experts comptables stagiaires	3,588
Accounting firms	5,557
Members of the *Compagnie Nationale des Commissaires aux Comptes:*	
Commissaires aux comptes	10,792 individuals and firms

CPE Requirements

23. To maintain the high standard of competence required by the profession, each practicing member must devote a certain amount of time each year to improving his or her own training, as well as that of subordinates.

Peer Review

24. *Commissaires aux comptes* are required to undergo a form of regular peer review generally conducted by other statutory auditors nominated on a voluntary basis by the Regional Council. The peer review inspection deals with—

a. Compliance with statutory regulations and professional ethics.

b. Compliance with regulations relating to the performance of audits.

For listed companies, a special peer review program is applied in cooperation with the *Commission des Operations de Bourse,* aimed at monitoring the quality of the statutory auditor's work.

2

Auditing Requirements

STATUTORY AUDITING AND REPORTING REQUIREMENTS

Purpose of the Statutory Audit

25. The Company law of July 24, 1966, requires that most companies have statutory audits. The role of the *commissaire aux comptes*, as defined by Article 228 of this law, is as follows:

a. Certification—The *commissaire aux comptes* shall certify that the annual financial statements, which are management's responsibility, are *réguliers et sincères* (requirements of regularity and truth) and give an *image fidèle* (a fair presentation) of the results of the operations for the accounting period, as well as of the financial position and assets of the business at year end.

b. Verification of information given to shareholders—The *commissaire aux comptes* verifies the truth of the information given in—
   - —The report of the Board of Directors to shareholders (management report).
   - —The reports and, more generally, any release addressed to the shareholders.

c. Verification of statutory requirements—The *commissaire aux comptes* is charged with ensuring that shareholders receive equal treatment. He or she checks compliance with provisions relating to directors' qualifying shares and reports on any irregularities or inaccuracies that he or she may have found in the performance of his or her duties, on acquisitions of investments in other companies, on the remuneration of highest paid employees, on management, and on expenses disallowed for income tax purposes. He or she informs the shareholders, by means of a special report at the annual general meeting, of any agreement that may exist between the company and any of its directors, or between the company and any other company having a director in common, except when these agreements relate to usual transactions with normal terms.

d. Going concern evaluation—The March 1, 1984 law (For the Prevention and Amicable Settlement of the Difficulties Experienced by a Business or Troubled Company Law) has significantly increased the role of the *commissaire aux comptes* in establishing an early-warning procedure whereby events that might impair a company's existence as a going concern are noted by the *commissaire aux comptes* and explanations are provided by the management. If the *commissaire aux comptes* is not satisfied with the explanations, these matters must be discussed at a board of directors meeting and the company's employee committee (*comité d'entreprise*) must be informed. If no action is taken by the company to improve a rapidly deteriorating financial situation, the *commissaire aux comptes* must present a special report at the next shareholders' meeting. This report must also be communicated to the employee committee.

e. Violation of company law—The *commissaire aux comptes* must report to the public prosecutor any violation of the law that comes to his or her attention. Failure to report a violation may result in criminal sanctions against the *commissaire aux comptes.*

f. Review of forecasts—For those companies having 300 or more employees (including employees of 50 percent or more owned subsidiaries) or annual revenues of at least FF (French francs) 120 million, the Troubled Company Law demands that management prepare the following:

- For each semiannual period, a statement of immediately disposable assets (excluding inventories) and liabilities that are due as of the date of the statement. The statement must be prepared within four months of the end of the current period.
- For each year, a statement of changes in financial position (within four months of the end of the current year); a financing plan (within four months of the end of the current year); and a profit forecast, to be revised, if necessary, at the end of the first six months and prepared within four months of the end of the current year.

g. Disclosure of breaches of law—If in performing his or her duties, the *commissaire aux comptes* becomes aware of circumstances in which a company or its officers have breached a legal requirement, he or she is obligated to reveal such facts to the public prosecutor.

These documents must be discussed in the written reports from the board of directors. They must be communicated to the employee committee and to the *commissaire aux comptes,* who must ensure that the assumptions are reasonable and report accordingly to the shareholders.

Entities Required to Be Audited

26. The obligation to have a statutory audit by a *commissaire aux comptes* applies mainly to the following types of companies:

- Corporations (*sociétés anonymes,* or SA) and limited partnerships with shares (*sociétés en commandite par actions*)
- Lending institutions
- Economic interest groups (*groupements d'intérêt économique,* or GIE) issuing bonds or with 100 or more employees
- Agricultural cooperatives with revenues of at least FF 500,000

27. In addition, statutory audits are required by entities that meet two of the following three criteria: (1) total assets are FF 10 million; (2) revenues are FF 20 million; and (3) the average number of employees is 50. Such entities are the following:

a. General or limited partnerships (*sociétés en nom collectif* or *sociétés en commandite simple*)
b. Limited liability company (*société à responsabilité limitée,* or SaRL)
c. Cooperatives (other than agricultural)
d. Associations and civil companies, when they conduct commercial activities
e. Governmental bodies, when they conduct industrial or commercial activities and do not use governmental accounting

Appointment and Qualifications of Auditors

28. If the company is raising money from the public, the *commissaire aux comptes* and his or her deputy auditor (*suppléant*) are

appointed at the company's first general meeting; if the company does not raise money from the public (for example, if it is privately owned), the *commissaire aux comptes* is appointed in the company's articles of incorporation. Subsequent appointments or reappointments are made, in both cases, at ordinary shareholders' meetings.

Number of Commissaires aux Comptes

29. Most companies are required to have only one *commissaire aux comptes*. However, two *commissaires aux comptes* must be appointed for—

a. Companies that are required to prepare consolidated financial statements. The law of January 3, 1985, which harmonizes French accounting practice with the EC Seventh Directive on Consolidated Financial Statements, requires publicly traded companies and governmental bodies over a certain size to produce consolidated financial statements for fiscal years beginning after December 31, 1985.

b. Lending institutions.

Term of Office

30. The standard term of office for *commissaires aux comptes* is six years. They can be reelected indefinitely. The *Compagnie Régionale des Commissaires aux Comptes* and the COB, in the case of a public company, must be informed of appointments and dismissals. The names of the *commissaires aux comptes* must be inserted in a legal journal (*Journal d'annonces légales*) to notify the public.

Failure to Appoint a Commissaire aux Comptes

31. Any shareholder's resolution is void when it is reached without the proper appointment of a *commissaire aux comptes* or based upon the report of a *commissaire aux comptes* improperly appointed or improperly remaining in office. In addition, the chairman or the members of the board of directors of a *société anonyme* are criminally liable when they fail to provide for the appointment of the *commissaire aux comptes* of the company or fail to give him or her notice of any shareholders' meeting.

Dismissal of a Commissaire aux Comptes

32. One or more shareholders representing at least one-tenth of the company's capital, the board of directors, the labor management

committee, the court (*ministère public*) and, in public companies, the COB, may ask for a change of *commissaire aux comptes*. In this situation, a new *commissaire aux comptes* may be appointed by the court until the next general shareholders' meeting. The former *commissaire aux comptes* is entitled to appeal any attempt at removal.

Professional Fees

33. For larger companies, such as those with total assets, operating income, and revenues (excluding value-added tax, or VAT) of more than FF 800 million, public companies, insurance companies, lending institutions, investment companies, and certain types of real estate development companies, fees are determined by mutual agreement between the parties.

34. For other companies, the CNCC has issued guidance as to the time necessary to complete an engagement, which is determined according to certain rules and the size of the company. However, these serve only as guidance, whereas fees are generally determined by mutual agreement.

35. Litigation relating to disputed fees falls under the jurisdiction of the discipline committee within the *Compagnie Nationale des Commissaires aux Comptes*.

Auditing and Reporting Responsibilities

Powers of Investigation

36. *Commissaires aux comptes* are entitled to inspect at the company's place of business all documents necessary in the performance of their duties. They may also obtain information for the purpose of their work from third parties who have carried out operations on behalf of the company. However, this right to information does not extend to documents, contracts, and any records held and owned by third parties, unless authorized by a court decision. Information cannot be withheld from *commissaires aux comptes* on grounds of professional secrecy, except by officers of the law.

Organization of Audit Work

37. For the purpose of carrying out their audit work, *commissaires aux comptes* may be assisted by experts or colleagues of their choice.

38. Where two or more *commissaires aux comptes* are appointed, each may carry out his or her audit work separately. In effect, they are sharing joint and several audit responsibility and must write a common report. If a disagreement between the *commissaires aux comptes* occurs, the report should express their separate opinions. Disagreements, however, seldom occur.

39. Any report or document issued by a firm of *commissaires aux comptes* covering the performance of the statutory audit assignment should include, in addition to the firm's signature, the signature of either the *commissaire aux comptes* or the engagement partner. However, one partner can act in both capacities if so authorized by the firm.

Professional Confidentiality

40. *Commissaires aux comptes,* as well as any experts or colleagues who assist in the audit assignment, are bound by the principle of professional secrecy regarding all information obtained in the course of their work.

Liability of Commissaires aux Comptes

41. In terms of civil liability, *commissaires aux comptes* are liable to both the company and to third parties for negligence in discharging their duties. However, they are not liable for information or disclosure of facts relating to potential going-concern problems, provided they have acted in good faith. They are not liable for any improper acts committed by the directors or management, except when they were aware of such acts and failed to disclose them to the shareholders in their report to the general meeting.

42. Regarding criminal liability, *commissaires aux comptes* are liable for punishment by imprisonment, fines, or both in the following circumstances:

a. They knowingly accepted, exercised, or kept the position of *commissaire aux comptes* for a company when they were not independent of that company.

b. They knowingly gave or confirmed false information regarding the financial position of the company or failed to report to the shareholders irregularities and errors of which they had knowledge.

c. They refused to attend a meeting of the employee committee or willfully obstructed the functioning of such a committee.
d. They divulged information concerning the affairs of their clients to someone who did not have the legal right to examine their working papers.
e. They conspired with a director in the commission of an illegal act.
f. They represented debenture bond holders.
g. They failed to mention in their report the acquisition by the company of an investment of more than 5 percent, 10 percent, 20 percent, 33 ⅓ percent, or 50 percent in another company.
h. They failed to disclose to the public prosecutor any misdemeanor relating to a violation of law of which they obtained knowledge during the performance of their duties.
i. They exercised the function of *commissaire aux comptes* while engaging in certain legally proscribed activities.

Filing of Reports

43. Two kinds of reports—reports to management and reports to shareholders—must be prepared by the *commissaire aux comptes* after completion of the statutory audit.

Reports to Management

44. Under Article 230 of the Company Law of 1966, statutory auditors should report to the directors, orally or in writing—

a. The procedures that they carried out, including the scope of their testing.
b. The balance sheet categories and other accounting documents that, in their opinion, require changes, together with any relevant comments necessary to highlight disclosures not included in the financial statements (and that were not required to be disclosed) relating to accounting policies adopted by the company.
c. Any irregularities or errors.
d. The conclusions on the above matters and the effect of any audit adjustments on the results of the current accounting period as compared with the results of the previous period.

45. Although the *commissaire aux comptes* is not required to attend, he or she must be invited to the meeting of the board of directors

held immediately before the annual general meeting to discuss his or her report. If the report recommends modifications to the financial statements that are not accepted by the directors, the report to the shareholders must be qualified.

Reports to Shareholders

46. The reports to shareholders take the form of a general report expressing an opinion on the annual accounts and, if required, on consolidated accounts, and, in the case of a corporation (SA) or limited liability company (SARL), a special report.

General Report

47. The general report includes the opinion of the *commissaire aux comptes* on the annual accounts and on the accuracy and compliance of the information contained in the report of the directors (senior management or owner) to the annual general shareholders' meeting. The opinion can take the form of an unqualified opinion (*certification sans réserve*), a qualified opinion (*certification avec réserves*), or an adverse opinion or disclaimer of opinion (*refus de certifier*).

48. In case of a fraudulent balance sheet, the *commissaire aux comptes* must notify the public prosecutor. Under law, the general report must specifically mention the following:

a. Reasons for giving a qualified opinion

b. Irregularities or inaccuracies discovered

c. Effects of changing accounting principles

d. Acquisitions of 5 percent, 10 percent, 20 percent, 33⅓ percent, 50 percent, or 66⅔ percent or more of the capital stock or voting rights of companies registered in France and certain other information regarding acquisitions or mutual investments

e. Names of individuals or legal entities holding more than 5 percent, 10 percent, 20 percent, 33⅓ percent, 50 percent, or 66⅔ percent of the company's share capital or voting rights and the changes in equity during the period (required if the company is listed on the Stock Exchange)

f. Names of companies under the company's control

g. Violation of the principle of equality among shareholders

h. Violation of the provisions relative to directors' qualifying shares
i. Illegal acts committed by directors or executives
j. General expenses disallowed for tax purposes

49. If the report of the directors does not contain all the information required by the company law, the *commissaire aux comptes* must provide the missing information in his or her report.

Special Report

50. The special report discloses agreements between the company and its directors or general managers, members of its management committee or supervisory board, or its managing directors, or between the company and other companies or enterprises in which these individuals have an interest. The *commissaire aux comptes* does not express any opinion on this information.

51. Both the general and special reports are addressed to the shareholders, and copies are available to the employee committee. The *commissaire aux comptes* must be invited to the annual shareholders' meeting, and he or she generally attends and reads their report.

52. For SAs and limited partnerships with shares, additional documents are presented by the directors at the annual general shareholders' meeting. These documents, which require prior verification by the *commissaire aux comptes* (although no report is issued), contain the following:

a. Statistics for the last five years (including sales, net income, and other information similar to U.S. selected financial data)
b. A schedule indicating the worldwide amount of remuneration of either the ten highest paid employees of the company, if the corporation has over 200 employees, or the five highest paid, if the total number of employees is 200 or less

53. Within one month after their approval at the annual shareholders' meeting, the annual financial statements, the report of the board of directors, a general report of resolution submitted to the shareholders to allocate profits to dividends or reserves, and the subsequently approved shareholder resolution are filed with the clerk of the Commercial Court. The special report is not filed with the clerk.

SUMMARY OF SIGNIFICANT AUDITING STANDARDS AND COMPARISON WITH U.S. GENERALLY ACCEPTED AUDITING STANDARDS (GAAS)

Standards Issued

54. In September 1987, the CNCC issued standards concerning audit engagements. These standards are applicable for audits of financial statements for years beginning January 1, 1988.

55. The standards reflect the views of the profession regarding the auditor's performance of engagements with reasonable due care. They are supplemented by comments intended to facilitate the implementation of the standards by describing their application and background.

56. The standards should be applied by all auditors. However, compliance with the comments is not mandatory. In addition, the CNCC issues guidelines (*notes d'information*) and specialized industry audit guides for statutory auditors.

General Standards

57. The general principles included within the standards are similar to U.S. practice. They specify—

- The scope of the engagement as determined by the law.
- That company management is responsible for preparing the financial statements, supervising the efficiency of the various departments of the company, and monitoring staff activity.
- That the statutory auditor is bound to show due care.
- That the statutory auditor should not make management decisions, although he or she may render advisory services.
- That the statutory auditor can carry out his or her work at various times during the year.
- That professional judgment is an essential element of the statutory auditor's work.
- That the statutory auditor can delegate some of his or her work but retains responsibility for the audit opinion.

Code of Conduct

58. The standards of professional behavior define principles for independence, expertise, work quality, confidentiality, and acceptance and retention of engagements.

Standards of Fieldwork

Planning the Engagement

59. The statutory auditor should have an overall knowledge of the company that will assist in the performance of the engagement and help evaluate significant systems and areas. The purpose of this approach is to identify the risks that could have a significant impact on the financial statements, enabling the auditor to—

- Determine the nature and scope of the work, after considering materiality.
- Perform the engagement in an efficient and timely manner.

Evaluation of Internal Control

60. The statutory auditor should evaluate the significant internal control systems to identify those internal controls that he or she intends to rely upon and the risks of error in processing accounting information. The statutory auditor should then develop an appropriate audit program.

Obtaining Evidence

61. In the course of the engagement, the statutory auditor should obtain sufficient relevant information to provide a reasonable basis for an opinion on the financial statements. In this respect, he or she can apply different audit procedures, including transaction tests, inventory observation, direct confirmation, analytical review, and so on.

Delegating and Supervising

62. The statutory auditor delegates much of the detailed work to assistants. To fulfill his or her professional responsibilities, the auditor must supervise the work delegated to ensure that it has been performed as intended and supports the audit opinion.

File Documentation

63. Working papers document the work performed and support the statutory auditor's report. Moreover, they help to better organize and control the engagement, as well as provide evidence that the audit included such tests and procedures as were considered necessary.

Relying on the Work of Internal Auditors

64. In order to determine whether to rely on the work carried out by internal auditors, the statutory auditor should—

- Evaluate the internal audit function within the company.
- Make appropriate tests of the internal auditor's work and determine that the conclusions reached are in compliance with the objectives of the audit engagement.
- Maintain sufficient documentation of their work.

Relying on the Work of the Expert-Comptable

65. The statutory auditor should determine the nature of the *expert-comptable*'s work. He or she should estimate to what extent it can be relied on to serve the objectives of the statutory audit engagement.

Relying on Work Performed by Other Auditors

66. The statutory auditors of the parent company bear sole responsibility for reporting that the consolidated financial statements give a true and fair view of the net assets, the financial position, and the results of operations of companies within the group. They should examine the reports issued by the statutory auditors of other group companies. If they consider it necessary, they may review the other auditors' work or even perform tests themselves at the subsidiary level.

Coordinating Work Between Joint Statutory Auditors

67. When a company has to prepare consolidated financial statements, joint statutory auditors are required. Joint statutory auditors are jointly responsible for the opinion on the statutory and consolidated financial statements, and should work together in planning the engagement and formulating their opinions.

Applying Audit Procedures to Small Companies

68. Although the auditor's objectives remain the same whether a company is large or small, the auditor should consider the special characteristics of the small company.

Standards of Reporting

69. The standard form of an unqualified report on annual accounts is as follows:

> In execution of the assignment that was entrusted to me by your annual general meeting, I hereby present to you my report on—
> - The audit of the annual accounts.
> - The specific verifications and disclosure prescribed by the law for the fiscal year ended ______.

70. An example of a report on the financial statements follows:

> I have made an audit of the annual accounts by applying the procedures that I have considered necessary in accordance with the standards of the profession.
>
> I certify that the annual accounts are regular and sincere and give a true view of the result of operations for the fiscal year last ended and of the financial position and assets and liabilities of the company at the close of that fiscal year.

71. Significant uncertainties or departures from generally accepted accounting principles that do not affect the overall fairness of the accounts require a qualified opinion. However, the specific wording indicating the qualification (and the reservation) will not make this distinction. If the departure from generally accepted accounting principles or the uncertainty affects the overall fairness, an adverse opinion or a disclaimer of opinion, respectively, will be expressed.

72. If the continuation of the company as a going concern is in doubt, the auditor should qualify or disclaim an opinion.

73. Following is an example of the second part of the report on other specific verifications:

> I have also performed auditing procedures with respect to certain specific information required by law in accordance with the standards of the profession.

I have no observations to formulate on the sincerity and conformity with the annual accounts of the information provided in the management report of the board of directors and in the documents addressed to the shareholders.

74. The following features of the report should be noted:

a. The report of the statutory auditor is mainly intended for shareholders of the company, but is also submitted to the public.

b. Adherence to generally accepted auditing standards, accounting principles, and the law is not explicitly referred to, but it is implied.

c. When the report is signed in the firm's name, the signing partner's name must also be mentioned.

d. The second part of the report should include comments from the auditor with respect to—

—The adequacy of information presented to the shareholders.

—Failure to comply with legal statutory regulations.

—Other specific information required by law. In addition to auditing the statutory and consolidated financial statements, if any, the statutory auditor should verify certain documents or elements. Paragraph 75 lists those documents or elements that must be verified for all companies. Paragraph 76 discusses the additional documents or elements to be verified for companies with a share capital.

75. The following documents or elements must be verified for all companies.

Document or Element	*Source of Requirement*	*Auditor's Procedures*
Annual and consolidated management report	art. L228 §3	All required disclosures should conform with the annual and consolidated financial statements
Other documents provided to shareholders with the financial statements	art. L228 §3	All required disclosures should conform with the annual and consolidated financial statements
Equal treatment of shareholders	art. L228 §4	Test of compliance with the requirement

Document or Element	*Source of Requirement*	*Auditor's Procedures*
Description of investments in subsidiaries	art. L356	Tests of the information in the management report
Disclosure of changes in accounting methods	art. L341	Assess adequacy of disclosure in the notes to the financial statements and in the management report
Documents relating to troubled company legislation	arts. L340-2 and L340-3	Limited review of the documents[1]
Agreements between the company and its directors	arts. L101-106, L145-147, and L50	Tests of terms of the agreements

76. The following documents or elements must be verified for companies with a share capital.

Document or Element	*Source of Requirement*	*Auditor's Procedures*
Remuneration of highest paid employees	art. L168, 4	Tests and confirmation of amounts
Contribution expense and detailed listing of contributions	art. L168, 5	Tests and confirmation of amounts
Directors' nominee shares	art. L97	Tests of ownership and of the number of shares held
Shareholder listing	art. L356-3	Tests of information in the management report

(Continued on next page)

[1]A limited review comprises an analytical review of the information and any additional information, obtained through discussion with the management of the company, that the auditor considers necessary.

Document or Element	*Source of Requirement*	*Auditor's Procedures*
Disallowed deductions	CGI art. 223	Tests of information in the management report and assessment of fiscal risk
Semiannual information	art. L341-1 §3	Limited review[2]

[2]See note 1 on page 23.

3

Accounting Principles and Practices

SOURCES OF ACCOUNTING PRINCIPLES

77. Statutory accounting principles are derived both from the Code of Commerce and from comments on the *Plan Comptable Général* (General Chart of Accounts). These texts are the result of the harmonizing of French principles with those of the other EC member countries, as required by the EC Fourth Directive. The *Plan Comptable Général* (PCG) does not apply to banks and insurance companies. The amendment to the Fourth Directive concerning banks was approved on December 31, 1986. It has not been incorporated into French law as of March 1992. For insurance companies, harmonization is in the process of being completed. French consolidation rules conform with the EC regulations contained in the Seventh Directive relating to consolidated financial statements. Some of these rules differ from those applicable to preparation of separate company financial statements (for example, LIFO accounting for inventories is permitted for consolidated financial statements but not for separate company financial statements, and deferred tax accounting is required in consolidated statements but is not permitted in separate company statements).

78. Interpretation of law may be found in publications issued by the *Conseil National de la Comptabilité* (National Accounting Board), the *Commission des Opérations de Bourse*, the *Compagnie Nationale des Commissaires aux Comptes* and the *Ordre des Experts-Comptables et des Comptables Agréés*.

79. The Code of Commerce and the *Plan Comptable Général* incorporate the fundamental principles of conservatism, evaluation of potential going-concern problems, matching of costs and revenues, and consistency. Offsetting of assets and liabilities or revenue and expenses is not allowed unless the right of offset exists.

FORM AND CONTENT OF FINANCIAL STATEMENTS

Presentation of Statements

80. The annual financial statements must be sufficiently detailed to satisfy the requirement of fair presentation (*image fidèle*). The statements must be prepared in the French language, using French currency. Following are two situations in which, to give fair presentation, generally accepted accounting principles may be supplemented or, in rare instances, disregarded:

a. When the application of such principles is insufficient for fair presentation as required by law, supplementary information should be given in the notes.

b. In exceptional cases, the application of generally accepted accounting principles may result in a misleading presentation. The situation should be described and justified in the notes, together with an indication of its effects.

Types of Statements Prepared

81. Under the *Plan Comptable Général*, the basic financial statements include an income statement (*compte de résultat*), a balance sheet (*bilan*), and notes to the financial statements (*annexe*). Comparative figures for the prior year must be shown.

82. The basic statements may be prepared according to one of the three accounting systems provided by the *Plan Comptable Général*, which are—

a. A simplified system (*système abrégé*), requiring presentation of the minimum number of accounts necessary to provide meaningful information. This system applies to small businesses meeting two out of three criteria defined by law (total assets FF 1.5 million or less, sales FF 3 million or less, and average number of permanent employees ten or less).

b. A basic system (*système de base*), requiring presentation of more accounts than the *système abrégé* and mandatory for all businesses other than small businesses meeting the aforementioned criteria.

c. An optional expanded system (*système développé*). The information required is more detailed than in the two other systems.

83. A statement of cash flows (*tableau de financement*) is not required. However, in the framework of the early-warning procedure, some companies meeting certain size tests must prepare, for internal use only, a statement of cash flows (together with other financial documents).

84. The income statement discloses the following three main classifications:

a. Trading transactions (such as operating income and operating charges, including prior-year items)

b. Financial transactions (including provisions against declining market values of investments, debenture issue expenses, etc.)

c. Unusual, extraordinary, and nonoperating transactions (including the accounting entries recorded as a result of significant differences between financial reporting and tax treatment, such as additional depreciation expenses and special provisions—the corresponding accounting entry is an adjustment to special reserves)

85. In addition, tax provisions must be shown separately. Deferred taxes are provided for only in consolidated financial statements. Revenues (net of VAT—value added tax) must be analyzed in the notes according to activity and geographical sources. Cost of sales may be disclosed in the notes as an alternative to income statement disclosure.

86. The balance sheet discloses the following separately:

- Fixed assets (subdivided into intangible, tangible, and financial assets, such as marketable equity securities)
- Current assets (classifying inventory and other current assets separately)
- Shareholders' equity (distinguishing between common stock, preferred stock, and retained earnings)

- Provisions for losses and expenses
- Debt (subdivided into financial, commercial, and other)
- Prepaid and accrual accounts, such as prepaid expenses and deferred revenue

87. Analyses of fixed assets and depreciation, schedules of current and noncurrent assets and liabilities, and analyses of reserves (distinguishing between legal and other reserves) are to be included in the notes to the financial statements. The notes should contain information not included in the balance sheet or income statement and deemed significant in giving a true and fair view (*image fidèle*) of the operating results and financial position of the company.

88. Disclosures that are required by law include—

a. Accounting principles and methods used.

b. Methods used for calculating depreciation and determining allowance for doubtful accounts; method of inventory valuation; and disclosure of the calculated amounts of the provisions for reserves. Separate disclosure should be made of amounts recorded for tax purposes.

c. Explanations of why comparison is difficult between current and prior-year financial statements and restatement of prior-year information, if appropriate, to make such comparisons meaningful. Disclosure should be made as to why restatement was made.

d. Changes in noncurrent assets during the year.

e. Nature, amount, and accounting treatment of translation differences.

f. In instances of asset revaluation, the methods used for calculating revalued amounts and the balance sheet and income statement accounts affected, including the amounts of revaluation.

g. Receivables and payables classified according to maturity, distinguishing receivables between current and noncurrent. The amount of payables should be shown for those due in less than one year, in more than one year but less than five years, and in more than five years.

h. For all payables, an indication of the amount covered by mortgages or other liens.

i. Amount of financial commitments, by category, noting separately those relating to senior management, subsidiaries, investees, and other affiliated companies.

j. For current assets (primarily inventories), the difference between carrying value and market value at year end.

k. List of subsidiaries and investees, disclosing for each the percentage held directly or indirectly, the amount of stockholders' equity, and the net income for the latest fiscal year.

l. Number and par value of the company's shares, by category, indicating amounts issued or canceled during the year.

m. Participating or preferred shares, including number and par value of rights attached.

n. Name of any parent company that includes the company in its own consolidated financial statements.

o. Proportion of noncurrent financial assets, receivables, liabilities, financial income, and financial expenses relating to affiliated companies.

p. Amount of commitments for pensions and additional retirement payments, indicating separately those for which provisions have been made and those relating to senior management.

q. Amount of advances and loans to senior management, indicating terms and the amount of repayments made during the year.

r. Supplementary information when the application of accounting principles is insufficient for fair presentation as required by law.

s. Reasons for nonapplication of accounting principles that may result in a misleading presentation and the effects on the financial statements.

t. Description and justification of changes in presentation of annual financial statements and valuation methods.

u. Reasons for significant adjustments to the allowance for doubtful accounts provided for in the prior period.

v. Comments on the elements of intangible assets.

w. Reasons for amortizing research and development cost over a period of more than five years (the maximum period generally allowed by law). Amortization over a longer period is allowed when economic or technical conditions justify it.

x. Methods used for amortizing redemption premium on loans.

y. Explanation of deferred income and expenses.

z. Lease obligations.

The *Commission des Opérations de Bourse* (French equivalent of the SEC) also requires certain information to be provided in the notes to financial statements.

89. In addition, the information in the list below, when significant, should be disclosed for companies that meet two of the following three criteria: total assets greater than FF 5 million, sales over FF 10 million, and an average number of permanent employees greater than fifty.

a. Remuneration of board of directors, the supervisory board, and the management board

b. For each category of convertible and exchangeable bonds and similar borrowings, the number, par value, and rights attached

c. Analysis of the income tax charge between extraordinary items and other items, with an indication of the method used for making the allocation

d. Analysis of sales by geographical area and sector of activity

e. Analysis, by category, of the number of employees

f. Extent to which net income has been affected by tax adjustments recorded for financial purposes and their effect on shareholders' equity; for example, additional depreciation recorded equal to the excess of tax over book depreciation

g. Deferred taxes on timing differences, even though deferred taxes are only recorded when consolidated financial statements are prepared

SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES AND COMPARISON WITH U.S. GENERALLY ACCEPTED ACCOUNTING PRINCIPLES (GAAP)

Valuation Principles

90. Financial statements are based on the historical cost convention. However, revaluation to current value of property, plant and equipment, and investments is permitted. The surplus or deficit arising on revaluation must be transferred to a separate reserve

account in stockholders' equity. An appraisal increase cannot be used to absorb operating losses or be distributed in the form of dividends. Current income tax at the normal rate, recorded on the income statement, is provided on the unrealized surplus on revaluation.

Revenue and Cost Recognition

91. Revenue is recognized when earned, and realization is reasonably assured. Costs are recorded when incurred.

Consolidation

92. To harmonize French accounting practice with the EC Seventh Directive on consolidated financial statements, as noted in paragraph 29, the law of January 3, 1985 requires publicly traded companies to produce consolidated financial statements for fiscal years beginning in 1986. Other companies, except for very small ones, are required to prepare consolidated financial statements for fiscal years beginning January 1, 1990. Since 1971, no French company is allowed to raise funds in the public market without issuing consolidated statements.

93. The method of accounting for subsidiaries depends on the following particular circumstances:

a. Full consolidation (*intégration globale*) of the group's dependent companies is ordinarily required. Dependent companies are those companies under the long-term control of the parent company (either direct or indirect). This control results from any of the following:
   - Holding a majority of the voting rights
   - The power to appoint more than half the members of the administrative, management, or supervisory body (this power is presumed when 40 percent of the voting rights are held and no other shareholder has an equivalent or a larger proportion of the voting rights)
   - The ability to exercise dominant influence over a company pursuant to contractual rights (such as a company dependent upon the parent as its sole supplier of raw materials)

b. The equity method (*mise en équivalence*) applies to shareholdings of 20 to 50 percent and must be applied in consolidated statements. Investments of 20 to 50 percent are carried at the lower of cost or net realizable value in the statutory financial statements.

c. Companies that are required to publish consolidated financial statements may account for investments in their subsidiaries exceeding 50 percent on the equity basis on their single financial statements. Under this method, the share ownership percentage of the underlying book value of the subsidiary is substituted for the historical cost of the investment. Any difference is recorded in a separate stockholders' equity account titled "difference arising from equity accounting." If the net difference arising from applying this method is or becomes negative, a provision for the negative balance is charged to the income statement.

d. In proportional consolidation, which applies to joint ventures, the percentage of shareholding is applied to each line of the balance sheet and the income statement, and is included in the consolidated financial statements in proportion to the ownership interest.

94. The law provides for some instances when an entity need not be consolidated although control is present. For example, an entity is not required to be included in consolidated statements when, in management's opinion, long-term restrictions could substantially hinder the parent's control over the assets or management of that entity. In addition, consolidation is not required when—

a. The shares of the entity are held for resale.

b. The entities are not material.

c. The information necessary for the preparation of consolidated statements cannot be obtained without disproportionate expense or undue delay.

Business Combinations

95. The purchase method of accounting (similar to U.S. generally accepted accounting principles) for a business combination involving the acquisition of a majority of another company's stock is used in France.

96. However, pooling of interests accounting is not acceptable in France. A merger (*fusion*) involves the liquidation of the absorbed company and is treated similarly to a purchase transaction. A merger can take two forms: one company can absorb one or more

companies that will then cease to exist, or two or more companies can combine to form an entirely new company that will be the sole survivor of the transaction. In a merger, the shareholders of the absorbed company receive shares issued by the acquirer. The acquirer receives the assets and liabilities of the absorbed company. Regardless of the actual date of the merger, all are generally deemed to take place at the beginning of the accounting year. Other forms of business combinations are *scission* (a subdivision of existing companies) and *fusion-scission* (companies transfer a part of their assets to new or already existing companies).

97. Following are the accounting consequences of a merger:

a. Values, which may not be greater than current values, are assigned to the assets of the absorbed company and constitute the new basis for subsequent depreciation. Liabilities are, when necessary, revalued (for example, if previously stated incorrectly). Goodwill (*fonds de commerce*), the excess of the value of the new shares issued to acquire the company over the value of the net assets acquired, may arise and is amortized over a five- to twenty-year period. (The Fourth Directive states five years and, although the French law implementing the directive does not refer to a specific time period, French practice may extend this period to twenty years.)

b. The excess of the value of the net assets acquired over the share capital issued by the acquiring company (*prime de fusion*) is treated as additional paid-in capital that may be used to offset deficits of the activities transferred or to absorb costs incurred in the combination.

98. Business combinations may have favorable tax implications under the following conditions:

a. No tax is payable on the capital gains on the revaluation of non-depreciable assets until the assets are sold by the absorbing company. At that time, tax is paid on the difference between the sales price and the absorbed company's carrying value. The estimated taxes payable are not reflected in the valuation of the asset at the time of combination.

b. The surplus resulting from the revaluation of depreciable assets is taxable at normal rates with payment spread over five years.

99. The statutory auditors must report to the shareholders on the method of effecting the combination and, in particular, the

valuation of assets of the acquired company. When the absorbing company is an SA, a limited partnership with shares, or an SARL, it is mandatory that an expert (*commissaire aux apports*) on the valuation of the net assets acquired be appointed by the courts. The expert must report on the value of the land, property, plant and equipment, and other assets and certify that the value of net assets acquired in the combination is at least equal to the capital increase.

Related-Party Transactions

100. The French definition of related-party transactions is more restrictive than that used in U.S. GAAP. Disclosure of related-party transactions in the *commissaire aux compte*'s special report to the shareholders is required of all contracts between the company and its directors or parties related to the directors. (See paragraph 50 for comments on contents of special reports.)

Accounting for Contingencies

101. A loss must be accrued when it becomes probable and when its amount can reasonably be estimated. Disclosure is required when there is at least a reasonable possibility that a loss may have been incurred.

Inflation Accounting

102. France has not yet developed a compulsory system of inflation accounting. The January 3, 1985 law on consolidated financial statements permits the presentation of supplemental consolidated financial statements adjusted for the effects of inflation using either the general purchasing power or current cost method.

103. Companies may provide reserves in the statutory accounts only that are deductible for tax purposes and that compensate for the adverse effects of price increases. These reserves are the following:

a. Reserve for price fluctuations (*provision pour fluctuation des cours*) is a tax-free reserve that may be created by companies that process certain raw materials (such as crude oil, cotton, aluminum, gold, or silver) whose prices are determined on international markets. The maximum reserve amount is recalculated annually according to an official cost index published for each raw material. No deferred tax effect is recognized in the financial statements. Any decrease in the reserve is subject to taxation at the normal rates in the year in which the change takes place.

b. Reserve for increased cost of inventories (*provision pour hausse de prix*) is calculated as the increase in the cost of inventories (current year end less prior year end) in excess of 10 percent of the book value of inventories at the beginning of the current or previous year and is deductible in the current year. However, this reserve must be added back to taxable profits within six years.

104. Reserves provided in the statutory accounts to support tax deductions (such as reserves for inventory price increases and accelerated depreciation) must be reversed in the consolidated accounts. In consolidation, these reserves represent timing differences and give rise to deferred taxes.

105. Inflation has periodically been acute, and companies have been required to revalue all assets according to a general price index. The latest revaluation was in 1976–77, when assets were revalued, tax-free, to market value and the surplus included in a revaluation reserve. Other revaluations are usually carried out for tax reasons. These revaluations are taxable and are made to absorb losses carried forward, which would otherwise be lost after a five-year period.

106. Tangible fixed assets and investments may be revalued only when all elements of both the assets and the liabilities of all consolidated companies are revalued according to a common criteria. However, the assets of companies in hyperinflationary countries may be revalued even when the assets of other companies in the consolidated group are not revalued.

Presentation of Assets

107. There is no strict distinction between current and noncurrent assets on the balance sheet because headings are classified by nature rather than by liquidity. The distinction between current and noncurrent is only provided in the notes. However, noncurrent assets are shown primarily in the upper part of the balance sheet, which includes intangible assets, fixed assets, and financial assets (for example, investment in subsidiaries and loans related to investments, other loans, and other investments, including, if any, the current portion thereof).

Receivables

108. As with all current assets, receivables are valued at the lower of cost or net realizable value. A provision for doubtful accounts may be set up, provided it covers specific items and can be substantiated. General reserves calculated as a percentage of the total receivables or sales are generally not tax deductible but are allowable for financial statement purposes.

109. In rare circumstances, receivables may be stated at their present value. However, different positions have been expressed by professional bodies, and the question is still under review.

Inventories

110. Inventories are categorized as raw materials, work in progress, and finished goods. Inventories are included at the lower of cost or net realizable value. Tax regulations require the use of the FIFO method of determining cost, but a moving-average cost method is also acceptable. LIFO is not permitted in financial statements (unless consolidated) or for tax purposes. The basis of valuation of inventories should be disclosed in the notes to the financial statements.

111. Inventory cost includes the purchase price of raw materials, direct production costs, and a reasonable proportion overhead. Financial costs, research and development costs, commercial costs, administrative costs, and warehousing costs are normally excluded except when the production cycle is more than one year.

Long-term Contracts

112. Long-term contracts should be valued at cost. Any foreseeable losses on these contracts should be accrued. Profits may be accounted for under either the percentage-of-completion method or the completed-contract method, with the completed-contract method being the predominant practice.

Fixed Assets

113. Fixed assets are stated at historical cost plus incidental costs, such as installation, repairs, and improvements prior to use.

114. Depreciation is calculated over the useful life of the assets. Depreciation of assets may be calculated using either the straight-line method or the declining-balance method (for purchases of new assets having a useful life of at least three years, if tax rules permit its use). Other asset valuation provisions (*provisions pour dépréciation*) may also be made if there is reason to believe that an unusual diminution in the value of the asset has occurred.

115. Additional depreciation based on standard asset lives, as defined by the tax authorities, is charged to profit and loss for tax purposes in the statutory accounts only. However, because this does not correspond to the depreciation of assets over their useful economic lives, the additional depreciation is not deducted from the gross book amount of the fixed assets but instead is classified under special reserves (*provisions réglementées*) in shareholders' equity. For the same reason, depreciation beyond normal requirements is shown on the statement of income as an exceptional item.

116. Fixed assets are presented on the balance sheet at their gross value less accumulated depreciation and amortization. The notes to the accounts disclose—

a. Methods used for calculating depreciation and provisions.

b. Amounts of depreciation and provisions, by category of fixed assets, noting separately those recorded for tax purposes.

Depreciation expense for the period is shown separately on the income statement.

Capitalization of Interest Costs

117. Interest expense may be capitalized if it relates to borrowings incurred during the construction period to finance the construction or the manufacture of fixed assets or inventory when the production cycle is longer than twelve months. For tax purposes, interest must be expensed as incurred.

Intangible Assets for Statutory Accounts and Consolidated Financial Statements

118. Intangible assets consist of organization costs, capitalized research and development, favorable leases, royalties, patents, licenses, trademarks, and similar rights (including software costs and goodwill). Intangible assets are amortized over periods similar

to those for fixed assets, although goodwill is amortized over a five- to twenty-year period. For tax purposes, goodwill trademarks and leasehold rights cannot be amortized.

119. Financial statement disclosure requirements are similar to those for fixed assets.

Financial Leases

120. Statutory accounting in France does not permit capitalization of leased assets. All leases are treated as operating leases unless an option to purchase is exercised, at which time it is accounted for as an acquisition at the actual exercise price. The notes should disclose the following:

a. The fair value of the asset at the inception of the lease
b. The amount of rentals paid under financial leases, separately presenting on the income statement real estate and other leases
c. The current year's depreciation and accumulated depreciation calculated on a pro forma basis, assuming the asset was purchased at the inception of the lease
d. The present value of rental commitments payable under financial leases analyzed between real estate and other leases indicating amounts payable: within one year, between years one and five, and amounts due after five years.

121. Capitalization of leases in consolidated statements is permissible if criteria similar to those of U.S. GAAP are met. Lease capitalization, however, is rarely done in France.

Liabilities

122. Liabilities are classified by function and the distinction between current and noncurrent liabilities is not used. The distinction between long- and short-term is only provided in the notes, in terms of less than one year, more than one year but less than five years, and more than five years.

Notes Payable

123. The total amount of notes payable included in the balance sheet under different headings should be disclosed. Moreover, the amount covered by mortgages or other liens on assets should be disclosed for all headings.

Transfers to Reserves

124. Five percent of net income must be transferred annually to legal reserves until the reserve reaches a maximum of 10 percent of capital. This is presented as a charge to retained earnings in the statement of stockholders' equity.

Research and Development Costs

125. Generally, research and development costs must be expensed, but they may be capitalized and amortized if the costs incurred are applied to a specific product or process and the marketability of the product or process is substantially ensured. Capitalized research and development costs should be amortized over a period not exceeding five years. A longer period may be adopted in unusual cases but should not exceed the estimated economic life of the related product.

Extraordinary Items

126. Extraordinary items consist mainly of items outside the normal course of business that are unusual in nature and size and are not expected to recur in the foreseeable future. Regardless of the treatment of extraordinary items in the financial statements, there is a general obligation to disclose any information not included in the income statement that is deemed significant to an understanding of the operating results of the business.

127. Disposal of a segment of a business must be accounted for according to the economic reasons that made it necessary. Costs of disposal, including estimated losses, should be treated as an extraordinary item in the income statement. Disclosure is required of the gain or loss on disposal of the segment, the financial conditions surrounding the disposal, and its operations to date.

Pensions

128. Retirement benefit plans in France are essentially compulsory state-sponsored plans based on an allocation principle under which contributions are collected from companies and then redistributed to retirees. A certain number of companies have also developed their own defined benefit plans.

129. Following are the pension accounting rules:

a. Yearly contributions payable to the plan are charged to expense as accrued.

b. Future pension commitments may be recognized as a liability though there is no obligation for such recognition in law. Professional bodies (mainly the OECCA and COB) have issued recommendations that pension costs be recognized for eligible employees over the term of employment. Different actuarial methods of calculation are allowed, and each company may decide on the method adopted. The pension provision is not deductible for tax purposes.

c. Disclosure in the notes to the financial statements is required of the amount of pension commitments and additional retirement payments relating to staff members or associates or members of the board of management. The total amount of retirement costs provided must be shown separately.

Income Taxes

130. Income taxes are accounted for on the accrual basis. Ordinarily, there are few differences between income and loss, as determined for statutory accounting and tax purposes. Timing differences generally arise because certain charges or provisions are disallowed as deductions in determining taxable income (for example, reserves for pension costs are not tax deductible until paid, and unrealized translation gains are not recognized for book purposes but are included in taxable income). Deferred taxes on timing differences are not recorded (unless consolidated financial statements are prepared) but are disclosed in the notes to the financial statements. Disclosures must also include an analysis of the income tax provision distinguishing between usual items (such as current or normal) and extraordinary items, and an indication of the extent to which net income and shareholders' equity have been affected by entries that have been recorded for financial statement purposes as a result of the related tax treatment (additional depreciation and special reserves).

131. Comprehensive deferred tax accounting is required in consolidated financial statements under the law of January 3, 1985, although it is not permitted in the statutory accounts.

132. For income tax purposes, operating losses may be carried forward to offset income in the five succeeding years, except that operating losses resulting from depreciation may be carried forward indefinitely. The effect of the loss carryforward is included in the determination of net income in the period that it is utilized.

133. Operating losses of a given fiscal year may be offset against undistributed taxable profits of the three preceding years. Any resulting tax refund is treated as a credit, to be offset against the corporate income tax of the next five years; any remaining credit may then be reimbursed in cash. The tax effects of this credit are included in financial reporting income in the period realized.

Foreign Currency Translation

134. Foreign currency transactions are transactions denominated in a currency other than the entity's functional currency. In France, the accounting for foreign currency transactions not settled at year end is as follows:

- Unlike U.S. accounting, if there is an unrealized profit from the difference between the rate applied when the transaction was recorded and the rate at year end, no profit is recorded in the income statement. This unrealized profit remains on the balance sheet in a conversion difference account. It should be noted that for tax purposes, this profit must be recognized.
- If there is an unrealized loss, a conversion difference asset may be provided, unless the company is able to hedge certain transactions. When unrealized profit and loss are in the same currency at the same maturity date, the translation adjustments may be offset, and thus no provision is needed. If there are no hedge items, the unrealized loss (in addition to the asset) is recognized in the income statement, and a corresponding provision is recorded on the balance sheet.

135. Translation of financial statements prepared in foreign currencies include statutory accounts. Investments in subsidiaries and other affiliates are generally stated at cost in the financial statements of the parent company and are converted to French francs at the date of the original investment. The operations of foreign branches denominated in foreign currencies may be measured

either in French francs, using the rate of exchange at the transaction date (in this case, the French franc, which is the reporting and functional currency), or in the local currency, with translation at year end using the current rate (in this case, the local currency is the functional currency).

136. The PCG encourages companies to use the first alternative above and, although this method is the most commonly used, both methods enjoy widespread usage. The PCG does not provide clear guidance for the translation of the income statement or for the accounting treatment of translation differences. Practice varies, with both closing and average exchange rates used for the translation of the income statement. Practice is similarly varied for the accounting treatment of translation differences, with such differences recorded either as a component of income or of equity. However, if a company prepares consolidated financial statements, it will commonly use the same accounting treatment in its statutory accounts as it uses for the consolidated financial statements.

137. The PCG permits both the temporal (as prescribed in FASB Statement No. 8, *Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements*) and the current-rate methods of foreign currency translation. The methods are as follows:

Items	*Temporal Method*	*Current-Rate Method*
Balance sheet		
Nonmonetary items	HR	CR
Monetary items	CR	CR
Equity	HR	HR
Income statement		
Depreciation or provisions	AR or HR	CR or AR
Other expenses	AR	CR or AR
Income	AR	CR or AR

Legend
HR = Historical rate
CR = Current rate
AR = Average rate

The PCG permits subsidiaries located in hyperinflationary countries to use an alternative method.

138. The temporal method is considered more appropriate when the foreign entity's operations are an extension of the parent company's opérations; the current-rate method is considered more appropriate when a foreign entity is economically and financially independent of the parent company and other consolidated subsidiaries. However, companies may select either method, regardless of their specific circumstances.

139. In most circumstances, using the temporal method for consolidated financial statements will produce the same results as using the French franc as both the reporting and the functional currency for translating statutory accounts. Similarly, using the current-rate method for consolidated financial statements corresponds to a situation in which the local currency is the functional currency and the French franc is the reporting currency for statutory accounts purposes.

140. When the temporal method is used, the translation difference is recorded in the income statement; when the current-rate method is used, the translation difference is reported in stockholders' equity in a specific account called translation difference.

4

Business Environment

FORMS OF BUSINESS ORGANIZATION

Entities With Corporate Attributes

141. The same forms of business organization existing in the United States are found in France, though the rules that apply to the conduct of each type of business may be different. Corporate entities are principally governed by the law of July 24, 1966 and the decree of March 23, 1967, as amended.

142. Following are the most common forms of corporate entities in France:

a. The *Société Anonyme*, or SA (corporation), in which the shareholders' liability is limited to their required capital contribution. The SA's shares are freely transferable and negotiable. All SAs must have at least seven shareholders who may be either French or foreign individuals or legal entities. There is no legal maximum number of shareholders. The share capital must be greater than FF 250,000, or greater than FF 1,500,000 if use is made of the public capital market either by being quoted on stock exchanges or by using financial institutions for the placing of shares.

b. The *Société à Responsabilité Limitée*, or SARL (limited liability company), has the attributes of both a partnership and a corporation. It has limited liability (similar to a corporation) and limitations on interest-share ownership (similar to a partnership). The associates of a SARL can be held personally liable for the company's debts in excess of their capital investment only if they agree to be personally liable (by giving a guarantee). A SARL must have a minimum of two, but not more than fifty, members. Minimum capital is FF 50,000.

c. The *Société en Commandite par Actions*, or SCA (limited partnership with shares), has transferable shares like SAs. It has two classes of partners: general partners (*commandites*) who are jointly and severally liable, and limited partners (*commanditaires*) who have only a limited responsibility.

Frequency of Shareholders' Meetings

143. There are two types of general meetings—ordinary and extraordinary. At least one ordinary meeting must be held annually, no later than six months after the end of the fiscal year, to approve the financial statements. The agenda of an ordinary general meeting addresses matters such as the election of directors and the election of statutory auditors every six years.

144. An extraordinary meeting must be called for capital increases or reductions, changes in the articles of incorporation, and approval of mergers and similar transactions.

Liabilities of Shareholders and Directors

145. A shareholder is only liable for any amount unpaid on his or her shares. Directors are at risk for—

a. Civil liability in cases of violation of legal or regulatory duties, violation of a clause in the articles of association, or breach of the management's duty of care. The 1966 law permits the tribunal to allocate a different proportion of damages to different directors depending on their degree of fault.

b. Criminal liability when they knowingly distribute illegal dividends, use fraudulent accounting records, knowingly publish an inaccurate balance sheet to defraud shareholders, appropriate corporate funds for their own use, or use their powers contrary to the interest of the company or to benefit another company in which they have an economic interest.

Legal Reserves

146. Under the 1966 law (until a maximum 10 percent of the share capital is legally reserved), 5 percent of each year's profit, less losses carried forward, must be retained in legal reserve.

Branch of a Foreign Company

147. A branch of a foreign enterprise is not recognized under French law as a separate legal entity. It is subject to income tax on the results of its operations in France. It is managed by one or more managers (*gérants*), whose powers are defined by the foreign head office.

148. A subsidiary may be organized as a French corporation having a separate legal identity and, therefore, subject to the same legal and tax treatments as any domestic French company. To create a branch in France, it is necessary to—

a. Obtain an authorization of direct investment from the Treasury Department. Two types of procedures apply according to the origin of the investor. Members of EC countries benefit from simplified formalities.

b. File with the clerk of the Commercial Court two copies, translated into French, of the articles of incorporation of the foreign head-office company.

c. File the following documents with the Commercial Register:
   —A commercial lease or a valid proof of address.
   —Commercial cards (giving the right to exercise a merchant activity) for the chairman of the board of directors of the non-EC foreign head-office company and for the manager of the branch, if he or she is not an EC national (nationals of EC countries do not need a commercial card).
   —Declaration to tax and other authorities.

149. No minimum capital is required to create a branch. However, before delivering the authorization of direct investment, the Treasury checks that the amount of invested capital is sufficient to cover the branch's capital expenditure and operating expenses for between three and six months.

150. Accounting requirements are the same as those applicable to SARLs, and no statutory audit is required (except for branches conducting banking activities).

Partnership Entities

151. A partnership is a legal entity under French law. In the absence of a contrary provision in the articles of incorporation,

partners have the power to incur liabilities on behalf of the other partners, to manage the partnership, and to dissolve it. In addition to the normal basis for dissolution of a company, a partnership will be dissolved upon the death, incapacity, or bankruptcy of a partner, unless otherwise provided in the articles of incorporation.

152. Requirements for maintaining books and records and for designating a statutory auditor are similar to those applicable to SARLs. Following are the two basic types of partnerships:

a. A *Société en Nom Collectif* (SNC) is a general partnership in which all partners are jointly and severally liable for an unlimited time for the debts and obligations of the partnership. Profits and losses of an SNC are shared in accordance with the partnership agreement.

b. A *Société en Commandite Simple* (SCS) is a limited partnership without shares in which there are two classes of partners: general partners and limited partners. In the SCS, limited partners' interests may only be transferred with the consent of all partners.

Other Forms of Business Organization

Entreprise Individuelle

153. In an *entreprise individuelle* (sole proprietorship), the business is managed under the sole responsibility of an individual who is personally liable for business debts to the extent of all of his or her business and personal assets.

Entreprise Unipersonnelle

154. *Entreprise unipersonnelle à responsabilité limitée*, or EURL (individual limited liability company), was created by a law issued in July 1985 to limit the risks encountered by individuals when they practice as sole proprietors. The EURL generally follows normal SARL rules.

Groupement d'Intérêt Economique

155. A *groupement d'intérêt économique*, or GIE (economic interest grouping), is essentially a means of consolidating certain services and equipment (such as research activities, market studies, common advertising campaign) among enterprises for economic reasons.

Members of a GIE are jointly and severally liable for its debts. Its activities must be limited to the same general line of business as its members or be an extension of their business activity.

REQUIREMENTS FOR PUBLIC SALES OF SECURITIES AND REQUIREMENTS FOR LISTING SECURITIES ON THE STOCK EXCHANGE

156. The requirements for public sales and for listing securities on the stock exchange are mainly contained in the recommendations issued by the *Commission des Opérations de Bourse.*

Registration Requirements for Public Sale

157. A public sale of securities (*offre publique de vente*) may only concern already listed securities. The following conditions must be fulfilled:

a. Prior approval must have been obtained from the brokers' professional association. This association examines the conditions of the offer (which must represent at least 10 percent of the share capital and have a value of at least FF 5 million, or 5 percent of the share capital and a value of FF 10 million) and, in certain instances, may also ask for some guarantees by the offerer.

b. Preparation of a prospectus (*note d'information*) must be approved by the COB. It includes all relevant information and financial information (financial statements, significant financial information, operating results, and consolidated statements) of the last five years. This information should be examined by the company's statutory auditor.

Requirements for Listing Securities on the Stock Exchange

158. In order for securities to qualify for quotation on the French Stock Exchange, a company must file a request with both the *Commission des Opérations de Bourse* and the brokers' professional association (*Société des Bourses Françaises).*

159. To qualify, the company must show that it is both profitable and expanding and of sufficient interest to the public. The company must offer to the public at least 25 percent of its share capital, representing at least 80,000 shares. If a company offers more than 600,000 shares to the public and has a share capital of at least 30 million francs, the 25 percent rule does not apply.

160. The following documents must be prepared:

a. For filing with the brokers' professional association, the company must provide information on the economic and financial activities of the company, details (form and value) of the proposed shares, and a copy of the articles of association of the company. The brokers' professional association examines the proposed listing and submits its conclusions to the COB.

b. For filing an admission request (*demande d'admission*) with the COB, the company must provide the required details (number, origin, price, etc.) of the proposed shares and a draft prospectus, including all information relating to the operation, the issuer, its activity, its board of directors, direction and control, and its recent history and forecasts. Historical financial information must also be included, showing the financial statements of the last three years and a summary of significant financial information and results of operations of the last five years. Consolidated information must also be presented. Financial information, including financial statements, must be examined by the company's statutory auditors.

161. The COB may approve listing of the shares on the quoted market, on the Unlisted Securities Market (USM, or *second marché*), or on the over-the-counter market. Medium-size companies that do not comply with requirements for listing on the stock exchange may ask to be quoted on the Unlisted Securities Market. They must offer to the public at least 10 percent of their share capital and arrange to comply, within a three-year period, with certain requirements regarding quality of reporting. These requirements also apply to companies that have securities listed on the over-the-counter market.

162. Once approval has been received, the company publishes a notice of sale in the *Bulletin d'Annonces Légalès Obligatoires* (BALO), announcing the availability of the prospectus. All prospective buyers must have the opportunity to obtain the prospectus.

163. Press releases and press conferences may be organized to publicize the offering. However, no information may be given at these meetings unless already contained in the prospectus.

Filing of Annual Financial Reports and Other Significant Information

164. Publicly traded companies must publish in the *Bulletin d'Annonces Légales Obligatoires*—

a. Within forty-five days of the end of each quarter, the total revenues (excluding VAT) for that quarter and for each of the preceding quarters of the year, and the corresponding figures for the preceding year. Consolidated revenues must be presented when a company has an obligation to publish group accounts.

b. Within four months of the end of the first six months, a summarized income statement (*tableau d'activité et de résultat*), together with a management report on the operations of the first six months.

c. Within four months of the year end and at least fifteen days before the annual shareholders' meeting—
- An unaudited draft of the annual financial statements.
- The proposed resolution for allocation of the profits between dividends, legal, and other reserves.
- Consolidated financial statements (when available).

d. Within forty-five days of the shareholders' meeting and in case of changes in the information previously published—
- Final annual and consolidated financial statements.
- Opinion of the statutory auditors.
- Final allocation of profits approved by the shareholders. If no changes are made, the announcement must indicate that the financial statements were approved together with opinion given by the *commissaire aux comptes.*

165. This information is also required for subsidiaries with total assets of over FF 20 million or investments with a market value of over FF 2 million.

SELECTED ECONOMIC DATA

166. Key demographic and social factors, based on 1990 French census data (unless otherwise indicated), follow:

Area (in thousands of square kilometers)	552
Population (in millions)	56.5
Labor force (in millions), as of 1989	22.2
Birthrate (per population of 1,000), as of 1989	13.6
Life expectancy (in years)	
Men	72.4
Women	80.9
Gross domestic product (in billions)	US$1.19
Internal debt (in billions), as of 1989	FF1.76
Per capita income	US$19,480
Inflation rate	3.4%

167. The major French trading partners, as of 1990, are as follows:

	Imports (FF billions)	*Exports (FF billions)*
Germany	238.7	196.8
Italy	146.5	129.9
Belgium/Luxemburg	111.8	107.3
United States	103.2	69.6
United Kingdom	91.8	108.1
Spain	59.6	72.5
Other	515.2	458.0
	1,266.8	1,142.2

168. French primary import and export products for 1990 are as follows:

	Imports (FF billions)	*Exports (FF billions)*
Semi-finished products	317.7	288.9
Machinery and equipment	298.1	273.4
Consumer goods	207.8	176.2
Food processing products	88.4	105.0
Agricultural products	50.5	85.0
Other	304.3	213.7
	1,266.8	1,142.2

TAXES

Principal Types

169. There are four types of taxes in France.

Taxes on Income

170. Taxes on income comprise—

a. Corporate income tax based on taxable profit of companies established in France. A standard rate of 34 percent has been in effect since January 1, 1991 (37 percent in 1990; 42 percent in 1989). Reduced rates of 15 percent, 19 percent, and 25 percent are applicable to long-term capital gains, depending on their nature.

b. Under certain conditions, a company that owns 95 percent or more of a subsidiary may compute its income tax on a consolidated basis. When this option is utilized, it applies for a minimum of five years. If the subsidiary is sold or excluded from consolidated tax results before the end of the five-year period, the company may have to pay additional taxes on its income previously reduced (for example, if the company utilized a tax deficit of the subsidiary in prior years).

c. Personal income tax, the calculation of which is based on a system of brackets (*tranches*) with rates ranging from 0 to 56 percent.

Taxes on Transactions

171. Taxes on transactions comprise—

a. VAT (sales tax), which varies from 5.5 percent to 22 percent according to the nature of the item to which it applies.

b. Registration taxes paid on transactions such as formation, reorganization of companies, or transfer of real estate property. The basic rate is 11.4 percent, to which local taxes are added. A reduced rate of 1 percent or a fixed fee may apply to special transactions.

c. Insurance tax, which is payable by the insurer on insurance contracts with rates ranging from 0.25 percent to 30 percent.

d. Inheritance taxes (*droits de succession*), which are payable based on the value of a person's estate having taxable value in France. Tax rates are progressive and based on the relationship of the beneficiary to the deceased.

e. Customs duties and taxes.

Payroll Taxes

172. Payroll taxes are paid by employers and are generally based on gross wages and salaries. They include—

a. Salary tax (*taxe sur les salaires*), which only applies if the value added tax is not applicable.

b. Apprenticeship tax (*taxe d'apprentissage*), at a rate of 0.5 percent.

c. Employee training tax (*taxe de formation professionnelle*), at a rate of 1.4 percent for 1992 and 1.5 percent after January 1993.

d. Housing construction tax (*taxe de construction*), at a rate of 0.45 percent.

e. Social security, pension, and unemployment contributions, which are paid to different governmental agencies.

Local Government Taxes

173. Local government taxes vary according to the revenue requirements of the local authorities (region, department, or municipality). The principal local government tax is the business tax (*taxe professionnelle*). Its amount is based on the rental value of fixed business assets (for example, property, plant, and equipment) and the total amount of wages paid.

Tax Returns

174. Corporation tax is paid in installments during the year based on the previous year's taxable income and is adjusted after the tax return is filed. The annual corporate income tax return is the sole responsibility of the taxpayer, who may use outside assistance for preparation. The corporate income tax return must be filed within three months following the close of each fiscal year.

175. The same set of financial statements is used for accounting and tax requirements.

APPENDIX A

Publications of the *Compagnie Nationale des Commissaires aux Comptes*

The following translated publications relating to auditing have been issued:

Members' Handbooks

- *Normes et commentaires des normes*—Basic information for the conduct of the audit.
- *Encyclopédie des controles comptables*—Best current practice concerning all aspects of auditing.
- *Etudes juridiques*—Legal aspects of the audit of the *commissaires aux comptes.*

Notes d'informations

1. General report (1988)
2. Special report (1991)
3. Evaluation of internal control (1984)
4. Direct confirmation (1991)
5. Inventory observation (1984)
6. Analytical review (1986)
7. Early-warning procedure (1985)
8. Going-concern principle (1987)
9. Specific controls (1987)
10. Forecasts documentation (1987)
11. Representation letter (1988)
12. Approach and organization of audit engagements (two volumes, 1988)
13. Orientation and planning of audit engagements (1988)
14. Consistency in application of accounting principles (1989)
15. Subsequent events (1989)
16. Duties of statutory auditors appointed to appraise contributions in kind or in case of mergers (1989)
17. Statutory audits in small companies (1990)
18. Sampling auditing (1991)

Standards (contained in the *Normes et commentaires des normes*)

Introduction	General Features of Engagements
Chapter 1	Code of Duties and Professional Care
Chapter 2	Statutory Audit Standards
Chapter 3	Specific Duties Standards
Chapter 4	Other Legal Engagement Standards

APPENDIX B

Publications of the *Ordre des Experts-Comptables et des Comptables Agréés*

Following are the three types of translated recommendations issued by the OECCA:

Accounting Principles

Number	*Title*	*Issued*
1.01	*Provisions and Reserves* (superseded)	1965
1.02	*Accounting for VAT* (superseded)	1966
1.03	*Depreciation of Fixed Assets**	1967
1.04	*Accounting for Capital Loss and Capital Gain* (superseded)	1967
1.05	*Accounting Information to be Prepared* (superseded)	1968
1.06	*Accounting for Commitments*	1968
1.07	*Statement of Changes in Financial Position**	1969
1.08	*Year-End Inventory**	1969
1.09	*Matching of Costs and Revenues**	1969
1.10	*Accounting for Bank Loans**	1971
1.11	*Losses on Long-Term Contracts*	1981
1.12	*Subsequent Events*	1982
1.13	*Accounting for Non-Interest Bearing Receivables**	1982
1.14	*Accounting for Business Combinations*	1984
1.15	*Changes in Accounting Principles*	1984
1.16	*Accounting for Pension Costs and Other Similar Benefits in the Employer's Financial Statements*	1985
1.17	*Preparation and Presentation of Forecasts*	1985
1.18	*Provisions*	1986
1.19	*Matching of Financial Costs and Revenues*	1987
1.20	*Accounting for Income Tax*	1987

*The publication is under review, which means its application to financial data is suspended and thus it is no longer compulsory. It has not, as yet, been formally superseded.

Number	Title	Issued
1.21	*Distinction Between Ordinary and Extraordinary Results*	1988
1.22	*Statement of Changes in Financial Position*	1988
1.23	*Pension Costs Calculation Methods*	1990
1.24	*Commitments and Contingent Assets and Liabilities*	1991
1.25	*Accounting for Revenues*	1991

Engagements

Number	Title	Issued
	Accounting Work	
21.01	*Preparation of the Financial Statements by External Accountant*	1984
21.02	*Due Care in Preparing the Financial Statements*	1984
21.03	*Engagement Letter and Terms and Conditions of Engagements*	1984
21.04	*Reporting on Work Performed*	1984
21.05	*Characteristics of Accounting Work in an EDP Environment*	1985
21.06	*Procedural and Organizational Manual*	1988
21.07	*The General Journal and General Ledger*	1988
	Contractual Auditing	
22.01	*Contractual Auditing Standards**	1966
22.02	*Auditing Inventories and Work in Progress**	1979
23.03	*Direct Confirmation**	1970
22.04	*Auditing Investments**	1975
22.05	*Auditing Consolidated Accounts**	1973
22.06	*Auditing Contributions of Assets and Liabilities in Business Combinations**	1973
22.07	*EDP Auditing:* 1—*General Principles* 2—*Effect of an EDP Environment on the Study and Evaluation of the Internal Control* 3—*Computer-Assisted Audit Techniques*	1985
22.08	*Materiality Concepts**	1976
22.09	*Auditing General and Administrative Expenses* (superseded)	1978
22.10	*Bank Confirmations*	1979
	EDP	
23.01	*Control of EDP Contracts with Service Bureau*	1984
23.02	*Assistance to EDP Implementation:* 1—*Participation of the External Accountant* 2—*Engagement Letter*	1984

*See note on page 57.

Number	Title	Issued
	3—Due Care	
	4—Reporting on Work Performed	
23.03	*Evaluation of EDP Systems:*	1985
	1—Participation of the External Accountant	
	2—Engagement Letter	
	3—Due Care	
	4—Reporting on Work Performed	
	Other Engagements	
24.01	*Relations with Labor Union Committee*	1986
24.02	*Auditing Standards of Budgets and Forecasts*	1986

Professional Behavior

Number	Title	Issued
3.01	*General Principles*	1985
3.02	*Recommendations Regarding Publicity by Public Accountants*	1986
3.03	*Workpaper Files of the External Accountant*	1987
3.04	*Training of a Public Accountant*	1989

APPENDIX C

Illustrative Auditor's Report and Financial Statements

The following translated financial statements are intended for illustrative purposes only. The statements presented are not intended to include all information that French law requires.

STATUTORY AUDITOR'S REPORT ON CONSOLIDATED ACCOUNTS
For the fiscal year ended March 31, 1991

To the Shareholders of Rémy & Associés,

In execution of the assignment that was entrusted to us by your general meeting, we are presenting to you our report on—

- The audit of consolidated accounts of Rémy & Associés.
- The verifications of the management report on the activities of the Group, for the fiscal year ended March 31, 1991.

1. Opinion on the Consolidated Accounts

We made an audit of the consolidated accounts by applying the auditing procedures that we have deemed necessary according to the standards of the profession.

We certify that the consolidated accounts are regular and sincere and give a true view of the patrimony (assets and liabilities) and the financial position, and of the result of operations of the companies included in the consolidated accounts.

2. Specific Verifications

We have also performed, according to the standards of the profession, the specific verifications prescribed by the law.

We have no observation to formulate on the sincerity and the conformity with the annual accounts of the information given in the management report of the board of directors on the activities of the Group.

Paris, July 16, 1991

The Statutory Auditors

Guy Baibier & Autres Member of the Arthur Andersen Worldwide Organisation	Auditeurs Associés et Conseils Member of DFK International

The Auditors

Arthur Andersen & Co
An Illinois, USA Partnership

CONSOLIDATED BALANCE SHEETS
(expressed in thousands of French francs)

Assets

		As at March 31, 1991	1990
Fixed assets			
Intangible assets	Note 4.1	1,165,721	993,388
Depreciation		(38,149)	(33,445)
		1,127,572	959,943
Goodwill on acquisition	Note 4.3	348,521	437,484
Depreciation		(65,651)	(56,691)
		282,870	380,793
Tangible assets	Note 4.2	737,844	724,359
Depreciation		(279,834)	(299,138)
		458,010	425,221
Investments	Note 4.4		
Investment in subsidiaries and affiliates			
Consolidated by equity method		—	13,583
Non-consolidated		99,009	244,566
Other investments		21,779	104,388
		120,788	362,537
Total fixed assets		1,989,240	2,128,494
Current assets	Note 4.5		
Inventories		2,322,880	1,980,429
Trade receivables and associated accounts		1,169,652	768,409
Other receivables		374,371	335,876
Cash and marketable securities		308,853	149,615
Accruals		120,823	94,063
Total current assets		4,296,579	3,328,392
Total assets		6,285,819	5,456,886

(Continued on next page)

CONSOLIDATED BALANCE SHEETS *(cont.)*

Liabilities

		As at March 31,	
		1991	*1990*
Shareholder's equity	Note 4.6		
Capital		918,253	909,091
Share premiums		428,309	411,761
Reserves		211,888	106,425
Consolidation reserve		292,850	277,117
Conversion differences		(77,010)	(96,458)
Consolidated net income (Group share)		102,281	157,560
		1,876,571	1,765,496
Minority interest		306,721	150,437
		2,183,292	1,915,933
Deferred income tax	Note 4.7	7,951	65,054
Reserves for losses and contingencies	Note 4.8	83,791	88,748
Debt			
Long- and medium-term	Note 4.9	732,384	1,585,703
Short-term		1,723,175	942,901
		2,455,559	2,528,604
Operating debt			
Trade accounts payable and related accounts		487,006	474,839
Other debt and accruals	Note 4.10	1,068,220	383,708
		1,555,226	858,547
Total liabilities		6,285,819	5,456,886

CONSOLIDATED STATEMENT OF INCOME
(expressed in thousands of French francs)

		Year ended March 31,	
		1991	*1990*
Sale of merchandise	Note 4.11	4,418,219	4,302,963
Other income	Note 4.12	328,632	222,301
		4,746,851	4,525,264
Purchases and inventory variation		(2,619,002)	(2,532,010)
Operating expenses		(1,632,852)	(1,545,777)
Charges to depreciation		(56,217)	(80,454)
Charges to reserves		(21,446)	(13,841)
Total operating expenses		(4,329,517)	(4,172,082)
Operating income		417,334	353,182
Financial results	Note 4.13	(248,171)	(160,714)
Non-current results	Note 4.14	12,431	79,090
Pre-tax income for globally integrated companies		181,594	271,558
Income tax	Note 4.15	(58,859)	(71,028)
Net profit for globally integrated companies		122,735	200,530
Share in profit of companies consolidated by equity method		—	(131)
Minority interests		3,350	(14,161)
Profit before amortization of goodwill		126,085	186,238
Amortization of goodwill on acquisition		(23,804)	(28,678)
Consolidated net profit (Group share)		102,281	157,560

CHANGES IN CONSOLIDATED SHAREHOLDERS' EQUITY AND MINORITY INTERESTS

For the year ended March 31, 1991
(expressed in thousands of French francs)

		Group Shareholders' Equity	*Minority Interest*	*Total*
Balance at March 31, 1990		1,765,496	150,437	1,915,933
Change in conversion adjustment	Note 1.3	19,448	281	19,729
Impact of changes in consolidation scope and percentage variations		—	171,506	171,506
Capital increase		25,710	—	25,710
Dividends:				
Rémy & Associés S.A.		(36,364)	—	(36,364)
Other companies		—	(12,153)	(12,153)
Net profit for period		102,281	(3,350)	98,931
Balance at March 31, 1991		1,876,571	306,721	2,183,292

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION*
(expressed in thousands of French francs)

	Year ended March 31, 1991	1990
Sources		
Consolidated net income	98,931	171,721
Charges to depreciation and reserves (net of reversals)	105,120	128,422
Deferred income tax	(51,072)	(32,510)
	152,979	267,633
Applications		
Variation in cash requirements:		
Inventories (gross)	360,532	124,576
Trade accounts receivable (gross)	406,068	61,100
Other receivables and accruals (gross)	135,975	170,896
Current liabilities	(113,251)	(299,285)
	789,324	57,287
Net increase (decrease) in tangible assets	13,485	13,351
Net increase (decrease) in goodwill on acquisition, intangible assets, and investments	(59,468)	185,983
	743,341	256,621
Excess of Applications Over Sources	590,362	(11,012)

Funding

	1991	1990
Increase in capital of Rémy & Associés S.A. from:		
• payment of dividends	25,710	20,530
• conversion of bonds	–	168,753
Debt	(73,045)	(29,437)
Current financial accounts with associate companies	654,217	12,632
Minority interests	171,506	(37,850)
Dividends	(48,517)	(28,171)
Increase (decrease) in conversion difference	19,729	(64,576)
Cash	(159,238)	(52,893)
	590,362	(11,012)

*Recent recommendations issued by the OECCA (Order of Accounting Experts and Qualified Accountants) allow for the presentation of a statement of cash flows similar to Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards No. 95.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
as of March 31, 1991

The consolidated financial statements have been prepared in accordance with current French legislation and rules concerning consolidation, which do not differ materially from IASC accounting standards.

The consolidated financial statements were approved by the Board on July 15, 1991.

1. Consolidation Principles and Rules

1.1. Consolidation Principles

Companies over which Rémy & Associés has exclusive control, resulting from one or other of the following—

- Direct or indirect capital interest exceeding 50%
- Effective power of management

are consolidated by the global integration method.

Companies over which Rémy & Associés has a notable influence and holds, directly or indirectly, a capital interest of between 20% and 50%, are accounted for by the equity method.

These principles only apply to companies of material importance.

Non-consolidated subsidiary/affiliate investments are included under non-consolidated investments in subsidiaries and affiliates at acquisition price, less appropriate provisions for adjustment to going-concern value, where appropriate.

Going-concern value is quantified on the basis of a number of criteria, including net assets and profitability potential.

1.2. Goodwill on Acquisition

Goodwill amounts correspond to the difference between acquisition price and pro rata shareholders' equity value (restated in accordance with Group consolidation rules) recognized at the time of acquisition of the investment, or at a date close to this event. The subsidiaries concerned are accounted for as follows:

- Excess costs at date of acquisition that can be individualized are posted to the appropriate asset.
- This covers tangible and intangible assets, brands, distribution rights, and inventories; any residual amount not so posted is included under goodwill on acquisition. Goodwill on acquisition is amortized in the statement of income, over periods not exceeding 30 years.

1.3. Conversion of Financial Statements and Transactions in Foreign Currencies

The balance sheets of foreign subsidiaries are converted into French francs at the exchange rate in effect at end of period. Statements of income are converted at the weighted-average exchange rate for the period. Any resultant exchange differences are included in shareholders' equity under conversion differences.

Transactions conducted in foreign currencies are recorded at the exchange rate in effect at the date of the transaction. The balance of assets and liabilities denominated in foreign currencies is converted at the exchange rate in effect at end of period. Deferred asset conversion differences are covered by a reserve for contingencies.

1.4. Deferred Income Tax

The Group uses the liability method for calculating deferred income tax, applying the rate of taxation at the date of the fiscal year end.

Restatements applied to the individual financial statements of consolidated companies, in order to achieve homogeneity with the accounting principles of the Group, or to eliminate the effect of local tax laws (elimination of reserves for price increases, in particular), as well as the existence of taxation timing differences, generate differences between taxable and consolidated pre-tax profit. These differences lead to recognition of deferred income tax, for which the net balance, provided all components of this balance are of the same nature and similar maturity date, is shown as a balance sheet liability.

No reserve is made for possible tax due by the Group on subsidiary dividend payments, except in the case where a dividend payment has already been decided prior to the closure date for the consolidated financial statements. Dividend distribution tax is included for the period during which the dividend is paid.

2. Accounting Principles and Valuation Methods

2.1. General

The financial statements of consolidated companies, prepared in accordance with rules in each of the countries concerned, are restated prior to consolidation in order to achieve homogeneity with Group accounting principles. Inter-company accounts and intra-Group operations, and any resultant profit/loss, have been eliminated.

2.2. Intangible Assets

This covers the value of brands and distribution rights resulting from appropriation of excess cost over underlying book value at date of acquisition. The amounts appropriated are determined on the basis of objectively verifiable criteria. Brands are not depreciated insofar as they are legally protected, make it possible to generate more profit than do other identical products not carrying a brand name, and have an effective life that is not limited in time. Annual valuation rules, based on specific criteria adopted at the time of acquisition, are applied. Where appropriate, any durable loss of brand value is provided in the statement of income for operating periods during which any such loss is observed.

A similar principle is applied for distribution rights.

Other intangible assets (essentially lease renewal rights and distribution contract cancellation indemnities) are amortized by applying the straight-line method over a maximum period of 10 years.

2.3. Tangible Assets

Tangible assets are shown on the balance sheet at acquisition price after appropriation of excess cost over underlying book value where appropriate. Fixed assets are depreciated for consolidation purposes by the straight-line method over the following estimated lifetime periods:

Buildings	20 to 50 years
Plant, equipment, and tooling	5 to 10 years
Other tangible assets	5 to 10 years

2.4. Inventory

Inventory items are valued at the lower of cost and are determined according to the weighted-mean method or net realizable value.

Where applicable (Champagne branch in particular), inventory value includes the amount appropriated on reallocation of excess cost over underlying book value.

2.5. Pensions and Other Commitments With Respect to Personnel

Where pension plans or other specific commitments exist and must be serviced by certain Group companies, corresponding commitments are accrued in full, as a general rule, on the basis of estimated rights acquired by personnel at the close of the fiscal year.

2.6. Hedging for Exchange and Interest-Rate Risks

The Group uses certain financial instruments for hedging its exchange and interest-rate risks. These instruments essentially comprise forward selling of foreign currencies, exchange options, and interest-rate swaps.

The accounting methods adopted for valuation of, and accounting for, these financial instruments are those generally accepted for hedging transactions.

3. Information Concerning Consolidation Scope and Level of Investment in Subsidiaries/Affiliates

3.1. Changes in Consolidation Scope and Level of Investment in Fully Integrated Companies

Changes occurred in the level of investment in consolidated companies during the operating period. These changes principally concerned—

—The restructuring of the financial activity of Rémy & Associés, as authorized by the Board on August 1, 1990.

— The acquisition of minority interests in La Gestion Mobilière S.A.
— A capital increase for companies in the Wines branch, the new stock issued being subscribed by third parties outside the Group.
— The merger of Cointreau America Inc.

Since these companies were already consolidated, the changes in investment levels had no impact on the consolidated financial statements, apart from the generation of goodwill on acquisition and a different Group share interest in the shareholders' equity and consolidated profit of the companies concerned. Nevertheless, certain of these transactions generated non-current profit for the operating period.

4. Information Concerning the Consolidated Balance Sheet and Statement of Income

4.1. Intangible Assets

Details of Intangible Assets (In thousands of French francs)	*1991*	*1990*
Brands	1,035,829	892,423
Distribution rights	64,599	63,812
Other intangible assets (net of amortization)	27,144	3,708
	1,127,572	959,943

The Brands line essentially comprises Piper Heidsieck Group brands (Piper Heidsieck, Heidsieck, and Piper Sonoma), the Charles Heidsieck brand, and the 21 Brands Group (Galliano and Mount Gay, in particular).

Distribution rights result from inclusion of the 21 Brands Group and Mount Gay in the consolidation scope during the operating period ending March 31, 1990.

For the most part, brands and distribution rights were valued on appropriation of excess cost over underlying book values for the companies owning the brands and distribution rights concerned.

The goodwill generated in the case of Charles Heidsieck, and shown previously under goodwill on acquisition, was amortized up to March 31, 1990, on the basis of a twenty-year period.

4.2. Tangible Assets

Details of Tangible Assets (In thousands of French francs)	*Gross*	*Depreciation or Reserve*	*Net*
Land	71,020	(2,359)	68,661
Buildings	343,849	(108,318)	235,531
Other tangible assets	320,778	(169,157)	151,621
In process	2,197	—	2,197
	737,844	(279,834)	458,010

Change in Tangible Assets and Depreciation (In thousands of French francs)	*Gross Value*	*Depreciation*
Balance at March 31, 1990	724,359	299,138
Acquisitions	89,339	–
Disposals	(101,677)	(77,519)
Charges for the period	–	56,217
Impact of changes in consolidation scope and monetary fluctuations	25,823	1,998
Balance at March 31, 1991	737,844	279,834

Breakdown of Tangible Assets by Geographical Zone (Net book value)	
France	245,086
Europe	37,692
North America	112,114
Pacific	63,118
	458,010

4.3. Goodwill on Acquisition

Goodwill on acquisition (non-appropriated residual excess cost of acquisition over underlying book value) principally concerns the Champagne branch.

4.4. Investment in Non-consolidated Subsidiaries and Affiliates and Other Financial Assets

The reduction in investment in non-consolidated subsidiaries and affiliates is principally due to the transfer by Krug Rémy Cointreau Amérique of its investment in Macallan, and convertible bonds issued by the latter, to its parent company, Pavis. This sale was made at market value for the stock and convertible bonds plus financial expenses incurred since the date of acquisition.

The drop in other investments is principally due to the reimbursement of a blocked current account.

4.5. Current Assets

Certain current assets items are covered by reserves. Inventories are shown net of a valuation allowance.

Trade receivables and associated accounts are also shown net of a reserve for doubtful debts.

4.6. Capital

The capital of Rémy & Associés SA was represented, as at March 31, 1991, by 9,182,533 fully paid up shares.

4.7. Deferred Income Tax

The amount of deferred income tax due is as follows:

Deferred income tax asset	38,209
Differed income tax liability	(46,160)
	(7,951)

4.8. Reserves for Losses and Contingencies (in thousands of French francs)

	1991	*1990*
Reserve for pension costs	41,930	39,528
Reserve for contingencies	41,861	49,220
	83,791	88,748

The reserve for pension costs covers the cost of all specific commitments, as serviced by Group companies.

Reserves for contingencies cover various risks, none of which is individually material, for which accruals have been made by Group companies.

4.9. Long- and Medium-term Debt

Long- and medium-term debt breakdown (In thousands of French francs)	*1991*	*1990*
Bonded and participating loans:		
1986 bonded loan, denominated in ECU, subject to interest at 7.625% and maturing in January 1992.	–	275,283
1986 bonded loan, subject to interest at Libor rate plus 0.0625%. The bonds carry an option for conversion of the variable interest rate to a fixed rate of 8.125%. This bonded loan is reimbursable by two annual payments of 100,000 each, in December 1992 and December 1993.	200,000	300,000
1989 bonded loan subject to interest at a fixed rate of 4.5% and maturing in July 1996. Rémy & Associés SA has transferred 212,000 Piper Heidsieck shares to its subsidiary, Rémy Finance, for this purpose.	438,358	419,380
Subtotal	638,358	994,663
Other bonded and participating loans	26,038	18,306

(Continued on next page)

	1991	*1990*
Other borrowing:		
Various medium-term borrowing, subject to interest at rates indexed to the money market, and maturing between July 1990 and March 1994	50,000	550,000
Other long- and medium-term borrowing	17,988	22,734
	67,988	572,734
	732,384	1,585,703

Maturities for long- and medium-term debts are as follows:

Operating Period	*Bonded and Participating Loans*	*Other Debt*	*Total*
1992/93	100,000	54,605	154,605
1993/94	114,754	1,425	116,179
1994/95	2,786	1,813	4,599
1995/96	8,498	1,201	9,699
after 1997	438,358	8,944	447,302
	664,396	67,988	732,384

Short-term maturities are shown separately on the balance sheet. Rémy & Associés SA also holds a total of 2 billion French francs of unused, confirmed medium-term credit lines.

4.10. Other Operating Debt

Other operating debt includes debt with associated companies.

4.11. Net Sales

Geographical Breakdown of Consolidation Net Sales (%)

	1991	*1990*
France	16	16
Other European countries	27	30
North America	21	22
Pacific	34	30
Other	2	2
	100	100

Breakdown of Net Sales by Activity (%)

	1991	*1990*
Cognac	47	44
Champagne	18	19
Other wines, spirits, and misc.	35	37
	100	100

4.12. Other Income

Up to March 31, 1990, advertising expenses incurred by the distribution subsidiaries were billed out directly by the latter to the production companies, on a direct basis.

Following modification of the management assistance agreement, signed by the production companies and Rémy & Associés SA and extended to include marketing support under the terms of an additional clause included during the operating period, advertising expenses are now billed out by the distribution subsidiaries to Rémy & Associés SA, which in turn bills these expenses to the production companies.

The increase in other income principally results from the extension of this agreement to include the coordination of advertising expenditure.

This line thus includes an amount for advertising expenses billed out to Rémy Martin & Cie, and recorded under operating expenses by consolidated companies. The change in billing method resulting from this additional clause has had no significant impact on operating profit, insofar as this change has been part of the reorganization of intra-Group price policy.

4.13. Financial Income (in thousands of French francs)

	1991	*1990*
Profit (loss) on exchange	(49,445)	18,699
Financial income (interest)	(198,726)	(179,413)
	(248,171)	(160,714)

4.14. Non-current Results

Breakdown of non-current results (In thousands of French francs)	*1991*	*1990*
Capital gain on disposal of casks	—	30,635
Capital gain from restructuring the capital of the Seguin Moreau cooperage	—	13,336
Restructuring of the financial activity	7,491	—
Restructuring expenses and net capital gains resulting from third party subscriptions to capital increases of the Wines branch companies	29,909	—
Capital gain on disposal of GFDVB Stock	—	40,025
Other (losses)	(24,969)	(4,906)
	12,431	79,090

4.15. Income Tax (in thousands of French francs)

	1991	*1990*
Income tax due	109,931	103,538
Deferred income tax	(51,072)	(32,510)
Total tax charge for the period	58,859	71,028
of which: tax on non-current income	(2,263)	15,072
tax on operating profit	61,122	55,956

Tax on current profit has been calculated at a rate taking into account the forecast of dividend payments to be made by each French company. As in previous years, the change in deferred income tax takes into account the decrease in the tax rate applicable to French companies, from 37% to 34%.

4.16. Off-balance Sheet Commitments and Litigations

Litigations exist regarding certain Group companies, but in the opinion of company management and its legal advisers, none are likely to result in a material liability at consolidated level, other than those already accrued.

Given the use of financial instruments for hedging exchanges risks (see Note 2.6), Group exposure to exchange rate fluctuations for all foreign currencies is not significant.

APPENDIX D

Checklist for Comparison of Generally Accepted Auditing Standards (GAAS) in the United States With Auditing Standards in France

General Information	Answer	Comments
1. Is a primary purpose of an audit—		
a. To attest to information used by investors, creditors, etc.?	Yes	
b. To satisfy statutory requirements (for example, the Companies Act)?	Yes	1*b.* Requirement included in art. 228 of Company Law of July 24, 1966
c. For tax purposes?	No	
2. A. The United States has ten generally accepted auditing standards, including general standards, standards of field work, and standards of reporting. Those standards and their interpretations constitute U.S. generally accepted	Yes	

Notes:

Checklist should be completed from the perspective of performing a local audit, *not* a referral audit.
AU numbers refer to sections in the *Codification of Statements on Auditing Standards,* unless otherwise noted.
This checklist does not include the latest GAAS pronouncements issued in the United States.

General Information	Answer	Comments
auditing standards, which have been published in *Codification of Statements on Auditing Standards*. Do generally accepted auditing standards exist in France?		
B. If so, are they published?	Yes	2B. In the *Normes-Commentaires-Déontologie* issued by CNCC.
C. If auditing standards exist in France, are they similar to U.S. standards?	Yes	2C. However, they are less detailed.
D. If not, what are they?		
3. Who is responsible for promulgating auditing standards (for example, the profession, a governmental body, etc.)?	The profession	3. The two professional bodies (OECCA and CNCC) issue recommendations for the use of their members. Additional comments are also done by the COB.

U.S. Generally Accepted Auditing Standards	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
4. Do auditors confirm receivables? (AU 331)	Yes. *Norme* CNCC 2103	✓			4–9. Practice varies depending on the size and nature of the company audited. These procedures are selectively conducted for major companies, including listed companies. For smaller companies, these audit techniques are not yet systematically applied.
5. Do auditors observe inventory counts? (AU 331)	Yes. *Norme* CNCC 2103	✓			
6. Do auditors receive written representations from management? (AU 333)	No		✓		

7. Do auditors receive written representations from management's legal counsel? (AU 337)	Yes. *Commentaires* CNCC 2103.4		✓	
8. A. Do auditors prepare and maintain working papers? (AU 339)	Yes. *Norme* CNCC 2105	✓		
B. If so, do they include a written audit program outlining procedures to be performed? (AU 339)	Yes. *Commentaires* CNCC 2101.19	✓		
9. Do auditors obtain a sufficient understanding of the internal control structure to plan the audit and to determine the nature, timing, and extent of tests to be performed? (AU 319)	Yes. *Norme* CNCC 2102 Booklet CNCC Internal Control	✓		
10. A. Do auditors communicate reportable conditions in the internal control structure to the audit committee? (AU 325)	Yes. *Commentaires* CNCC 2102.10	✓		10A. When weaknesses have a material effect on the accounts, relevant information may be included in art. L230 report to the board of directors.
B. If so, is the communication documented? (AU 325)	Yes. *Commentaires* CNCC 2102.10		✓	
11. In obtaining evidential matter, does the auditor apply either statistical or non-statistical procedures? (AU 350)	Yes. *Norme* CNCC 2103	✓		
12. Is the auditor responsible for designing the audit to provide reasonable assurance of detecting errors and irregularities that are material to the financial statements? (AU 316)	No	✓		12. Although the statutory auditor is not required to systematically search for all errors and irregularities (CNCC *Caractéristiques générales des missions*), the auditor should report any errors or irregularities that come to his or her attention.

U.S. Generally Accepted Auditing Standards	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
13. A. Does the auditor perform procedures to identify related-party transactions and their effects on the financial statements? (AU 334)	No		✓		13A. Although a legal obligation to report on these transactions does exist in France, the auditor is not required to perform procedures to identify related-party transactions. They form part of the special report issued by the *commissaire aux comptes* to shareholders. These transactions must have received prior approval of the board of directors, and the *commissaire aux comptes* mainly reviews the minutes of the board of directors meetings held during the year. He or she does not have to perform a special review to find them (booklet CNCC *Rapport spécial*).
B. If so, list the procedures.					
14. Does the auditor consider the adequacy of cutoff procedures to ensure that movements into and out of inventories are properly identified in the accounting records? (AU 313)	Yes. *Commentaires* CNCC 2103.05	✓			
15. A. Are specific auditing procedures applied to transactions occurring after the balance-sheet date? (AU 560)	Yes. *Commentaires* CNCC 2103.11	✓			
B. Are other auditing procedures applied to ascertain the	No		✓		

occurrence of subsequent events that require adjustment to or disclosure in the financial statements? (AU 560)				
16. The concept of "joint auditors" in certain countries (e.g., U.K., Canada, and Australia) is that two auditors or audit firms jointly audit the financial statements of a company and issue a single report signed by the two firms. This practice is not generally followed in the United States. Does the concept of "joint auditor" exist in France?	Yes. Company Law L233	✓		16. Two *commissaires aux comptes* must be appointed when the company publishes consolidated accounts.
17. When a principal auditor is reporting on financial statements that include one or more subsidiaries, divisions, branches, or investees (AU 543)—				
A. Must the principal auditor assume responsibility for the work of the other auditor as it relates to the principal auditor's opinion?	Yes. *Norme* CNCC 2106.3	✓		
B. May the principal auditor decide not to assume that responsibility by making reference to the other auditor and indicating the division of responsibility?	No		✓	
18. A. Is there a standard form of auditor's report? (AU 508)	Yes. *Norme* CNCC 2501 Company's accounts and *Normes* CNCC 2502 Consolidated accounts	✓		18A. The standard form of the report is more detailed and consequently may differ in content.

U.S. Generally Accepted Auditing Standards	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
B. List the circumstances that require a departure from the standard report and indicate the type of report required. (AU 508)					18B. *Opinion avec reserve(s)* (qualified opinion) occurs— *a.* When errors or irregularities in the application of accounting principles have been found but are not significant enough to warrant rejection of the annual accounts. *b.* When the *commissaire aux comptes* has not been able to perform all examinations deemed necessary. These limitations on the auditor's work do not prevent him or her, however, from establishing an opinion. *Réfus de certifier* (disclaimer of opinion or adverse opinion) occurs when errors and irregularities or limitations in his or her work are so important that they prevent the issuing of an unqualified opinion.
19. A. Does the auditor's report require an explanatory paragraph for a change in accounting principles or in the method of their application? (AU 508)	No			✓	
B. If not, does it imply that either consistency exists or the financial statements disclose the inconsistency?	Yes. *Code de commerce* art. 11	✓			19B. The reference is implicit in the word "regular" used in the standard report, which means "in conformity with rules and

			regulations" and thus encompasses consistency. Unless there is a consistency exception, consistency is only rarely specifically referred to in the author's report. If there is a consistency exception, then it must be specifically referred to in the opinion.
20. A. Is the auditor's report dated as of the last day of fieldwork? (AU 530)	Yes. *Commentaires* CNCC 250.03		
B. If not, what date is used?			
21. To express an opinion, must the auditor be independent? For the purpose of this checklist, independence is defined as not having a financial interest in or connection with the client. (Code of Professional Conduct, Rule 101 and its interpretations.)	Yes. *Déontologie* CNCC 11		
22. Please describe any standards in France for which there are no corresponding U.S. standards.			22. None

APPENDIX E

Checklist for Comparison of Generally Accepted Accounting Principles (GAAP) in the United States With Accounting Principles in France

General Information	Answer	Comments
1. Are there generally accepted accounting principles in France? If so, are they codified?	Yes	1. They are codified by— • Commercial code, law of April 30, 1983, as amended (hereafter C. com. art. D) and decree of November 29, 1983, as amended (hereafter C. com. art. D). • The *plan comptable général* 1982 (PCG) General Chart of Accounts.
2. Who is responsible for promulgating accounting principles (for example, the profession, a governmental body, etc.)?	See Comment	2. Accounting principles are established in law after consultation of the *Conseil National de la Comptabilité* (National Accounting Council) and of professional bodies (e.g., CNCC, OECCA). Information on the interpretation of law may be found in publications issued by the *Conseil National de la Comptabilité*, the *Commission des Operations de Bourse* (COB), CNCC, and OECCA.

Notes:

References are to section in the *FASB Current Text*, unless otherwise noted.
This checklist does not include the latest GAAP pronouncements issued in the United States.

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
3. Are assets and liabilities recorded on the historical cost basis?	Yes. C. com. art. 12	✓			
4. Are interest costs, incurred while activities that are necessary to get an asset ready for its intended use are in progress, capitalized as part of the historical cost of an asset? (I67)	Yes. C. com. art. D 7-2	✓			4. Predominant practice for companies that engage in long-term contract and in the building industry. Interest capitalized on the following: • Fixed assets • Inventories only when the manufacturing period exceeds one year (this limitation is excluded for consolidated financial statements).
5. A. Is a general revaluation (either upward or downward) of assets permitted? (D40)	Yes. C. com. art. 12		✓		5A. See paragraph 90 of text.
B. If so, define the basis.					5B. Current value (*valeur actuelle*).
6. Are nonmonetary transactions that culminate an earnings process accounted for on the basis of the fair market value of the assets involved when that value is determined within reasonable limits? (N35)	Yes. PCG p. 98, for an asset received in exchange for another asset	✓			
7. Is revenue recognized when it is earned and its realization is reasonably assured (rather than when money is received)? (Statement of Financial Accounting Concepts No. 5)	Yes. C. com. art. 9	✓			

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
8. Are costs recorded when incurred rather than when money is paid? (Statement of Financial Accounting Concepts No. 5)	Yes. C. com. art. 9	✓			
9. A. Are consolidated financial statements required when one company has control over another company? (C51)	Yes. Comp. Law Art. L357-1 for listed companies; other companies are required as of 1990	✓			9A. To date, few consolidated financial statements have been prepared for unlisted companies. See paragraphs 92 through 94 of text.
B. Is control usually indicated by ownership of over 50 percent of the outstanding voting shares? If not, how is control indicated?	Yes. Comp. Law Art. L357-4	✓			9B. Exclusive control is indicated by— • More than 50% voting rights. • Less than 50% voting rights but full power on the board of directors.
10. A. Are there instances when an entity would not be consolidated even though control is present? (C51)	Yes. Comp. Law Art. L357-4	✓			
B. If so, list them.					10B. An entity would not be consolidated in the following circumstances: • Subsidiary is not material to the consolidated statements. • Subsidiary is held only temporarily. • The costs to obtain information are excessive or the infor-

					mation cannot be obtained timely. • Control of the subsidiary is threatened.
11. If consolidation is not otherwise appropriate, is the equity method used for unconsolidated subsidiaries, corporate joint ventures, and other investees, if the investments give the investor the ability to exercise significant influence over the investees' operating and financial policies? (I82)	Yes. Comp. Law Art. L357-3	✓			11. Equity method used except for joint ventures, which utilize proportional consolidation.
12. Are there two methods of accounting for business combinations—the pooling-of-interests method and the purchase method? (B50)	No			✓	12. The pooling-of-interest method is not recognized.
13. Is the method used to account for a business combination disclosed? (B50)	No			✓	
14. A. Do criteria exist for treatment of business combinations as a pooling of interests? (B50)	No			✓	14A. This method is not recognized.
B. If so, list the criteria.					
15. A. Is goodwill arising from a business combination accounted for as an asset? (I60)	Yes	✓			
B. If so, is it amortized as a charge to income over the period estimated to be benefited?	Yes		✓		
16. Are the following disclosures made for related-party transactions: (R36)					

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
a. The nature of the relationship?	16*a–d.* Yes. Art. 101–105 of the July 1966 law, as amended for the SA and Art. 50 for the SARL	✓			16*a–d.* Art. 101-105 and Art. 50 refer only to transactions between companies with common directors or management. Other related-party transactions of significance should be disclosed in notes to financial statements. See paragraph 100 of text.
b. A description of the transactions for the periods presented?		✓			
c. The amounts of the transactions for the periods presented?		✓			
d. The amounts due to or from related parties at the balance-sheet		✓			
17. Is an estimated loss from a loss contingency accrued only if it is probable that an asset has been impaired or a liability incurred and the amount of loss can be reasonably estimated? (C59)	Yes. C. com. art. 14	✓			
18. If a loss contingency is not accrued because both conditions for accrual listed in question 17 are not met, is disclosure of the contingency required when there is at least a reasonable possibility that a loss may have been incurred? (C59)	No	✓			18. Although not specifically required, it is done in practice as an application of general principles.
19. Are guarantees of the indebtedness of others or other loss contingencies disclosed in financial statements even though the possibility of loss may be remote? (In the United States, guarantees are usually disclosed as loss contin-	Yes. C. com. art. D 24a	✓			

gencies even if the possibility of loss is remote.) (C59)				
20. Are the following items disclosed in a public enterprise's financial statements for each industry segment: (S20)				20*a–f*. If the information regarding sales is considered "strategic" by the company, it can prevent the disclosure of this kind of information. In that case, it is possible just to mention in the notes that the disclosure is incomplete.
a. Sales to outsiders and inter-segment sales?	No		✓	
b. Operating profit or loss?	No		✓	
c. Identifiable assets and related depreciation, depletion, and amortization expense?	No		✓	
d. Capital expenditures?	No		✓	
e. Equity in net income and net assets of unconsolidated subsidiaries and other investees?	No		✓	
f. Effect of a change in accounting principle?	No		✓	
21. A. Are there any requirements or recommendations to disclose the effects of inflation? (C28)	No		✓	21A. See paragraphs 102 through 106 of text.
B. If so, list the disclosures required.				
22. Are assets segregated into current and noncurrent classifications with a total for current assets presented? (B05)	No. C. com. art. D 24-7	✓		
23. A. Are noncurrent assets those not expected to be realized within one year or the current operating cycle? (B05)	Yes. PCG II-80	✓		
B. If not, how are noncurrent assets defined?				

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
24. A. Is an allowance established for uncollectible receivables? (C59)	Yes. C. com. art. 14	✓			
B. If so, what is the basis (e.g., percentage of sales, aging of receivables, etc.) for calculating the allowance?					24B. Estimated net realizable value.
25. Are receivables and payables, not arising in the normal course of business or subject to normal trade terms, recorded at an amount that takes imputed interest into account? (I69)	No			✓	
26. A. Is inventory stated at the lower of cost or market (or net realizable value)? (I78)	Yes. C. com. art. D 8	✓			
B. If not, how is inventory stated?					
C. Is the basis disclosed?	Yes. C. com. art. D 8	✓			
27. Does cost for inventory purposes include:— (I78)					
a. Materials?	27*a–d.* Yes. C. com. art. D 7-2	✓			
b. Direct labor?		✓			
c. Factory overhead?		✓			
d. If the answer to *c.* is yes, is an allocable share of all factory overhead included?		✓			
28. A. Are the following cost methods permitted for reporting purposes: (I78)					

a. First-in, first-out (FIFO)?	Yes. C. com. art. 12	✓		
b. Last-in, first-out (LIFO)?	No		✓	28*b.* Permitted in consolidated financial statements or for tax purposes. Comp. Law Art. D 248-8 and C. com. art. 12.
c. Average cost?	Yes. C. com. art. 12	✓		
B. Are the same methods permitted for tax purposes?	Yes	✓		
29. Is the inventory costing method used disclosed? (I78)	Yes. C. com. art. D 24-1	✓		
30. A. Are fixed assets depreciated over their estimated useful lives by systematic charges to income? (D40)	Yes. C. com. art. 12	✓		
B. If so, is an accumulated depreciation account used?	Yes. PCG II-102	✓		
31. Are disclosures made of— (D40)				
a. Depreciation expense for the period?	31*a–d.* Yes. C. com. art. D 24	✓		
b. Balances of major classes of depreciable assets?		✓		
c. The methods used to compute depreciation for the major asset classes?		✓		
d. Accumulated depreciation, either by major class of assets or in total?		✓		
32. A. Do criteria exist for classifying leases as operating leases? (L10)	No		✓	
B. If so, list the criteria and disclosure requirements.				

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
33. A. Do criteria exist for classifying leases as other than operating leases for the lessor and lessee? (L10)	No			✓	
B. If so, list the criteria, type of lease, and disclosure requirements.					
34. Are liabilities segregated into current and noncurrent classifications with a total for current liabilities presented? (B05)	No			✓	
35. A. Are noncurrent liabilities those whose liquidation is not expected to require the use of current assets or the creation of current liabilities? (B05)	Yes. PCG II-80	✓			
B. If not, how are noncurrent liabilities defined?					
36. For notes payable, is disclosure made of— (C32)					
a. Interest rates?	No		✓		
b. Maturities?	Yes. C com. art. D 24-7	✓			
c. Assets pledged as collateral?	Yes. C. com. art. D 24-8	✓			
d. Covenants to reduce debt?	No			✓	
e. Minimum working capital requirements?	No			✓	
f. Dividend restrictions?	No			✓	

37. A. For long-term construction-type contracts, are the percentage-of-completion and completed contract methods used? (Co4)	Yes. C. com. art. 15 and PCG p. 224	✓		37A,B. Criteria same as those in U.S. pronouncements ARB 45 and FASB Statement 56. However, if the criteria are met, a company can choose between the two methods.
B. If so, what are the criteria for determining the method to be used?				
38. A. Are research costs charged to expense when incurred? (R50)	Yes. PCG p. 119	✓		38A,B. See paragraph 125 of text.
B. Are such costs disclosed?	Yes. C. com. art. D 19	✓		
39. A. Are development costs charged to expense when incurred? (R50)	Yes. PCG p. 119	✓		39A,B. See paragraph 125 of text.
B. Are such costs disclosed?	Yes. C. com. art. D 19	✓		
40. A. In the United States, events and transactions are presented in the income statement as extraordinary items when they are unusual in nature and are of the type that would not reasonably be expected to recur in the foreseeable future. Do similar criteria for identifying extraordinary items exist in France? (I17)	No		✓	
B. If not, what are the criteria?				40B. See paragraphs 126 and 127 of text.
41. Are material events or transactions that are unusual in nature or expected to occur infrequently,	Yes. PCG II-71	✓		

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
but not both (and thus do not meet the criteria for classification as extraordinary), shown as a separate component of income or expense? (I22)					
42. A. Are disclosures required for—					
a. Extraordinary items? (I17)	42A, *a–c.* Yes. Application of C. com. art. D 24-3	✓			
b. Material events or transactions not classified as extraordinary items? (I22)		✓			
c. Disposal of a segment of a business? (I13)		✓			
B. Indicate the financial statement presentation of these items.					42B. See paragraphs 126 and 127 of text.
43. A. Are pension costs provided for covered employees over the term of employment? (P16)	No. Allowed but no obligation exists (C. com. art. 9)		✓		43A,B. See paragraph 129 of text.
B. If so, do they include charges for costs assigned under the actuarial method used in years prior to the plan's inception?	Yes. OECCA No. 16, Accounting for Pension Plans		✓		
44. A. Are specific disclosures required relating to pension plans? (P16)	Yes. C. com. art. 9 and D 24-16	✓			44A,B. See paragraph 129 of text.
B. If so, list them.					
45. A. When accounting income and taxable income differ, are deferred income taxes	See comments	✓ Consol. fin. stmts.		✓ Annual fin. stmts.	45A. See paragraphs 130 and 131 of text.

recorded for temporary differences (as opposed to permanent differences)? (I25)				
B. If so, are deferred taxes provided for all timing differences (as opposed to only those meeting certain criteria)?	Yes, for consolidated fin. stmts. Comp Law Art D 248-11	✓		
46. A. Are deferred taxes determined on the basis of current tax rates? (I25)	Yes. OECCA Reg. no. 20		✓	
B. If not, on what basis?				
47. A. Is specific information related to income taxes required to be disclosed? (I25)	Yes. Annual accounts C. com. art. D 24-24, consolidated accounts Comp Law Art D 248-12	✓		
B. If so, list the requirements.				47B. See paragraph 130 of text.
48. A. Are operating losses reported on the income tax return allowed to be carried back to earlier periods? (I25)	Yes, but under certain conditions only	✓		48A,B. See paragraph 133 of text.
B. If so, are the tax effects of a loss carryback included in the income in the period?	Yes. CNC (avis No. 26)	✓		
49. A. Are operating losses reported on the income tax return allowed to be carried forward? (I25)	Yes. Fiscal Code art. 290-1	✓		49A,B. See paragraph 132 of text.
B. If so, are the tax effects of a loss carryforward included in the income in the period realized?	Yes. C. com. art. D 24-24	✓		
50. Are financial statements of a foreign entity prepared for	Yes	✓		50. See paragraph 134 of text.

U.S. Generally Accepted Accounting Principles	Required by Government or Professional Pronouncements	Predominant Practice	Minority Practice	Not Done	Comments
consolidated purposes measured in the currency of the primary economic environment in which the entity operates? (F60)					
51. Are all elements of financial statements translated at current exchange rates? (F60)	Yes	✓			
52. A. Are translation adjustments reported separately? (F60)	Yes	✓			
B. Are they accumulated in a separate component of stockholders' equity until ultimately realized?	Yes	✓			
C. Is there an analysis of the changes during the period in the component of stockholders' equity relating to translation adjustments?	Yes		✓		
53. A. Are gains and losses resulting from transactions denominated in a currency other than that of the environment in which the entity operates included in determining net income for the period in which the exchange rate changes? (F60)	Yes	✓			53A. Losses are recorded. Gains are not anticipated, except in consolidated financial statements (Comp. Law Art. D 248-8g), for which the option is available.
B. Is the aggregate transaction gain or loss included in determining net income for the period disclosed in the financial statements or notes?	Yes	✓			

54. Are gains or losses on foreign currency transactions that are intended to hedge a foreign currency commitment deferred and included in the related transactions? (F60)	Yes. PCG p. 105	✓	
55. What information is disclosed about foreign currency restrictions? (F60)	None specifically required	✓	
56. Are significant events arising subsequent to the balance-sheet date reflected in the financial statements or notes thereto? (C59)	Yes. C. com. art. 14, al. 3 OECCA no. 12, post balance sheet events	✓	
57. Please list any standards for France for which there are no corresponding U.S. standards.			57. None.

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