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From the "Accounting Audit" to the "Accounting Exam": the quarrel of the old and the modern

The new accounting proceeding, introduced recently, and commented by the Administration even more recently, has not raised many discussions so far.

Yet, this new procedure, which relocates the place of the accounting audit in the premises of the Administration, compromises the "sacred" territory of the oral and adversarial debate.

That the tax creates a pecuniary debt for individuals, as well as for companies, and thus, affects the constitutional right of private property, is an evident truth.[1]

Or, since the French tax system is essentially based on tax returns that taxpayers file spontaneously, important means to verify its veracity are recognized to the Administration by the State.

For the businesses, these tax returns are based on social accounting, which serves, on one hand, to establish the principal tax base (CGI ann. III, art 38 quater) and, on the other hand, as a tool to verify the sincerity of the tax returns (LPE, art L. 10).

To this matter, in order to make a critical comparison between the accountancy and the tax return, the Administration has in its disposal the procedure of "accounting audit", defined as the operation by which

[1] Constitutional Council 2011, nmb.33

the tax administration "controls on the spot, the sincerity of the statements subscribed [by the company] by comparing them with the ledger entries or other supporting documents brought to its knowledge and if needed, can call into question its accuracy ".[2]

As an outcome of the accounting audit, an additional tax may be established, a drawdown that will affect the company's assets, once again.

Therefore, tax cohabitation exists between the value-creating enterprise, most often with private capital, and the State.

The taxpayers' rights of defense are at stake, and a solution must be found to balance the rapports between the powerful Administration and the taxpayers.

This is why the procedure of accounting audit, which is an external procedure for the Administration, but binding and intrusive for the company, is strictly framed by the law in the articles L. 47 and sequels of the LPF, and this for a long time now, following the serious incidents between the public authorities and the world of artisans and tradesmen in 1955.

Hence, the law (LPF, Articles L. 13 and L. 47 and seq.) and the regulation provide for (i) the prior sending of an accounting audit notice to the firm, mentioning the years audited and the possibility for the company to have recourse to the counsel of its choice, (ii) the performance of the control operations “on-the-spot” (LPE, art L. 13), and (iii) in principle the prohibition to take files out of the company premises, in order to respect the obligation of an oral and adversarial debate on the spot.
Finally, the duration of intervention on the spot is limited.

If a proposal of rectification is then sent, it must be duly motivated.

The accounting auditing operations are also framed by the judge.

The Council of State, in a judgment of 21st May 1976[3] specified the four necessary conditions in order to derogate from the principle according to which the auditor cannot take files out of the company premises.

Moreover, the right for the taxpayer, eventually assisted by an advisor, to meet and discuss with the auditor at the headquarters of his company is an essential condition.

This is a procedure which “allows the Administration to be aware of the concrete conditions of the enterprise operations and forces the taxpayer to admit this effort to apprehend the reality through dialogue"[4] or, according to others, to encourage the Administration to ensure the irreplaceable human contact "allowing the auditor to explain himself in the intimacy of a head-to-head".[5]

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[2] Council of State 6 October 2000, nmb.208765
[3] Council of State 21st Mai 1976, nmb.94052
[4] Ibid
[5] Ibid

This “on-the-spot” debate is based on the idea that only the possibility of an evolutionary and constructive dialogue in the company's premises is likely to allow the taxpayer to usefully present its first observations, or, depending on the case, to learn from the Administration the innumerable subtleties of the French tax law.

Furthermore, it allows the taxpayer to apprehend in serene conditions the confrontation with the auditing department.

For a long time now, this double legislative and jurisdictional structure allows a moderate and effective fiscal control and the establishment of an entrepreneurial management which is adapted to the requirements of the tax audit.

So, a balance admitted and recognized by all the actors of the tax audit. But, under the impetus of the Secretary of State for Budget and Public Accounts at the time, initiated by a concern for "modernity", the 2016-1918 law of 29th December 2016 about amended finance for 2016, allowed to the agents of the Administration, when taxpayers are compelled to keep and submit accounting documents by means of computerized systems, to examine the accounts without being present on-the-spot (LPF, Articles L. 13 and L. 47 AA new).

It emerges, from the summary of the reasons of the mentioned law, that this new legislation aims to modernize the procedures of tax audit in business accounting by creating a new world of remote control called "accounting exam".

The Government has outlined the scope of this new procedure, stating that it "will be particularly appropriate for companies presenting low risk or low complexity issues, thus, not requiring an on-the-spot control.

The administration can in this way, be able to concretize the biggest operations on the taxpayers who justify it ".

Normally, an accounting notice, will specify the period of the review and indicate the ability of the taxpayer to be assisted by the counsel of their choice.
The taxpayer will later be informed of the results of the accounting review, within 6 months at the latest.

Actually, the on-the-spot control, which as has been pointed, is fundamentally protective and really important for companies in the management of tax auditing, can be dismissed at the discretion of the tax authorities.
In her report on behalf of the Finance Committee of the National Assembly, Valérie Rabaul, general rapporteur, reminds that the accounting audit is surrounded by many guarantees for the taxpayer under Article L.47 of the LPF.

She quotes a case law of the Council of State which has held in particular, that this procedure does not exceed "the needs related to the economic well-being of the country"[6], does not violate

[6] Council of State 18 March 1994, nmb.68799

"the right of the taxpayer for respect to his private life"[7], nor the "freedom of information and expression"[8] or the "right to a fair trial"[9] provided in Articles 6, 8 and 10 of the Convention for the Protection of Human Rights and Fundamental Freedoms.

Referring to the important decision of the Council of State in 1976[10], the report also points out the principle, pursuant to which, the accounting audit must be conducted on the spot in order to provide the taxpayer with "opportunities for an oral and adversarial debate" and to allow it to meet the auditor in order to discuss its point of view.

Further, the report also states that, in accordance with the general principle issued by the Council of State, and even if the text does not provide it, the Administration, in case of an accounting exam, is obliged to offer to the taxpayer, the possibility of an oral and adversarial debate.

In addition, the Council of State ensures the respect of a minimum investigation[11] at the headquarters of the company, since it is a fundamental guarantee to allow the taxpayer to profit from the oral or adversarial debate to which he is entitled to, in case of an accounting audit.

This protection is affirmed even against the opinion of the eminent Commissioner of the Government, Mr. Jacques Arrighi de Casanova, who, in his conclusions under a decision of the Council of State on December 10, 1999,[12] proposed to separate the place where the accounting audit is exercised from the proof of the existence of an oral and adversarial debate, by considering that a dialogue between the taxpayer and the auditor on the spot was, in his opinion, irrelevant and that "the tax judge would demonstrate excessive formalism by canceling an imposition, on the sole ground that the auditor did not carry out a minimum of investigation at the headquarters of the company"[13].

By not retaining the position of its Government Commissioner, the Council of State demonstrates the importance that it attaches to the respect of the on-the-spot control, a guarantee that the debate between the audited taxpayer and the Administration is oral and adversarial.

It goes even more far and poses a presumption of an oral and adversarial debate, when the accounting audit has taken place on the premises of the audited taxpayer.[14]

The pre-assessment of this new "accounting exam" indicated that the Government's objective was to increase the number of controls, by benefiting from the time saved by this new procedure.

The general reporter, Mrs. Valérie Rabault précised that this period "aims to allow the Administration to effectuate more controls.

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[7] Council of State 15 December 1993, nmb.84181
[8] Council of State 18 March 1994, nmb.68799
[9] Council of State 5 July 1995, nmb.153942
[10] Council of State 21st Mai 1976, nmb. 94056
[11] Council of State 2nd July 1986, nmb. 50872
[12] Council of State 10 December 1999, nmb. 201067
[13] Ibid, Concl. Of Mr. Arrighi de Casanova
[14] Council of State 17 February 1997, nmb. 165573

Rather than the on-the-spot audit, in which dialogue is certainly possible, the proposed provisions offer the possibility of controls by the Administration from its own offices, [...] without further displacement of the staff of the General Directorate of public finances."

The main purpose of the new scheme is to increase the profits and, therefore, it is comprehensive to question about the impact that this objective will going to have on the quality of the audits.

In the pre-evaluation is further specified that "these simplifications should not be aimed at reducing the taxpayers' guarantees but at stopping the delaying tactics", without specifying whether the "debate on-the-spot" was considered as "dilatory".

The number of the additional controls envisaged which should justify this measure, has not been quantified by the Government either.

It is because nothing seems to change in appearance, that particular vigilance is required.

The accounting exam is effectuated without the presence of the auditor on the spot, without the head-to-head meeting between the economic sphere of the company and the Administration, in favorable conditions for the defense of the taxpayer.

Actually, many elements are now afforded by the taxpayer, and no longer by the Administration. This is the contribution of "modernity", linked to the existence of computerized accounting.

The Constitutional Council does not seem to identify a problem, as, in its decision about the financial law for 2016[15], it has declared conform to the Constitution the procedure of accounting exam, stating that the new legal dispositions "do not confer [to the Administration] an enforcement power" and that " do not deprive the taxpayer of the guarantees provided in the Tax Procedures Book in case the Administration exercises its right of control" ; as a result, they "do not violate the rights of defense or any other constitutional requirement".

The parliamentarians who seized the Constitutional Council in application of Article 61 of the Constitution, nevertheless, argued that this measure affects the respect of the rights of the defense, by not allowing an oral and adversarial debate.

The administrative doctrine confirms both the parliamentary debates and the remarks of the Central Audit Office and states that the "audit" is the operation which ensures the sincerity of a tax return by comparing it with external elements, and that it may be for a company: either an accounting audit, which we shall call "classical", or an accounting exam, which must now be described as "modern".

In the latter case, the service will perform, from the office, the examination of the accounts without visiting the company, even if the taxpayer expressly requests it. The latter may still, fortunately, ask to be heard by the audit department to discuss about the case, but, this interview takes place on the premises of the Administration.

[15] Constit. Counc. 29 December 2016, nmb.2016-743 DC

Once the accounting examination terminated, the administrative doctrine specifies that a point must be made with the taxpayer by phone, prior to sending the proposal for rectification. If the taxpayer asks to be received, the appointment will take place on the premises of the Administration.

The procedures to “audit” the companies’ are now well established.

The accounting audit by the service, and the verification of legal and accounting documents, has as a corollary the protection of the company through an oral and adversarial debate, itself guaranteed by the presence of the auditor on the spot.

The accounting exam by the service, and the verification of legal and accounting documents, has as a corollary the protection of the company through an oral and adversarial debate, itself substantially guaranteed by the absolute prohibition of the auditor to be present on the spot...

From the practitioners' point of view, what about the rights of defense for the taxpayer?

What about the understanding of the economic structure investigated by the service?

What about the protection of the entrepreneur?

Finally, what will the qualitative and quantitative use of this new procedure by the Administration be?

The tax audit is based, since a very long time, on dialogue and a consensual approach between the Administration and the audited taxpayer.

For the latter, this is an external audit to determine whether the tax law has been correctly applied.

A constructive and non-conflictual relationship should be established, allowing the Administration to become aware of the way the activity is exercised.

The on-the-spot control is thus, a prerequisite, for oral and adversarial debate.

In absence of such an on-the-spot presence, the need for assistance by advisers experienced in the tax procedure field is considerably strengthened.
It will be up to these councils, to maintain the oral and adversarial debate even outside the premises of the company, in order to compensate, as much as possible it may be, the immense deficit of protection created by this "modernity of everything digital".

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