

The Court of Auditors' role as auditor of the Federal State of Hesse's consolidated accounts and as advisor in the process of developing public-sector accounting standards

- Lessons learnt and outlook -

Presentation

20 May 2011

by

Prof. Manfred Eibelshäuser

President of the Court of Audit of Hesse

From cash-based to accrual accounting

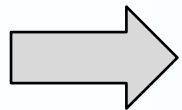
- Hesse's path to commercial financial reporting -

14/7/1998	Resolution by the government of Hesse to introduce commercial accounting
2/6/1999	Resolution by the government of Hesse: implementation throughout Hesse by 2008
since 2003	Court of Auditors: audit procedures for selected opening balance sheets and annual accounts issued by individual accounting areas of the State of Hesse Group, with assistance from outside auditors
since 2007	Court of Auditors: pilot audit procedures for the opening balance sheets and annual accounts of all Hesse's higher state authorities
20/11/2009	Presentation of the consolidated opening balance sheet of the Federal State of Hesse, audited by the Court of Auditors of Hesse
2/11/2010	Presentation of the first consolidated account of the Federal State of Hesse, audited by the Court of Auditors of Hesse

The Court of Auditors as advisor in the process of developing public-sector accounting standards

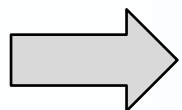
- legal bases -

- **Section 33 a HGrG (f.v.)*:** Public-sector accounting according to the principles of proper bookkeeping **in faithful application of HGB**** (additional, optional)



Hesse decided at an early stage to adhere closely to the accounting principles of HGB**


- **Section 1 a (1) HGrG (n.v.)*:** The budget can be managed according to the principles of **public sector double-entry bookkeeping** as established in Section 7a (as of 1 January 2010)



Under Section **7a HGrG* (n.v.)**, the accounting principles of HGB** are mandatory for public entities that decide to pursue commercial bookkeeping.

*German law on public-sector budget principles (f.v. = former version / n.v. = new version). **German Commercial Code





The Court of Auditors as advisor in the process of developing public-sector accounting standards

- legal bases -


Section 71 a LHO*: “Details will be regulated by the Ministry of Finance **with the agreement of the Court of Auditors.**”

For example:

- Double-entry bookkeeping
- Accounting principles and valuation methods
- Presentation of annual accounts and subgroup accounts
- Standard form of accounts

*Hessian state financial regulations





The Court of Auditors as advisor in the process of developing public-sector accounting standards

- guided by the accounting principles of HGB -

- Content and issues specific to the public-sector must be entered in the system of commercial accounting principles
- Exploiting options for **simplification** in HGB* (e.g. asset valuation)
- Further simplification only if necessary
- Limits to simplification: when it would breach the principles of proper bookkeeping.

*German Code of Commercial Law



The Court of Auditors as auditor of the consolidated accounts

- legal bases -

- **Section 88 (1) LHO***: “The financial management of the entire state budget, including separate property funds, is subject to the audit powers of the Court of Auditors, pursuant to the following provisions.”
- **Section 1 (1) RHG****: “... It (the Court of Auditors) approves the opening balance sheets and the annual accounts of the higher state authorities.”
- **Section 94 (2) LHO***: “The Court of Auditors can call in experts.”

* Hessian state financial regulations

** State Code on the Court of Auditors



The Court of Auditors as auditor of the consolidated accounts

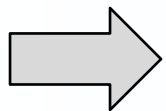
- Auditing by external accountants or by the Court's own personnel? -

By the Court's own personnel

- Initially, too few of the Court's staff members had experience in auditing commercial annual statements.
- It would have been necessary for the Court to establish two additional departments.

By external accountants

- Experience in auditing annual accounts
- Auditor's report delivered
- Technical coordination by a steering committee at the Court of Auditors
- Auditing annual accounts is a seasonal business, taking just 3-4 months per year.



Audit by external accountants is more efficient



- Reactions to the disclosure of Hesse's opening balance sheet -

Bold Honesty

(...) By switching the state's budget management from cash-based to accrual accounting, Hesse is setting a good example for transparency. (...) Exactly this kind of discussion is overdue. It could well be encouraged by this new, more honest way of accounting.

FAZ. NET 11/21/2009

We welcome the fact that, in disclosing the balance sheet, the government has taken a big step towards greater honesty.

Frank Kaufmann (Grüne)

Hesse undertakes honest accounting

It's a pity this kind of data system isn't available at the federal level: this is an honest account.

Frankfurter Rundschau 11/21/2009

Hesse's Balance Sheet:

The state is now calculating like a private Enterprise, and it's highlighted a tremendous need for action.

Wiesbadener Kurier 11/21/2009

This is nothing less than an oath of disclosure.

Norbert Schmitt (SPD)



- Outlook -

- One flaw (still) remains, which caused a qualification to the auditor's report, and which still needs to be corrected (the valuation of art objects).
- Cash-based accounting will become dispensable in Hesse, once the amendment to the State Budget Code (LHO) is adopted.
- Information gained through the new public-sector accounting should be used more effectively, for both **global budget steering** and the **fine-tuning of expenditure**:
 - **Budget planning** must reflect the findings in the annual accounts.
 - Balance sheet data (and data from-profit and-loss reporting) must be used for **cost accounting** and **controlling**.
 - Opportunities must be sought for **decentralized management** and decentralized budgets.

