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Faculty of Economics Commercial and Management Sciences

Sectoral Accounting I

Course Handbook

For First-Year Master's Students

Specialization: Accounting and Auditing

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Introduction to sectoral accounting :

Sectoral accounting is concerned with accounting techniques and treatment in one of the sectors of importance in the local and international economy, as it is characterized by some characteristics that distinguish it from other sectors, which are represented in the nature of the product or service provided, or the period taken to achieve revenue, as well as the elements that make up this product or service

Because of these peculiarities and transactions that characterize these sectors, it has led to the existence of some special accounting treatments that respond to these peculiarities and transactions, which has made local and international professional accounting bodies pay attention to sectoral accounting.The International Accounting Standards Board (IASB) has allocated special standards, such as: the International Reporting Standard (IFRS).4 "Insurance contracts", which was replaced by the IFRS17 standard starting from 01/01/2023, the IFRS 15 standard "Revenue from customer contracts", IFRS 4 "Insurance Contracts."

Similar to the financial accounting system issued through Law No.07-11 of November 25, 2007, which includes a set of recognized accounting rules and principles that make them applicable in several areas of economic activities without the fundamental foundations differing depending on the activity that is the subject of the accounting, the difference may be stipulated in the method of treatment.Accounting without the foundations, as each sector has its own accounting called sectoral accounting, such as: the insurance sector, the agricultural sector, Banking sector, tourism sector, construction and public works sector,...ETCS

Sector accounting aims to achieve a set of objectives that we summarize as follows :

Providing sector-specific information to achieve administrative purposes for custodians

Providing financial information that confirms the correct application of the sector's accounting rules

Providing financial information about the various types of products and services provided by the sector

Providing financial and accounting data to prepare financial reports for the sector

Providing financial information regarding the sector's accounting policies

Providing the necessary information for tax administration

In this context, the publication was divided into two main chapters through which we address the insurance sector and the construction and public works sector according to the ministerial program scheduled for first-year Master of Accounting and Auditing students

Chapter 01: General Framework of Accounting Operations in Insurance Companies

Section One: General Framework of Insurance and/or Reinsurance and Insurance Companies

First: Insurance

1. **Concept of Insurance**

   There are multiple definitions of an insurance contract from various perspectives.

   According to the IFRS 17 international financial reporting standard, an insurance contract is defined as:

   "A contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event adversely affects the policyholder."

From an economic perspective, insurance is defined as a process through which the burden of losses resulting from the occurrence of a risk is transferred to an insurance company in return for the policyholder paying a premium or multiple premiums.

The insurance process is executed through a "policy document" that outlines the obligations of both contracting parties. The contract consists of two parties: the insurer (the insurance company) and the insured (the person seeking coverage). The insurer (the first party) commits to paying compensation to the insured (the second party), or to a third-party beneficiary, in the form of a lump sum or periodic payments known as insurance premiums.

Legally, the Algerian legislator defines the insurance contract in Article 2 of Ordinance No. 95-07 dated January 25, 1995, related to insurance, as follows:

"According to Article 619 of the Civil Code, an insurance contract is a contract under which the insurer commits to providing the insured or a third-party beneficiary, in whose favor the insurance was stipulated, with a sum of money, income, or any other financial performance in the event of the occurrence of the risk specified in the contract, in exchange for premiums or any other financial payments made by the insured to the insurer."

The insurance contract must be made in writing and must, in addition to being signed by both contracting parties, include the following mandatory data:

- The names and addresses of both contracting parties;
- The insured object or person;
- The nature of the covered risks;
- The date of subscription;
- The effective date and duration of the contract;
- The amount of the guarantee;
- The amount of the insurance premium or contribution.

2. Elements of the Insurance Contract:

Based on the above, the main elements of a comprehensive insurance operation are:

- **Insurance Policy**: Issued by the insurance company as the official contract of the insurance operation. It includes the various terms of the insurance process, such as the insured amount, the value and schedule of premiums to be paid by the insured, the agreed-upon insurance period, the beneficiary of the insurance, and the amount of compensation.
- **Insurer (First Party)**: The specialized insurance company responsible for collecting the premiums and paying the agreed-upon compensation once the covered risk occurs.
- **Insured (Second Party)**: The party seeking insurance who is required to pay the premiums on the specified dates.
- **Beneficiary**: The third party who benefits from the insurance coverage. This may be the insured themselves or a third party, such as in certain life insurance cases.
- **Insurance Premium**: The amount that the insured (policyholder) must pay to the insurer (insurance company), as scheduled in the policy, in exchange for compensation to themselves or the beneficiary.

- **Insurance Amount**: The compensation or financial obligation the insurer assumes toward the insured in the event of the covered risk.
- **Insured Risk**: The event or hazard covered by the policy. It represents a potential danger to the insured and is a fundamental element in the insurance process. It must be clearly defined in the policy and meet the following conditions:
    - The risk must be uncertain and not inevitable;
    - It must be beyond the insured's control;
    - It must be legal and not contrary to public order or morals.

3. Characteristics of the Insurance Contract:

An insurance contract has several defining characteristics, including:

- **Consensual Contract**: It only becomes valid through the mutual consent of both parties.
- **Bilateral Contract**: Both parties have obligations — the insured must pay premiums, while the insurer must provide compensation.
- **Commutative Contract**: Each party receives something in return - the insured pays a premium in exchange for coverage, and the insurer receives premiums for providing that protection.
- **Aleatory Contract**: Because the occurrence of the risk is uncertain.

- **Adhesion Contract**: The insurer, being the stronger party, imposes the terms, and the insured must accept them without negotiation.

4. Insurance Intermediaries:

Under Ordinance No. 95-07, as amended by Law No. 06-04 (Article 53), insurance intermediaries include the general agent and the insurance broker.

- **General Agent**: A natural person who represents one or more insurance companies under a designation contract. They offer their technical expertise and personal experience to both the public and the companies they represent.
- **Insurance Broker**: A natural or legal person who acts on their own behalf to mediate between potential policyholders and insurance companies. The broker acts as the agent of the insured and is responsible toward them.

5. Types of Insurance:

There are various classifications of insurance depending on the type of risk and socioeconomic development:

5.1. Based on Legal Structure:

- **Mutual Insurance**: Formed when individuals facing similar risks contribute to a shared fund that compensates any member who suffers a loss. Profits may be distributed, and additional contributions may be required if the fund is insufficient.

- **Commercial Insurance**: Carried out by companies whose main goal is profit, though competitive pressure limits excessive premium pricing.
- **Social Insurance**: Developed to protect workers against old age, disability, illness, and work-related accidents. Costs are shared between employers and employees, with public institutions often managing the coverage to reduce costs.

5.2. Based on Contractual Freedom:

- **Voluntary Insurance**: Includes policies where the individual chooses to insure or not, such as life insurance, theft insurance, and fire insurance.
- **Mandatory Insurance**: Imposed by law for social or public interest reasons, such as workers' compensation or civil liability for vehicle owners. These are not subject to individual discretion.

5.3. Based on the Basis of Payment:

According to Ordinance No. 95-07, amended by Law No. 06-04 of February 20, 2006, insurance types include:

- **Damage Insurance**: Covers financial loss to the insured's assets. It compensates for damage to the financial estate due to covered risks. Categories include:
    - *Property Insurance*: The insured covers their property in exchange for premiums and is compensated for damage under the policy terms. Examples include:

    - Theft insurance
    - Fire and associated perils
    - Livestock mortality insurance
    - Cargo insurance
    - Surety insurance
  - *Liability Insurance*: Covers financial consequences of the insured's civil liability for harm caused to third parties. Examples include:
    - Liability insurance for companies covering bodily, material, and moral damages
    - Motor vehicle, ship, and aircraft liability insurance
    - Workplace accident and occupational disease insurance
- **Personal Insurance**: As defined in Article 10 of Law No. 06-04 (modifying Article 60 of Ordinance No. 95-07), it is a contingency contract between the policyholder and the insurer, whereby the insurer pays a sum (lump sum or annuity) upon the occurrence of a defined event or the expiry of the contract. According to Article 63 of Ordinance No. 95-07, the risks covered include:
  - ✓ Risks related to human life expectancy
  - ✓ Accidental death
  - ✓ Partial or total disability

- ✓ Temporary incapacity to work
- ✓ Reimbursement of medical, pharmaceutical, and surgical expenses

Personal insurance policies benefit the insured or a named beneficiary upon the occurrence of the insured event, and the beneficiary acquires a direct legal right to the compensation.

5-4 Other Forms of Insurance:

Joint Insurance: Joint insurance is the contribution of multiple insurers to cover the same risk under a single insurance contract. The management and execution of the insurance contract are entrusted to a lead insurer, who is legally authorized by the other participating insurers. These insurers are interested in participating in the insurance to distribute large risks (such as aircraft, large ships, and large marine cargo risks, etc.) among themselves, allowing them to handle large or risky insurance operations and to fulfill their obligations, thus achieving the purpose of insurance for them.

There are two types of joint insurance:

- **Voluntary Joint Insurance:** In this type, the terms, pricing, and management of the contract are entrusted to the lead insurer by the other participating insurers. The lead insurer sets the terms of the insurance after negotiating with the policyholder, and then distributes the insurance to the other insurers based on their agreed share. In return, the lead insurer receives a commission known as the "lead insurer's commission."

- **Joint Insurance Managed by Groups:** The conditions, procedures, and management methods in this type of joint insurance are defined within a group of participating insurers, with the group being responsible for managing the technique rather than the lead insurer.

Second: Reinsurance

The process of insurance is based on the idea of risk distribution, so an insurance company may engage in reinsurance for part of its operations with a reinsurance company.

1. **Definition of Reinsurance Process:** Reinsurance is the process in which the reinsurance company (referred to as the ceding company or the reinsurer) assumes all or part of the insurance risk previously borne by another company, referred to as the original company (or the cedent or ceding company), in exchange for a premium paid by the original company. It is also important to note that the legal rights of the policyholder (claims) are not affected by reinsurance, and the insurer that issued the original insurance contract remains responsible for all benefits (insurance premiums) arising from the contract.
2. **Elements of Reinsurance:** The key elements in a reinsurance contract are as follows:

- ✓ **Direct Insurer:** The original insurer that cedes part or all of the risk to a reinsurer.
- ✓ **Reinsurer:** The entity that accepts reinsurance from the original company, which could be a regular insurance company or one specialized in reinsurance.
- ✓ **Reinsured Amount:** This is the amount received by the original insurer from the reinsurer to cover the expenses the original company incurred when issuing the insurance contract with the client.

Reinsurance can be divided into three types:

3-1 **Voluntary Reinsurance:** This type of reinsurance is based on the voluntary choice of the ceding insurer, without a prior agreement between the insurer and the reinsurer. The ceding insurer presents to the reinsurer the operations it wishes to reinsure, and the reinsurer has full discretion to accept, reduce, or reject the reinsurance.

3-2 **Mandatory Reinsurance:** This type of reinsurance is required by law under the insurance sector's supervision and regulation, where laws mandate that insurance companies must cede a portion of their operations to other local insurance companies to reduce the transfer of large sums of money abroad.

3-3 **Treaty Reinsurance:** This type of reinsurance is based on a prior agreement between the insurer and the reinsurer. It includes:

- ✓ **Reinsurance of a specific share of risk:** The direct insurer cedes a fixed percentage of each operation within the scope of the agreement to the reinsurer.
- ✓ **Excess of loss reinsurance:** The direct insurer reinsures the excess of risk generally, for all types of risk without prior review, which they do not wish to insure.
- ✓ **Surplus loss reinsurance:** The direct insurer sets an upper limit for the loss they can bear when a covered risk occurs, and the reinsurer will bear any excess over this limit.

Reinsurance can also be classified based on its sources into:

- ✓ **Inward Reinsurance:** This refers to reinsurance operations accepted by the company from other companies.
- ✓ **Outward Reinsurance:** This refers to reinsurance operations ceded by the company to other companies, either mandatorily by law, voluntarily, or by agreement.

Third: Nature of Operations in Insurance Companies

1. **Definition of Insurance Companies:**

   Insurance companies are financial institutions that collect insurance premiums from clients in exchange for providing them with insurance policies that protect against financial losses from specific events. The company then invests its assets in its operations and industries, offering financial resources to other commercial enterprises to conduct or expand their activities.

As defined by Algerian legislation in Article 203 of Order 95-07, amended and supplemented by Article 23 of Law 06-04 on insurance, insurance and reinsurance companies are companies that underwrite and execute insurance and/or reinsurance contracts, as outlined in the applicable legislation.

According to Article 215 of Order 95-07, as amended and supplemented by Article 34 of Law 06-04 on insurance, insurance and reinsurance companies must comply with Algerian commercial law and can take the following forms:

- Joint-stock companies
- Mutual companies

Insurance and/or reinsurance companies can only operate after obtaining approval from the finance minister based on the conditions outlined in Article 218 of Order 95-07, as amended by Article 36 of Law 06-04.

2. **Functions of Insurance Companies:**

- **Pricing Function:** This function determines the premium to be paid by the policyholder for a specific risk the insurance company will cover. A price is set based on the degree and likelihood of the risk, the amount of insurance, and the circumstances of the insured risk.
- **Underwriting Function:** The company accepts insurance applications that are expected to be profitable and rejects those likely to result in losses or are not feasible.

- **Production Function:** In insurance, production refers to sales and activities carried out by insurance companies, and the sale process is the insurance service offered by the company.
- **Claims Settlement Function:** This function involves paying claims to policyholders when the insured event occurs. Specialized personnel in insurance companies study the claims and determine the appropriate compensation.
- **Reinsurance Function:** This refers to transferring part of the risk to other entities capable of handling it.
- **Investment Function:** Since premiums are collected at the start of the insurance process, the insurance company has substantial funds that can be invested.
- **Accounting Function:** The accounting department is responsible for recording financial results, managing general accounting records, monitoring cash receipts and payments, and overseeing the preparation of the company's financial statements.

3. **Technical Operations of Insurance Companies:**

The key activities carried out by insurance companies include:

- Receiving insurance applications and signing contracts through direct contact with clients or through the company's agents and brokers. It also includes receiving operations from other insurance companies in the context of reinsurance operations.

- Collecting insurance premiums as per the signed contracts through various sources and investing these premiums in different investment areas within the limits authorized by the laws regulating insurance companies.
- Estimating provisions related to various insurance operations, which must be held to meet the covered risks, as well as calculating premiums due for various insurance operations.
- Estimating and paying the compensation due for risks faced by policyholders.
- Reinsurance, where the insurance company may transfer risks to other companies if it fears it will not be able to meet the insured risks on its own.

4. **Characteristics of Insurance Activity:**

   Insurance activity is characterized by two main features:

- Reversal of the production cycle: The sale price (premium) is immediately collected, while the service (payment of compensation) occurs later.
- Possible time difference between the occurrence of the damage causing the claim and the actual payment of the claim**.**

From these features, we derive key effects on the accounting system:

- Insurance companies hold large amounts of funds that need to be managed, which reflects the importance of investments alongside assets on the balance sheet and the significance of financial income alongside revenue in the income statement (results and surplus or deficit from asset disposals).

- Insurance companies do not know their true cost price except in the long term, necessitating provisions for claims to be made during the early periods. These provisions are estimates or evaluations to some extent, and an appropriate margin of safety is needed to avoid any possible underestimation of these provisions.
- There is no alignment between the fiscal year for recording premiums and the fiscal year for recording claims, which necessitates the use of a distribution account that represents the provisions for active risks in general insurance and provisions for life insurance.
- An insurance company cannot precisely determine its profit or loss at the end of the financial year. This is primarily due to two reasons: first, insurance contracts often extend beyond the fiscal year in which they were concluded, and second, the financial obligations and burdens associated with insurance contracts cannot be precisely determined until the end of the contract term. Therefore, the profit or loss figure at the end of the financial period is an estimate, reflecting the probabilistic nature of the results in insurance companies.

Chapter Two: Accounting System in Insurance Companies

The accounting system is responsible for providing information to management and other external parties. It is defined as "an integrated system of human and material resources that operates through the organization to gather, classify, process, analyze, and compile data into reports and financial statements" to serve the purposes of different entities and assist them in making timely and appropriate decisions.

1- Insurance Company Accounting According to International Accounting Standards

The insurance sector has its own international accounting standards aimed at improving the accounting policy for insurance contracts. One of these is the IFRS 17, which addresses the accounting for insurance instruments. However, its application faced several challenges in handling various insurance contracts in different ways, leading to difficulties for investors and analysts in determining which insurance contracts were profitable or unprofitable, and analyzing trends related to insurance contract data. This was addressed by the introduction of IFRS 17, which has become a necessary standard due to its positive impact on the financial statements and performance indicators of insurance companies. It also solved comparison issues that arose when applying IFRS 4, as IFRS 4 did not require accounting for different insurance contracts in a consistent manner. On the contrary, insurance contracts were accounted for differently between companies, and sometimes even within the same company.

The IFRS 17 standard specifies principles for the recognition, measurement, presentation, and disclosure of insurance contracts within its scope. It ensures that insurance companies provide relevant information that faithfully represents the contracts. This information is the basis for users of financial statements to assess the impact of insurance contracts on the company's financial position, performance, and cash flows. On May 18, 2017, the International Accounting Standards Board issued IFRS 17 "Insurance Contracts," which applies for periods beginning on or after January 2023, replacing IFRS 4. Its goal is to enhance the relevance and transparency of financial statements in insurance companies by introducing various techniques for measuring and representing insurance contracts in a more accurate and transparent manner.

2- Components of the Accounting System in Insurance Companies

1- Accounting Records and Ledgers Used in Insurance Companies:

The application of the accounting system in insurance companies is based on the operations carried out by the company. The company is divided into several specialized technical departments that handle specific processes related to the insurance business it undertakes. Therefore, the accounting structure of insurance companies can be achieved through maintaining various ledgers and records. Below are the main accounting records and ledgers used in insurance companies.

1-1 Records Used in Insurance Companies

The specialized departments in insurance companies are responsible for issuing insurance policies, making amendments or cancellations, and maintaining records to prove these operations, divided as follows:

- **Technical Department Records**: The technical departments typically maintain the following records:
  - ✓ **Issuance Record**: This record contains all the data related to the insurance policies issued by the department. The premiums due on the issued policies represent the earned revenue for the company. Therefore, this record is particularly important in insurance companies, as it keeps a statistical log of all policy data and acts as an auxiliary journal to track earned revenues.
  - ✓ **Claims Record**: This record contains data about claims reported to the insurance company. When an insured risk occurs, the insured submits a specific form to notify the insurance company of the incident, which is directed to the relevant department for processing and tracking claims.
  - ✓ **Renewal Record**: It is common for insurance companies to renew previously issued contracts approximately two weeks before the end of the insurance period. This renewal is usually automatic, and each department maintains a renewal record in the form of loose cards arranged by chronological order.

- ✓ **Amendment and Cancellation Record**: This record contains data related to cancelled policies, which terminate the insurance contract between the company and the policyholder. Cancellations reduce the company's revenues due to the loss of premiums due on the cancelled policy. Amendments, such as changes in coverage amount, risks covered, or insurance duration, affect the premiums due.
- ✓ **Broker Record**: Insurance companies register sufficient data for each broker handling intermediary services between the company and policyholders, including name, address, registration number, and date. The department sends a statement about the broker's commissions to the accounting department for posting in the general journal on a monthly basis.
- ✓ **Agreement Record**: When an insurance company enters into a reinsurance agreement with another insurance company, either locally or abroad, the transactions are recorded in the agreement register and forwarded to the accounting department for posting in the general journal.

- **Collection Department Records**: The collection departments typically maintain the following records:
  - ✓ **Cash Receipt Record**: Once the relevant department issues receipts for premiums, they are sent to the treasury. When

the policyholder pays the premium, it is recorded in the cash receipt record, which includes details such as policy number, client name, premium amount, and stamp duty. The monthly total of this record is communicated to the accounting department to post the collected premiums in the receipts and payments ledger.

- ✓ **Commission Payment Record**: This record tracks commissions owed to agents based on the premiums collected for policies they issued.
- ✓ **Paid Claims Record**: The treasury department maintains a record for each insurance department that tracks claims payments made, showing the amount paid, the payment date, the policy number, the policyholder's name, the subject of insurance, and the estimated and paid claim amounts. These records are auxiliary journals, and their totals are posted in the general cash book in the accounting department at the end of each period.

1-2 Accounting Ledgers:

The accounting department maintains several ledgers to ensure the accuracy of the transactions conducted by the insurance company. The number and size of these ledgers depend on the scale of the company’s operations. Commonly used accounting ledgers include:

- **General Cash Book**: Also known as the receipts and payments register, it records the totals from the subsidiary cash books maintained by the treasury department. It also records all types of receipts and payments, providing a detailed analysis of the various payment and collection items.
- **General Journal**: This records all company operations periodically, either on a monthly or other periodic basis. The size and number of fields in this ledger are determined by the nature of the work, including the volume and scope of operations and the importance of each account.
- **General Ledger**: This ledger contains all of the company's accounts. Monthly, it posts the totals of recurring accounts, while non-recurring accounts are posted daily.
- **Subsidiary Journals and Ledgers**: Insurance branches are considered primary accounts in insurance companies, and each type of insurance has a primary column in both the general journal and the general ledger. Since each insurance branch contains several accounts, these accounts are further detailed into subsidiary accounts, clearly outlined in the subsidiary journals and ledgers to facilitate the recording of financial transactions and provide clarity regarding the balances of each subsidiary account.

2- Objectives of the Accounting System in Insurance Companies:

The accounting system in insurance companies aims to:

- Record financial events related to all insurance operations in chronological order and according to the dates of occurrence.
- Post those recorded events to the relevant accounts, reconcile them, and make the necessary adjustments at the end of the period.
- Prepare the closing accounts necessary to determine the results of operations for the period and prepare the closing balance sheet to determine the net result at the end of the financial period.
- Assist in providing the necessary data and reports for control purposes, decision-making, and performance evaluation.

In general, the accounting system aims to provide a set of financial and non-financial information necessary for decision-making by users of financial reports. However, understanding the nature of the accounting system in insurance companies requires an understanding of the nature of their activities, as there are specific characteristics of their business operations.

3- The Chart of Accounts for the Insurance Sector:

The current system for insurance accounting follows the Financial Accounting System (SCF) issued in 2007 and implemented starting in 2010 after it was adapted through notice number 89 issued on March 10, 2011, concerning the chart and rules of account operation, the content of financial statements, and their presentation for insurance and/or reinsurance companies. This notice included the following:

- Provisions specific to insurance and/or reinsurance companies.
- The chart of accounts and the rules for their operation.
- Financial statement templates.
- A glossary explaining the terms used.

The chart of accounts for the insurance sector includes:

- **Class 1: Own Funds**
- **Class 2: Fixed Assets**
- **Class 3: Technical Provisions**
- **Class 4: Accounts Payable**
- **Class 5: Financial Accounts**
- **Class 6: Expenses**
- **Class 7: Revenues**

Class 01: Capital Accounts

The capital accounts have not changed under the financial accounting system and include:

- Accounts 10-11-12-13-15-16-17-18.
- Account 14 - Technical Provision: Previously available in the financial accounting system, it has now been allocated to "Regulated Provisions" required by law to meet the technical commitments made by the insurance or reinsurance company to policyholders. It branches into:

- ✓ Account 140 (Guarantee Provisions): For life insurance, defined by law as 1% of total premiums recorded during the year, even if the company experiences a loss.
- ✓ Account 141 (Additional Provisions for Claims to be Paid): Used for insurance against risks, set at 5% of claims to be paid.
- ✓ Account 142 (Provisions for Risks and Disasters): These provisions contribute to national solidarity in the face of natural disasters and are set at 95% of the technical profit from disaster insurance operations.

- Account 19: Previously available in the financial accounting system, this is now labeled "Funds or Values Received from Reinsurers" and represents the guarantee received from the reinsurer for the ceded risks.
    - ✓ Account 190/Related Entities: Debt from cash balances received from related entities.
    - ✓ Account 191/Contributing Entities: Debt from cash balances received from contributing entities.
    - ✓ Account 192/Other Entities: Debt from cash balances received from other entities.

Class 2: Fixed Assets

This group includes all accounts provided by the financial accounting system, except for certain exclusions such as the accounts related to industrial equipment and depreciation due to their non-existence in insurance and/or reinsurance companies.

- Account 277: Previously in (SCF) to record amounts deposited with ceding companies by the reinsurance company, now referred to as "Funds or Values Deposited with Ceding Companies," representing commitments made by the reinsurer against reinsurance contracts.

Class 3: Technical Provisions (No Inventory in Insurance Companies)
Due to the absence of inventory of materials and supplies in insurance companies and the importance of technical provisions, accounts in this group are allocated to provisions related to insurance activities, mandated by the legislature. These provisions represent a crucial aspect of insurance company accounting and reinsurance.

Technical provisions are defined as potential expenses to fulfill the agreements made between the insurance company and its policyholders, whether individuals or entities. In other words, they are provisions established to ensure the complete settlement of obligations undertaken by the insurance company for policyholders, in addition to being used to adjust premiums.

It is important to note that the accounts in Class 03 appear in both assets and liabilities as follows:

- **Liability Accounts**: These relate to obligations to policyholders, beneficiaries of insurance contracts, cedents, and retrocedents.

- **Asset Accounts**: These pertain to the rights of shared insurance and reinsurance companies (the share of shared and reinsurance companies in these liabilities).

Note: A distinction must be made between:

- Damage insurance operations and life insurance operations.
- Premium provisions (contributions) and accident provisions.
- Current premium provisions and provisions for previous years' premiums.
- Direct operations and operations at acceptance for both shared insurance and reinsurance.

These distinctions are further detailed in the chart of accounts for the insurance sector with different accounting numbers, despite the similarities in the names of the main and subsidiary accounts.

Class 4: Third-party Accounts

The insurance activity in third-party accounts is limited to accounts 40 and 41, while the remaining accounts are the same as those found in the Financial Accounting System (SCF).

- **Account 40**: Represents the current account for transactions with cedents, retrocedents, ceding companies, cedents and retrocedents who are considered the main suppliers of services. Account 40 branches into the following sub-accounts:
    - ✓ **Account 401**: Current account for cedents and retrocedents.

  - ✓ **Account 402**: Current account for ceding companies and retrocedents.
  - ✓ **Account 403**: Current account for reinsurance brokers.
  - ✓ **Account 404**: Current account for co-insurance policyholders.
- **Account 41**: Rights and debts arising from direct insurance and co-insurance operations. These include all rights and debts resulting from the sale of insurance contracts. This account branches into the following sub-accounts:
  - ✓ **Account 411**: Policyholders.
  - ✓ **Account 412**: Insurance agents.
  - ✓ **Account 413**: Policyholders – Commercial papers for collection.
  - ✓ **Account 416**: Questionable policyholders.
  - ✓ **Account 417**: Questionable insurance brokers.
  - ✓ **Account 418**: Policyholders – Premiums under negotiation.
  - ✓ **Account 419**: Creditor policyholders, advance payments received, discounts granted, and other assets that need to be created.

At the **Account 46** "Various Debtors and Creditors," the **Account 460** "Suppliers" replaces **Account 401** in the Financial Accounting System.

Class 5: Same Accounts as in the Financial Accounting System

Class 6: Expenses

This class represents the total liabilities resulting from the guarantees granted by the insurance and reinsurance companies when the insured risk occurs, compensating either the cedent or the co-insurer.
The particularity of recording this account lies in its connection with estimates and evaluations calculated based on declared or potentially declared incidents during the year, which are recorded in Class 03 (Technical Provisions).
The expense (service) accounts, like technical provisions, are divided into two main types: Property Insurance and Life Insurance:

- **Account 600**: Service performance on direct operations - Property insurance.
- **Account 601**: Claims on accepted reinsurance operations - Property insurance.
- **Account 602**: Service performance on direct operations – Life insurance.
- **Account 603**: Claims on accepted reinsurance operations – Life insurance.
- **Account 608**: Ceded share of co-insurance services.
- **Account 609**: Ceded share of reinsurance services.
- Sub-account **601** was created to record consumption of various materials and supplies.
- At **Account 66**, for financial expenses, sub-account **663** records interest paid on deposits to cedents and retrocedents.

Accounts 63, 65, 66, 67, 68, 69 remain the same as in the Financial Accounting System.

Class 7: Revenue Accounts

- **Account 70** records premiums, which represent the main aspect of covering risks. Premiums (also known as contributions) represent the amount underwritten by the insurer or policyholder to cover the potential risk, as the service provided by the insurance sector is risk coverage. This premium is recorded through an insurance contract and can be adjusted if necessary. The account branches into the following sub-accounts:
  - **Account 700**: Premiums from direct operations – Property insurance.
  - **Account 701**: Premiums upon acceptance – Property insurance.
  - **Account 702**: Premiums from direct operations – Life insurance.
  - **Account 703**: Premiums upon acceptance – Life insurance.
  - **Account 708**: Ceded share of co-insurance in premiums.
  - **Account 709**: Ceded share of reinsurance in premiums.
- **Account 71**, previously available in the financial accounting system, is now "Deferred Premiums," which records the portion of premiums related to subsequent years.

- Due to the absence of a concept of inventory or stored goods in insurance and reinsurance companies, **Account 72** is used to record commissions due to cedents and retrocedents in relation to the assignment and retrocession process in reinsurance under the title "Reinsurance Commissions."
- At **Account 76**, for financial income, sub-account **764** records interest received on deposits, representing rewards for deposits held by cedents and retrocedents.

Section 3: Accounting Treatment of Insurance and/or Reinsurance Operations

1. **Accounting Treatment of Insurance Operations**

The accounting treatment of operations in insurance companies is carried out through the following entries:

- Accounting treatment of insurance premiums (production process).
- Accounting treatment of brokerage operations.
- Accounting treatment of claims (damage compensation).
- Accounting treatment of appeals.

1-1 Accounting Treatment of Insurance Premiums (Production Process)

In insurance companies, production refers to the process of entering into insurance contracts directly with policyholders. This agreement is documented through a contract called the "Insurance Contract," which includes various clauses such as the insurance premium, the insurance period, the type of risk, what is covered, etc. The premium is recorded as follows:

A. The insurance transaction is recorded upon signing the contract, resulting in a receivable from the insured company:

Debit Account	**Credit Account**	**Description**	**Debit Amount**	**Credit Amount**
411		Policyholder - Premiums for collection		
	7000	Direct insurance premiums - Property insurance		
	7020	Direct insurance premiums - Life insurance		
	7003	Insurance contract expenses and their accessories - Property insurance		
	7023	Insurance contract expenses and their accessories - Life insurance		
		VAT on issued premiums		
	44501	Vehicle Guarantee Fund (FGA)		
	4431	Stamp duties on size		
		Progressive stamp duties		
	44271	Recording the issuance of the		
	44272	insurance policy		

The insurance policy consists of the following elements:

- **Insurance premium or net premium**, which includes (damage premium + civil liability premium);
- **Expenses related to the contract** (commissions or costs);
- **Guarantee funds** (FGA, FGAS, FGCA), where:
  - ✓ **Automobile Guarantee Fund (FGA)**: Established by Ordinance 74/15, this fund aims to cover the damages resulting from bodily injuries in traffic accidents where the driver or victim is unknown or uninsured. The fund collects and pays the subscription amount, which is collected from policyholders. It applies to all types of vehicles (passenger vehicles, trucks, trailers, etc.) and is set at 3% of (civil liability premium + related expenses).
  - ✓ **Policyholders' Guarantee Fund (FGAS)**: This fund collects money to pay, "within available resources," all or part of the debts arising from insurance contracts for insurance companies in case they are unable to pay (lack of assets).
  - ✓ **Agricultural Damage Guarantee Fund (FGCA)**: This fund is intended to financially support farmers in the event of damage to agricultural equipment and products.
- **Stamp Duty (DT)**:
  - ✓ **Volume-based Stamp Duty (DTD)**: This is calculated based on the size of the paper and the number of pages,

according to Article 52 of the Stamp Duty Law.

Volume-based stamp duty = Number of pages × Cost per page.

Paper Type	Price
Register Paper	60 DZD
Ordinary Paper	40 DZD
Half Sheet of Ordinary Paper	20 DZD

The source: Article 52 of the Stamp Law

Stamp Duty Graduated (DTG) Droit de Timbre Gradué: This tax is only imposed on automobile insurance contracts and agricultural equipment insurance contracts. It does not appear in personal insurance. The graduated stamp duty rate for automobile insurance certificates is determined based on the premium amounts, according to the following table:

Premium Amount	Rate
Premium ≤ 2500 DZD	300 DZD
Premium between 2500 DZD and 10000 DZD	5% of the premium
Premium between 10000 DZD and 50000 DZD	3% of the premium
Premium ≥ 50000 DZD	2% of the premium

Source: Article 8-147 of the Stamp Law

Stamp Duty (SD): According to Article 100 of the Stamp Law, if the premium is paid in cash, the stamp duty is calculated as 1% of the amount (Tax Included), or 1 DZD for every 100 DZD, with a minimum of 5 DZD and a maximum of 2500 DZD.

Value Added Tax (VAT): This tax is applied to the sales of the insurance company at a rate of 19% on (the net premium + attached expenses). The agency pays it to the state treasury after collecting it monthly and sending it to its associated unit. The unit records it every three months in the journal of miscellaneous transactions. Note that insurance agreements for personal insurance, natural disasters, and reinsurance agreements are not subject to VAT, as stated in Article 9 of the Value Added Tax Law.

Value Added Tax (VAT) = (Net Premium + Attached Expenses) × 19%

Total Premium = Net Premium + Attached Expenses + VAT + Stamp Duty + Guarantee Funds

B. Payment Stage: The insured party pays the total premium based on the contract amount, either in cash or via bank transfer.

- If paid in cash: A corresponding intermediary account, which is the "cash" account, is used to record the daily transactions for the insured. The journal entry is made in the cash journal (code 530), reflecting the collections for that day, as follows:

Debit A/C No.	Credit A/C No.	Account Description	Debit Amount	Credit Amount
530		Cash Account	44,270	
	411	Policyholder Account		44,000
	44270	Stamp Duty Rights Account		270
		Recording the collection of the premium in cash in the cash journal		

The funds are then transferred to the agency's bank account. This involves transferring the cash premiums collected from various insurance contracts into the bank account used by the agency. The accounting entries are as follows:

Entry for Transferring Funds:

Debit A/C No.	Credit A/C No.	Account Description	Debit Amount	Credit Amount
581		Financial Transfers Account		
	530	Cash Account		
		Balancing the Cash Account		
512		Banks – Current Accounts		
	581	Financial Transfers Account		
		Balancing the Financial Transfers Account		

If the Payment is Made by Cheque:

In this case, the accounting process goes through the following steps:

Step 1: Submission of the Cheque by the Policyholder

An intermediary account, "Cheques Presented for Collection" (Account 511), is used to offset the policyholder account (Account 411), with the following entry:

Debit A/C No.	Credit A/C No.	Account Description	Debit Amount	Credit Amount
511		Checks Presented for Collection Account		
	411	Policyholder Account		
		Recording the presentation of a check by the policyholder in the bank journal		

Step 2: The Agency's Creditor Status Toward the Bank

After the agency sends the cheque to its bank, two scenarios may occur:

Scenario 1: Bank Issues a Credit Advice

Once the cheque is received and validated by the bank, the intermediary account is cleared, and the bank account of the agency is updated as follows:

Debit A/C No.	Credit A/C No.	Account Description	Debit Amount	Credit Amount
512		Banks – Current Accounts		
	511	Checks Presented for Collection Account		

		Collection of the check amount		

Scenario 2: Returned Cheque Due to Insufficient Funds

If the cheque is dishonored, the intermediary account is offset by creating a "Doubtful Policyholder on Unpaid Cheque" account

Debit A/C No.	Credit A/C No.	Account Description	Debit Amount	Credit Amount
4162		Doubtful Policyholder – Unpaid Check		
	511	Checks Presented for Collection Account		
		Recording the return of an unpaid check		

If the cheque is rejected, additional fees may apply. These may be borne either by the insurance company or the policyholder. The accounting treatment varies accordingly:

Case 1: Policyholder Bears the Charges

Debit A/C No.	Credit A/C No.	Account Description	Debit Amount	Credit Amount
416		Doubtful Policyholder Account		
	512	Banks – Current Accounts		

		Recording financial expenses borne by the policyholder		

Case 2: Insurance Company Bears the Charges

Debit A/C No.	Credit A/C No.	Account Description	Debit Amount	Credit Amount
668		Other Financial Expenses Account		
	512	Banks – Current Accounts		
		Recording financial expenses borne by insurance companies		

Example: Insurance Contract Issuance

An insurance company issued a car insurance policy with the following details:

- Contract Start Date: 01/07/2022
- Contract End Date: 30/06/2023
- Net Premium: 60,000 DZD
  - Civil liability portion: 40,000 DZD
- Additional Charges: 5,000 DZD
- Fixed Stamp Duty: 60 DZD
- Progressive Stamp Duty: 500 DZD
- Motor Insurance Guarantee Fund (FGA): 3%
- VAT: 19%

- Payment: Cash
- Stamp duty rate: 1%

Required: Calculate the gross premium and record the insurance issuance and collection.

Solution:

- **VAT** = (Net Premium + Additional Charges) × 19%
  = (60,000 + 5,000) × 0.19 = 12,350 DZD
- **FGA Contribution** = (Civil Liability Premium + Additional Charges) × 3%
  = (40,000 + 5,000) × 0.03 = 1,350 DZD
- **Gross Premium (TTC)** = 60,000 + 5,000 + 12,350 + 1,350 + 60 + 500 = **79,260 DZD**
- **Stamp Duty (1%)** = 79,260 × 0.01 = **792.60 DZD**

Accounting Entry for Insurance Issuance

1. Issuance of Insurance Policy

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
411		Policyholders Account	79,260	
	7000	Direct Premium – Property Insurance		60,000
	7003	Additional Contract Charges		5,000

	44501	Value Added Tax (VAT)		12,350
	44271	Fixed Stamp Duty		60
	44272	Progressive Stamp Duty		500
	4431	Motor Insurance Guarantee Fund (FGA)		1,350
		Issuance of Property Insurance Policy		

2. Cash Payment of Insurance Premium

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
53	411	Cash Account / Policyholders	80,052.6	79,260
	44270	Stamp Duty Account		792.6
		Cash Payment for Contract Premium		

3. Transfer of Cash to Bank Account

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
581	53	Financial Transfers / Cash	80,052.6	80,052.6

		Transfer of Cash to Bank Account		

4. Receipt of Funds in Bank Account

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
512	581	Bank – Current Account / Financial Transfers	80,052.6	80,052.6
		Receipt of Transferred Funds in Bank		

c. In the Case of Benefiting from a Discount:

Sometimes, the policyholder benefits from a discount at the time of issuing the insurance contract. This discount is recorded as a debit to account **7008 – Discounts Granted on Issuance – Property Insurance**. In the case of personal insurance, the discount is recorded under account **7028 – Discounts Granted on Issuance – Personal Insurance**.

The granted discount is considered a **reduction in the turnover of the insurance company**. Accordingly, the accounting entry for the insurance contract in the case of benefiting from a discount is recorded as follows:

Debit Account	Credit Account	Description
411		Policyholder – Premiums Receivable
7008		Discount Granted on Premiums – Property Insurance
7028		Discount Granted on Premiums – Personal Insurance
	7000	Direct Premiums – Property Insurance
	7020	Direct Premiums – Personal Insurance
	7003	Insurance Contract Expenses – Property Insurance
	7023	Insurance Contract Expenses – Personal Insurance
	44501	Value Added Tax (VAT) on Premium Issuance
	44431	Motor Insurance Guarantee Fund (FGA)
	44271	Fixed Stamp Duty
	44272	Progressive Stamp Duty
		Recording the Issuance of an Insurance Policy with Discount

Based on the Previous Example:

Let us assume that the policyholder benefited from a **10% discount** on the net premium at the time of issuing the insurance contract. The corresponding accounting treatment would be as follows:

Since the policyholder receives a 10% discount on the net premium, this will affect:

- **Account 411 – Policyholders**, as the receivable amount will decrease
- **Account 44501 – VAT**, as the tax is calculated based on *(net premium after discount + additional charges)*
- **Account 4431 – Motor Insurance Guarantee Fund (FGA)**, as it is calculated based on the civil liability premium included in the net premium

Calculation Details:

- **Account 7008 – Discount Granted on Premiums (Property Insurance):**
  60,000 × 10% = **6,000 DZD**
- **Account 44501 – Value Added Tax (VAT):**
  (60,000–6,000)+5,000(60,000 – 6,000) + 5,000(60,000–6,000)+5,000 × 19% = **11,210 DZD**
- **Account 4431 – FGA Contribution:**
  (40,000–4,000)+5,000(40,000 – 4,000) + 5,000(40,000–4,000)+5,000 × 3% = **1,230 DZD**

1. Insurance Policy Issuance with 10% Discount

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)

411		Policyholders – Premiums Receivable	72,000	
7008		Discount Granted on Premiums – Property Insurance	6,000	
	7000	Direct Premiums – Property Insurance		60,000
	7003	Insurance Contract Expenses – Property Insurance		5,000
	44501	Value Added Tax (VAT)		11,210
	44431	Motor Insurance Guarantee Fund (FGA)		1,230
	44271	Fixed Stamp Duty		60
	44272	Progressive Stamp Duty		500
		Issuance of Insurance Policy with 10% Discount		

2. Cash Payment of Contract Premium

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
53	411	Cash Account / Policyholders	72,720	72,000
	44270	Stamp Duty Account		720
		Cash Payment of Insurance		

		Contract Premium		

3. Transfer of Cash to Bank Account

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
581 53		Financial Transfers / Cash Account	72,720	72,720
		Transfer of Cash to Bank Account		
512		Bank – Current Account	72,720	
	581	Financial Transfers		72,720
		receiving transferred cash in the bank account		

d. Insurance Contract Modification:

The modification of an insurance contract results in what is known as an **endorsement**, which constitutes a supplementary insurance agreement. It is issued at the request of the customer in order to introduce changes or amendments to the original, currently active contract. Endorsements can be **positive** or **negative**.

- **Positive Endorsement:**
  This involves issuing an additional premium. Examples include the extension of the contract duration or the inclusion of additional risks. The accounting treatment for a positive endorsement follows the same process as the issuance of a new contract.
- **Negative Endorsement (or Cancellation of the Insurance Policy):**
  The policyholder may cancel the contract or reduce the amount of the premium. In such cases, the cancelled portion of the premium is refunded, while the policyholder remains responsible for the associated administrative expenses and stamp duties.

The accounting treatment for a negative endorsement is as follows:

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
7009		Cancelled Premiums – Property Insurance	×××	
7029		Cancelled Premiums – Personal Insurance	×××	

44501		VAT on Cancelled Premiums	×××	
4431		Guarantee Fund Contributions (if refundable)	×××	
	411	Policyholders		×××
	7003	Cost of Premium and Related Expenses – Property Insurance		×××
	7023	Cost of Premium and Related Expenses – Personal Insurance		×××
	4451	VAT on Contract Expenses		×××
	44271	Fixed Stamp Duty		×××
		Negative Endorsement (Cancellation of Insurance Policy)		

Note:

In the case where the **negative endorsement** (cancellation) occurs **after the collection of the contract's receivables from the policyholders**, **Account 419 – Refunds Granted** is used instead of **Account 411 – Policyholders**.

Example:

On March 9, 2023, the insurance company SAA issued a negative endorsement with the following details:

- Cancelled net premium: 12,000 DZD
- Additional contract charges: 500 DZD
- Fixed stamp duty: 40 DZD
- Value Added Tax (VAT): 19%

Required:

Record the accounting entry for the negative endorsement at the insurance company SAA.

Solution:

The accounting entry at SAA Insurance Company is as follows:

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
7009		Cancelled Premiums – Property Insurance	12,000	
44501		VAT on Cancelled Premiums	2,280	
	419	Refunds Granted		13,645

	7003	Insurance Contract Expenses – Property Insurance		500
	4451	VAT on Contract Expenses		95
	44271	Fixed Stamp Duty		40
		Negative Endorsement of Insurance Contract – SAA		

e. Premium Deferral (Carrying Forward of Premiums):

In many cases, the insurance contract period extends across two or more financial periods. In adherence to the accrual basis principle (the principle of independence of financial periods), at the end of the financial year, the portion of the net insurance premium that pertains to subsequent years must be carried forward (deferred).

The following accounting entry is recorded at the end of the fiscal year:

- **Deferral of Net Insurance Premiums Related to Subsequent Years:**

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
7150		Deferred Premiums – Property Insurance		
7152		Deferred Premiums – Personal Insurance		

	3000	Deferred Premiums on Direct Insurance Operations – Property Insurance		
	3200	Deferred Premiums on Direct Insurance Operations – Personal Insurance		
		Deferral of Net Insurance Premiums Related to Subsequent Financial Years		

- Reversal of Deferred Premiums from Previous Years:

At the beginning of the following financial period, the previously deferred premiums, which now relate to the current year, are reinstated and become part of the current year's revenue. The following accounting entry is made:

Debit Account	Credit Account	Description 01/01/N+1	Debit Amount (DZD)	Credit Amount (DZD)
3000		Deferred Premiums on Direct Insurance – Property Insurance		

3200		Deferred Premiums on Direct Insurance – Personal Insurance		
	7100	Deferred Premiums from Previous Years – Property Insurance		
	7102	Deferred Premiums from Previous Years – Personal Insurance		
		Reversal of Deferred Premiums into Current Period Revenue		

Example:

Referring to the previous case, the **insurance contract duration spans two financial periods**: **2022 and 2023**.

- **Premium related to the year 2022 (6 months):**

  60,000 × 6/12 = **30,000 DZD**

- **Premium related to the year 2023 (6 months):**

  60,000 × 6/12 = **30,000 DZD**

The accounting entry for the deferral of premiums is as follows:

. Deferral of Premiums to Following Year (31/12/2022)

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
7150		Deferred Premiums – Property Insurance	30,000	
	3000	To: Deferred Premiums on Direct Insurance – Property Insurance		30,000
		Deferral of Premiums for Future Financial Years		

Reversal of Deferred Premiums (01/01/2023)

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
3000		Deferred Premiums on Direct Insurance – Property Insurance	30,000	
	7100	To: Deferred Premiums from Previous Years – Property Insurance		30,000
		Reversal of Deferred Premiums into Revenue for Current Period		

f. Acceptance of Premiums under Co-Insurance Agreements

The accounting registration of a **co-insurance contract** is carried out as follows:

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
4142		Current Account with Co-Insurer – Acceptance		
6224		Co-Insurance Commission Fees		
	70140	Accepted Premiums – Property Insurance		
	70340	Accepted Premiums – Personal Insurance		
	44501	VAT on Accepted Premiums		
		Recognition of Co-Insurance Premium Acceptance		

In the Case of Cancellation or Negative Adjustment of Co-Insurance:

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)

701490		Cancelled Premiums – Property Insurance (Co-Insurance)		
703490		Cancelled Premiums – Personal Insurance (Co-Insurance)		
44501		VAT on Cancelled Premiums		
	6224	Co-Insurance Commission Fees		
	4142	Co-Insurer Current Account – Acceptance		
		Cancellation of Co-Insurance Agreement		

- Premium Collection:

The collection of premiums under a co-insurance agreement may be done either in cash or by bank cheque. The accounting treatment follows the same procedures used for direct insurance premium collection, with the exception that:

- **Account 4142 – Co-Insurer Current Account** is used **instead of**
- **Account 411 – Policyholders**

1.2 Accounting Treatment of Compensation Operations (Claims for Damages)

Compensation refers to the amounts paid (or to be paid) by the insurance company to third parties (the beneficiaries) as reimbursement for verified incidents.

The compensation process involves the following stages:

a. Provisioning (Recognition of Claims Reserves):

When the insured risk occurs, the policyholder is required to file a claim report within 48 hours of the incident. A claims adjuster (expert) evaluates the damage and issues an assessment report.

Based on this report and depending on:

- The nature of the damage
- Whether the policyholder is the victim or liable (e.g., in car insurance)

The insurance company recognizes a claims reserve (provision) corresponding to the estimated compensation amount.

This includes:

- The expected indemnity to be paid
- Any associated costs, such as:
  - Expert fees
  - Legal expenses (if applicable)

The accounting entry upon receipt of the claim report is recorded as follows:

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)

6009		Claims Reserve – Direct Operations – Property Insurance		
6029		Claims Reserve – Direct Operations – Personal Insurance		
	3060	Indemnities and Expenses Payable – Property Insurance		
	3260	Indemnities and Expenses Payable – Personal Insurance		
		Recognition of Claims Reserve (Provisioning)		

- Adjustment of Claims Reserve:

- If the expert's report determines that the compensation amount is greater than the initially recognized claims reserve,
  then the reserve must be increased by recording the same entry used for the initial provisioning.
- If the expert's report determines that the compensation amount is lower than the reserve,
  the reserve must be reduced by the corresponding amount, or fully cancelled if the compensation conditions are no longer met.

In such cases, the accounting entry is recorded as the reverse of the initial provisioning, as follows:

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
3060		Indemnities and Expenses Payable – Property Insurance		
3260		Indemnities and Expenses Payable – Personal Insurance		
	6009	Claims Reserve – Direct Operations – Property Insurance		
	6029	Claims Reserve – Direct Operations – Personal Insurance		
		Reduction or Cancellation of Claims Reserve		

b. Claim Settlement:

After completing the administrative and technical procedures, and verifying both the occurrence of the insured event and the amount of compensation, the indemnity is paid to the policyholder or to the beneficiaries (in the event of the policyholder's death).

The accounting entry is recorded as follows:

- **Payment of the Compensation Amount:**

  At the time of payment, the claims reserve account is debited by the corresponding compensation amount.

1. Payment of Compensation (Claim Settlement):

Debit Account	Credit Account	Description	Debit Amount	Credit Amount
6000		Claims Payable – Property Insurance		
6020		Claims Payable – Personal Insurance		
	512	Banks – Current Accounts		
		Payment of Compensation to Policyholder		
3060		Indemnities and Expenses Payable – Property Insurance		
3260		Indemnities and Expenses Payable – Personal Insurance		
	6009	Claims Reserve – Direct Operations – Property Insurance		
	6029	Claims Reserve – Direct Operations – Personal Insurance		
		Clearing of Claims Reserve (Equivalent to Paid Compensation)		

Payment of Incidental Expenses:

Similarly, when incidental expenses are paid-such as expert fees, legal charges, or other claim-related costs-the claims reserve account is credited by the amount of those expenses.

The accounting entry is recorded as follows:

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
6006		Incidental Expenses – Property Insurance		
6026		Incidental Expenses – Personal Insurance		
	512	Banks – Current Accounts		
		Payment of Incidental Expenses		
3060		Indemnities and Expenses Payable – Property Insurance		
3260		Indemnities and Expenses Payable – Personal Insurance		
	6009	Claims Reserve – Property Insurance (Direct Operations)		
	6029	Claims Reserve – Personal Insurance (Direct Operations)		
		Clearing the Reserve for Paid Incidental Expenses		

Example:

On 05/08/2021, the AXA Insurance Agency entered into a one-year automobile insurance contract with a customer. The contract details were as follows:

- Net premium: 50,000 DZD
- Additional charges: 5,000 DZD
- VAT (19%): (50,000 + 5,000) × 0.19 = 10,450 DZD
- Fixed stamp duty (DTD): 40 DZD
- Progressive stamp duty (DTG): 300 DZD
- Motor Insurance Guarantee Fund (FGA): 900 DZD
- Additional stamp duty: 43 DZD

The total premium: 66,690 DZD

Payment was made in cash and immediately transferred to the bank account the same day.

On 28/08/2021, the policyholder reported a traffic accident to the agency. The initial damage was estimated at 30,000 DZD, with additional expert fees amounting to 25,000 DZD.

On 04/09/2021, an expert was appointed, and the final assessment report determined the total damage to be 35,000 DZD. Both the compensation and expert fees were paid by bank cheque.

Required:

1. Record the previous accounting entries in the journal of AXA Insurance Agency.

2. Record the premium deferral entries at the end and beginning of the financial year.

Deferred premium (for 2022): 50,000 × 7/12 = 29,166.66 DZD

Debit Account	Credit Account	Description 05/08/2021	Amount (DZD)
411		Policyholders	66,690
	7000	Direct Insurance Premiums – Property Insurance	50,000
	7003	Contract-Related Charges – Property Insurance	5,000
	44501	Value Added Tax (VAT)	10,450
	4431	Motor Insurance Guarantee Fund (FGA)	900
	44271	Fixed Stamp Duty (DTD)	40
	44272	Progressive Stamp Duty (DTG)	300
53		Cash	66,733
	411	Policyholders	66,690
	44270	Stamp Duties	43
581	53	Financial Transfers / Cash Account	66,733
512	581	Bank – Current Account	66,733
		28/08/2021	
6009		Claims Reserve – Property Insurance	50,000
	3060	Indemnities & Expenses Payable – Property	50,000
		04/09/2021	
6009		Claims Reserve – Property Insurance	5,000
	3060	Indemnities & Expenses Payable – Property	5,000
6000		Claims Payable – Property Insurance	35,000
	512	Banks – Current Accounts	35,000
6006		Incidental Expenses – Property Insurance	25,000

	512	Banks – Current Accounts	25,000
3060		Indemnities & Expenses Payable – Property	60,000
	6009	Claims Reserve – Property Insurance	60,000
		31/12/2021	
7150		Deferred Premiums – Property Insurance	29,166.66
	3000	Deferred Premiums on Direct Insurance Operations	29,166.66
		01/01/2022	
3000		Deferred Premiums on Direct Insurance Operations	29,166.66
	7100	Deferred Premiums from Previous Years – Property Ins.	29,166.66

1.3 Accounting Treatment of Insurance Intermediation Operations:

When an insurance contract is obtained through intermediaries (such as brokers or general agents), the accounting treatment differs slightly from that of direct insurance.

Instead of using **Account 411 – Policyholders**, the company uses:

- **Account 412 – Insurance Intermediaries**, subdivided as follows:
  - ✓ **4121 – General Agents**
  - ✓ **4122 – Insurance Brokers**

Debit Account	Credit Account	Description	Amount (DZD)
412X		Insurance Intermediary Account (Broker or General Agent)	×××
622		Intermediary Commission	×××

	7000	Direct Insurance Premium – Property Insurance	×××
	7020	Direct Insurance Premium – Personal Insurance	×××
	7003	Contract-Related Charges – Property Insurance	×××
	7023	Contract-Related Charges – Personal Insurance	×××
	44501	VAT on Issued Premiums	×××
	4431	Motor Insurance Guarantee Fund (FGA)	×××
	44270	Stamp Duty – Paid in Cash	×××
	44271	Fixed Stamp Duty (DTD)	×××
	44272	Progressive Stamp Duty (DTG)	×××

1.4 Accounting Treatment of Recourse Claims

Premiums are collected either through the cashier (cash) or the bank, as previously outlined in the procedures for collecting direct insurance premiums.

- **Definition of Recourse:**

Recourse refers to a process whereby an insurance company submits a compensation claim (recourse request) to another insurance company, where the insured party of the latter is the one who caused damage to the former's policyholder.

- **Recourse in Favor of the Insurance Company:**

In certain situations, when the insurance company initially sets up a claims reserve, it may do so under the assumption that its own policyholder was responsible for the incident.

However, if investigations later reveal that the policyholder was in fact the victim, the insurance company becomes entitled to recover the compensation from the insurer of the liable party.

As a result, the company must recognize a receivable from the other insurance company, and reduce the amount of the previously established claims reserve.

This is done by crediting the claims expense and debiting a receivables account, through the following accounting entry:

Recognition of the Recourse Claim:

Debit Account	**Credit Account**	**Description**	**Amount (DZD)**
3067		Recourse Claims Receivable	×××
	6009	Claims Reserve – Property Insurance (Direct Operations)	×××

This accounting entry is recorded upon the recognition or increase of a recourse claim.

However, in the event of cancellation or reduction of the recourse amount, the reverse entry must be recorded.

Furthermore, when the recourse amount is successfully recovered, the corresponding claims reserve must be cleared, as shown in the following accounting entry:

Debit Account	**Credit Account**	**Description**	**Amount (DZD)**
512		Banks – Current Accounts	×××
	6007	Recourse Claims	×××
6009		Claims Reserve – Property Insurance (Direct Operations)	×××
	3067	Recourse Claims Receivable	×××

Recourse in Favor of the Policyholder:

If it is determined that the policyholder is the victim, the insurance company files a recourse claim to obtain compensation from the insurance company of the person responsible for the damage.

Upon receiving the funds, the insurer proceeds to compensate its policyholder for the sustained damage.

The corresponding accounting entry is as follows:

Recognition of Recourse in Favor of the Policyholder

Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)

3067	4196	Recourse Claims Receivable / Compensation Collected on Behalf of Policyholder	XXX	XXX

Upon Receiving the Compensation from the Other Insurance Company, It Is Transferred to the Policyholder as Follows:

Accounting Entry – Receipt of Compensation

Debit Account	**Credit Account**	**Description**	**Amount (DZD)**
512		Banks – Current Accounts	×××
	3067	Recourse Claims Receivable	×××
4196		Compensation Collected on Behalf of the Policyholder	×××
	512	Banks – Current Accounts	×××
3060		Indemnities and Expenses Payable – Property Insurance	×××
	6009	Claims Reserve – Property Insurance (Direct Operations)	×××

2. Accounting Treatment of Reinsurance Operations

An insurance company may transfer a portion of the risks associated with an insurance contract to another insurance company before the occurrence of the insured event, particularly when it believes that its own financial capacity does not allow it to fully compensate the client in case the risk materializes.

This process is known as reinsurance.

The Fundamental Elements of Reinsurance Operations: Assumption, Cession, and Retrocession

2-1 Assumption Operations:

An assumption operation refers to the reinsurance process in which the insurance company acts as the reinsurer. In this context, the company may be either the direct reinsurer or the retrocessionaire. Thus, it becomes the party that accepts the premiums ceded by another party, whether the latter is a direct cedent or a retrocedent. The company that accepts the reinsurance premiums is referred to as the "assuming company" or the "reinsurer."

- **Proof of Premium Acceptance:**

  The accounting records at the assuming company, which has accepted the ceded reinsurance premiums, are recorded as follows:

Debit Account	Credit Account	Description	Amount (DZD)
402		Cedents and Retrocedents	×××
7290		Granted Commissions – Property Insurance Claims	×××
7292		Granted Commissions – Life Insurance Claims	×××

	7010	Accepted Reinsurance Premiums – Property Insurance	×××
	7030	Accepted Reinsurance Premiums – Life Insurance	×××

Accounting Entry – Collection of Ceded Premiums

Description: The collection of ceded premiums can be done either in cash or by cheque. The accounting entry is recorded as follows

Debit Account	Credit Account	Description	Amount (DZD)
512 / 53 – Bank Account / Cash Account		Collection of accepted premium in cash or by cheque	×××
	402 – Cedents and Retrocedents Account	Recording the receipt of premium from the cedent	×××

Notes:

- Commissions are usually calculated as a percentage of the ceded premiums, and the net ceded premium amount - as determined by the cedents or retrocedents - is calculated by subtracting the commission value from the gross ceded premium.
- In certain cases, after the reinsurance contract has been accepted, one of the parties may be forced to cancel the contract. In such cases, the accounting entry is the reverse of the previous entry (i.e., the reinsurance assumption entry).

Posting of Accepted Premiums:

When reinsurance contracts extend beyond a single financial year, the portion relating to future years must be carried forward and recorded as follows:

Debit Account	Credit Account	Description	Amount (DZD)
71510		Deferred Premiums – Property Insurance	×××
71530		Deferred Premiums – Life Insurance	×××
	31000	Accepted Premiums Carried Forward – Property Insurance	×××
	33000	Accepted Premiums Carried Forward – Life Insurance	×××

At the beginning of year N+1, the accounting entry is recorded as follows:

Debit Account	Credit Account	Description	Amount (DZD)
31000		Accepted Premiums Carried Forward – Property Insurance	×××
33000		Accepted Premiums Carried Forward – Life Insurance	×××
	71010	Accepted Reinsurance Premiums – Property Insurance	×××
	71030	Accepted Reinsurance Premiums – Life Insurance	×××

Claims (Indemnities):

When the insured risk occurs, the policyholder contacts their original insurance company (the ceding company), which in turn contacts the company that accepted the reinsurance. The accepting company proceeds to set up a provision (reserve), appoint an expert, and eventually settle the claim. The related accounting entries are recorded as follows:

Debit Account	**Credit Account**	**Description**	**Amount (DZD)**
60109		Claims Reserve – Accepted Reinsurance (Property Insurance)	×××
60309		Claims Reserve – Accepted Reinsurance (Life Insurance)	×××
	3160	Indemnities and Expenses Payable – Reinsurance (Property Insurance)	×××
	3360	Indemnities and Expenses Payable – Reinsurance (Life Insurance)	×××
6010		Reinsurance Claims – Property Insurance	×××
6030		Reinsurance Claims – Life Insurance	×××
	402	Current Account – Ceding and Retroceding Companies	×××
402		Current Account – Ceding and Retroceding Companies	×××
	512	Bank	×××

Important Note: After the claim has been paid, the provision must be reversed accordingly.

Exercise:

On 01/02/2021, SAA entered into a reinsurance contract on behalf of CAAR. The contract included the following details:

- The amount of accepted premiums was DZD 500,000 for a full year.
- CAAR paid a commission of DZD 15,000.

On 01/12/2021, the policyholder submitted a claim to the original insurance company (SAA), which notified CAAR.

Based on the expert's report, a provision of DZD 90,000 was established. The policyholder was compensated 15 days later by a bank cheque for the same amount as the provision.

Required: Record the transactions in CAAR's accounting books.

Solution:

Accounting entries at the insurance company CAAR (the accepting company):

Date	Debit Account	Credit Account	Description	Debit Amount (DZD)	Credit Amount (DZD)
01/02/2021	402	7010	Ceding and Retroceding Companies / Accepted Reinsurance Premiums – Property Insurance	485,000	500,000
	7290		Commission Granted – Property Insurance	15,000	
01/12/2021	60109	3160	Claims Reserve – Accepted Reinsurance (Property) /	90,000	90,000

			Indemnities and Expenses Payable – Reinsurance (Property)		
15/12/2021	6010	402	Claims Paid – Accepted Reinsurance (Property) / Ceding and Retroceding Companies	90,000	90,000
15/12/2021	402	512	Ceding and Retroceding Companies / Bank – Payment of Indemnity	90,000	90,000
15/12/2021	3160	60109	Indemnities and Expenses Payable – Reinsurance (Property) / Claims Reserve – Accepted Reinsurance (Property)	90,000	90,000
31/12/2021	7150	31000	Deferred Premiums – Property Insurance / Accepted Premiums Carried Forward – Property Insurance	41,667	41,667

2. **Cession and Retrocession Transactions:**

   In this case, the insurance company cedes premiums relating to future years and consequently cedes part of its turnover. If the insurance is ceded for the first time, this is referred to as a **cession**. However, if the company cedes premiums that were originally received through reinsurance acceptances — meaning the company had accepted premiums and subsequently ceded them to another company - this is referred to as a **retrocession**.

The accounting entry is recorded as follows:

Recording of Cession and Retrocession Transactions:

Debit Account	Credit Account	Description	Debit Amount	Credit Amount
70900		Ceded Premiums – Property Insurance		
70910		Retroceded Premiums – Property Insurance		
		Ceded Premiums – Life Insurance		
70920		Retroceded Premiums – Life Insurance		
70930	7210	/Commissions Received on Cessions – Property Insurance		
	7211	Commissions Received on Retrocessions – Property Insurance		
	7212	Commissions Received on Cessions – Life Insurance		
	7213	Commissions Received on Retrocessions – Life Insurance		
	401	Current Account – Cessionaries and Retrocessionaries		
		Recording the cession and/or retrocession transaction		

Provision Formation and Compensation:

The accounting entry is recorded as follows:

Debit Account	Credit Account	Description	Debit Amount	Credit Amount
39060		Account of Claims and Expenses Payable – Cession (Property Insurance)		
39160		Account of Claims and Expenses Payable – Retrocession (Property Insurance)		
39260		Account of Claims and Expenses Payable – Cession (Life Insurance)		
39360	**60909**	Account of Claims and Expenses Payable – Reinsurance Acceptance (Life Insurance**)**		
		/ Account of Claims Provisions – Property Insurance		
	60919	Account of Claims Provisions – Reinsurance (Property Insurance)		
	60929	Account of Claims Provisions – Life Insurance		
	60939	Account of Claims Provisions – Reinsurance **(Life Insurance)**		
		recording the compensation amount to be received from the transfer or retransfer transaction.		
401		On the compensation date		

	60900 **60910** **60920** **60930**	Current Account of Cessionaries and Retrocessionaries To / Compensation for Cession Expenses – Non-Life Insurance Compensation for Retrocession Expenses – Non-Life Insurance Compensation for Cession Expenses – Life Insurance Compensation for Retrocession Expenses – Life Insurance Recording the compensation amount.		
512	**401**	Bank to C/ Current Account of Cessionaries and Retrocessionaries Collection of the compensation amount.		
60909 60919 60929 609**39**	39060 39160 39260 39360	Claims Provision – Non-Life Insurance Claims Provision – Reinsurance Non-Life Claims Provision – Life Insurance Claims Provision – Reinsurance Life To / Payments and Expenses for Cession /Recovery – Non-Life Insurance Payments and Expenses for Retrocession /Recovery – Non-Life Insurance / Payments and Expenses for Cession Recovery – Life Insurance / Payments and Expenses for Accepted Reinsurance Payment – Life Insurance Provision settlement.		

➢ Recording of Posting Transactions:

Premiums ceded are posted in the same manner as follows

Debit Account	Credit Account	Description	Debit Amount	Credit Amount
		31/12/N		
39000		Provisions for ceded premiums – Property insurance		
39200		Provisions for ceded premiums – Life insurance		
	71590	To / Ceded premiums to be posted – Property insurance		
	71592	Ceded premiums to be posted – Life insurance.		
		Posting of ceded premiums		
		01/01/N+1		
71090		Ceded premiums to be posted – Property insurance		
71092		Ceded premiums to be posted – Life insurance		
	39000	TO/ Provisions for ceded premiums – Property insurance		
	39200	Provisions for ceded premiums – Life insurance		
		Ceded premiums carried forward from previous years		

➢ Posting operations of retroceded premiums:

Debit Account	Credit Account	Description	Debit Amount	Credit Amount
39100 39300	71591 71593	31/12/N Provisions for retroceded premiums – Property insurance Provisions for retroceded premiums – Life insurance To /Retroceded premiums to be posted – Property insurance / Retroceded premiums to be posted – Life insurance Posting of retroceded premiums		
71091 71093	39100 39300	01/01/N+1 Retroceded premiums to be posted – Property insurance Retroceded premiums to be posted – Life insurance To /Provisions for retroceded premiums – Property insurance Provisions for retroceded premiums – Life insurance Retroceded premiums carried forward from previous years		

Exercise:

According to the previous example, record the necessary accounting entries in the company **SAA**

Debit A/C No.	Credit A/C No.	Date	Description	Debit Amount	Credit Amount
7090		01/12/2021	Ceded Premiums – Property Insurance	500,000.00	
	7210		To/ Commissions Received – Ceded Property Insurance		15,000.00
	401		To/ Current Account – Ceding & Retroceding Parties		485,000.00
			Record the cession transaction		
39060		15/12/2021	Claims Paid and Expenses – Ceded Property Insurance	90,000.00	
	60909		To/Create reserve for cession transaction		90,000.00
401			Current Account – Ceding & Retroceding Parties	90,000.00	
	60900		To/Record indemnity payable by retrocessionaire		90,000.00
512			Bank	90,000.00	

	401		To/Payment of indemnity		90,000.00
60909			Claims Reserve – Property Insurance	90,000.00	
	39060		To/Reversal of previously created reserve		90,000.00
3900		31/12/2021	Provision for Ceded Premiums – Property Insurance	41,667.00	
	71590		To/Record deferral of ceded premiums		41,667.00

3 -Comprehensive Case Study:

During the month of April, the insurance company SAA carried out the following operations:

02/04/2021, SAA signed a property insurance contract with one of its clients (covering a private car) for a period of one year. The contract included the following details:

- Insurance premium excluding tax: 400,000 DZD
- Policy issuance fees: 8,000 DZD
- Value Added Tax (VAT): 19%
- Contribution to the Automobile Guarantee Fund (FGA): 5,000 DZD
- Fixed stamp duty (DT): 500 DZD
- Progressive stamp duty (TG): 400 DZD

- Payment method: by cheque

- 05/04/2021, the client informed the company of an accident, with an initial estimated damage of 50,000 DZD, in addition to related expenses amounting to 3,000 DZD, representing the expert's fees.
- 20/04/2021, after completing all administrative procedures and upon the client's request for a second assessment, the damage reported on 05/04/2021 was confirmed. The final estimated amount of damage was 70,000 DZD, and payment was made by bank cheque.
- 10/05/2021, the company acquired a personal insurance contract (disability coverage) through insurance intermediaries, which included the following details:
  - Insurance premium excluding tax: 40,000 DZD
  - Additional policy-related fees: 2,500 DZD
  - Fixed stamp duty: 70 DZD
  - Stamp tax: 1% of the total premium value
  - Broker's commission: 4,000 DZD
  - Payment method: cash
- 03/06/2021, a client (Client B) reported a car accident, with an estimated damage of 80,000 DZD

- 15/06/2021, the expert's report confirmed that Client B was the victim and that the party at fault was insured by AXA Insurance. A recovery claim was submitted to AXA along with a complete administrative file including the expert report.

- 10/07/2021, after completing all required procedures, AXA Insurance agreed to compensate, and the recovery amount of 80,000 DZD was collected via bank cheque.
- 12/07/2021, the compensation was paid to Client B by bank cheque.
- 01/09/2021, SAA entered into a reinsurance contract with CAAR Insurance, with accepted premiums amounting to 500,000 DZD. SAA paid a ceding commission to CAAR amounting to 1% of the accepted premiums.
- 20/09/2021, the company signed a retrocession agreement with Alliance Insurance for 50% of the reinsurance contract obtained from CAAR on 01/09/2021. In return, SAA agreed to pay a retrocession commission of 5% of the retroceded premium amount.

Required:

Record the necessary accounting journal entries for SAA Insurance.

It should be noted that during the year 2021, previously deferred premiums (recorded in prior years) were reintegrated into the current year's revenue, amounting to 500,000 DZD

Accounting Journal (SAA Insurance Company - 2021)

Debit	Credit	Account Description	Debit Amount (DZD)	Credit Amount (DZD)	Date
3000	7100	Deferred Premiums on Direct Operations - Property Insurance / To: Deferred Premiums from Previous Years - Property Insurance	500,000	500,000	01/01/2021
411		Policyholders	491,420		02/04/2021
	7000	/ To: Direct Insurance Premiums - Property InsuranceInsurance		400,000	
	7003	Policy Fees and		8,000	
	445	AccessoriesVAT		77,520	
	443	FGA Car Fund		5,000	
	44271	Stamp Duty onVolume		500	
	44272	Graduated Stamp Duty		400	
512	411	Bank / Policyholders - Insurance Premium Payment Collection	491,420	491,420	02/04/2021
7150	3000	Premiums to be Deferred - Property Insurance / To:	100,000	100,000	31/12/2021

		Deferred Premiums on Direct Operations - Property Insurance (400,000 x 3/12)			
6009	3060	Claims Reserve - Direct Operations / To: Compensation and Expenses Payable - Property Insurance (50,000 + 3,000)	53,000	53,000	05/04/2021
6009	3060	Claims Reserve - Direct Operations / To: Compensation and Expenses Payable - Property Insurance (Additional Reserve: 70,000 - 50,000)	20,000	20,000	20/04/2021
6000	512	Claims Due - Property Insurance / To: Bank - Compensation Payment	70,000	70,000	20/04/2021
3060	6009	Compensation and Expenses Payable / To: Claims Reserve - Clearing the Reserve	70,000	70,000	20/04/2021
6006	512	Related Expenses of Claims (Expert Fees) / To: Bank	3,000	3,000	20/04/2021
3060	6009	Compensation and Expenses Payable / To: Claims Reserve - Expert Fees Clearing	3,000	3,000	20/04/2021
412 622	 7020	Insurance Brokers Broker Commission	38,995.7 4,000	 40,000	10/05/2021

	7023 44271 44273	/ To: Direct Insurance Premiums - Personal InsuranceContract Fees - Personal Insurance Stamp Duty on Volume Stamp Tax (1%) = (40,000 + 2,500 + 70) x 1% = 425.7		2,500 70 425.7	
53	412	Cash / To: Insurance Brokers - Premium Collection	38,995.7	38,995.7	10/05/2021
6009	3067	Claims Reserve - Direct Operations / To: Compensation and Expenses Payable - Property Insurance	80,000	80,000	03/06/2021
3060	4196	Compensation and Expenses Payable / To: Claims Receivable from Others - AXA Appeal Filed	80,000	80,000	15/06/2021
512	3067	Bank / To: Claims Receivable from Others - Collection from AXA	80,000	80,000	10/07/2021
4196	512	Claims Collected for Policyholder / To: Bank - Compensation Payment to Policyholder (Client B)	80,000	80,000	12/07/2021
3060	6009	Compensation and Expenses Payable / To: Claims Reserve - Clearing the Reserve	80,000	80,000	12/07/2021

402 7290	 7010	Ceding Company and Successors Commission Granted / To: Accepted Premiums - Property Insurance	450,000 50,000	 500,000	01/09/2 021
512	402	Bank / To: Ceding Company and Successors - Premium Collection	450,000	450,000	01/09/2 021
7091	 401 7210	Receded Premiums - Property Insurance / To: Ceded Companies Recession Commission Granted	250,000	 225,000 25,000	20/09/2 021
401	512	Ceded Companies / To: Bank - Recession Commission Payment	225,000	225,000	20/09/2 021
39100	71591	Deferred Premiums on Receded Business / To: Receded Premiums to be Deferred - Property Insurance (250,000 x 9/12)	187,500	187,500	31/12/2 021
71510	31000	Accepted Premiums to be Deferred / To: Deferred Accepted Premiums - Property Insurance (500,000 x 8/12)	333,333. 33	333,333.33	31/12/2 021

Chapter Two: General Framework of Accounting Operations in the Construction and Public Works Sector

The activity of the construction and public works sector is conducted through what is known as **construction (contracting) contracts**, which are agreements concluded between the implementing entity (the contracting company) and the project owner. In this chapter, we will examine the specific characteristics and transactions that distinguish the sector, as well as the governing laws and regulations. Additionally, we will address the **accounting treatment** specific to this sector.

Section One: Introduction to Accounting in the Construction and Public Works Sector

1. The Concept of Contracting Contracts:

Contracting contracts are defined as *agreements between a company and a contractor for the purpose of constructing, reconstructing, restoring, or maintaining tangible assets*. Alternatively, they can be described as *agreements between two parties, under specific terms, to carry out a particular asset or group of assets according to defined specifications*.

According to the **Algerian Civil Code**, Article 549 states:

"A contract is an agreement under which one of the parties undertakes to produce something or perform a task in exchange for compensation (fees) agreed upon with the other party."

According to the Commercial Code, Article 02 stipulates:

"Any construction, excavation, or land preparation operation is considered a commercial activity by its nature."

According to the Public Procurement and Public Utility Delegation Law: Article 02 of Presidential Decree No. 15-274 governing public procurement and public utility delegations states:

“Public procurement contracts are written agreements, within the meaning of applicable legislation, concluded for consideration with economic operators under the conditions set out in this decree to meet the needs of the contracting authority in terms of public works, supplies, services, and studies.”

This Public Procurement Law constitutes the primary legal reference governing the relationship between the contractor (economic operator) and public entities of various forms, including the State, local authorities, public administrative institutions, and public enterprises subject to commercial legislation when tasked with implementing projects that are fully or partially funded by the State or local authorities, either temporarily or permanently.

According to the Algerian Financial Accounting System (SCF), such contracts are classified under *long-term contracts*:

“A long-term contract involves the execution of goods or services, or a group of goods or services, whose start and end dates span different fiscal years. This includes construction contracts, restoration of assets or environments, and service provision contracts.”

According to International Financial Reporting Standard IFRS 15: Revenue from Contracts with Customers (which replaced IAS 11 "Construction Contracts" as of January 2018), a construction contract is defined as:

“An agreement between two or more parties that creates enforceable rights and obligations. The enforceability of rights and obligations in the contract is a legal matter. Contracts may be written, oral, or implied by customary business practices of the entity.”

The practices and mechanisms for establishing contracts with customers vary from one country to another. In Algeria, these contracts are subject to the Public Procurement Law.

2. Parties to Construction Contracts:

The key stakeholders in a contracting activity can be summarized as follows:

- **The Beneficiary (Project Owner):**
  The entity that commissions the project and awards it to the contractor.
- **The Engineer:**
  The individual responsible for designing the project according to the required specifications and applicable standards.

- **The Main Contractor:**

  Represents the construction company, as the party contracted directly with the project owner. The main contractor bears the primary responsibility for executing the contract and may supervise other subcontractors.
- **The Subcontractor:**

  Some construction companies delegate specialized tasks—such as carpentry, plumbing, and electrical work—to companies with expertise in these specific complementary services. These specialized companies are referred to as *subcontractors*, and their tasks are performed under a subcontract agreement between the main contractor (construction company) and the subcontractor.

3.Content of Contracting Contracts:

A contracting contract must include a set of essential conditions, both technical and financial, as well as a number of important details specified in the specifications document. These include:

- The contract price or the method of its determination;
- The project execution period, including the project start and delivery dates;
- The timing and amount of any advance payments, as well as the method of repayment;

- The percentage and schedule of guarantees required by the project owner. These guarantees vary depending on the different stages of the contracting contract. Among them:

• **Bid Bond (Commitment Guarantee):**
Provided by the contractor in the context of public procurement as proof of seriousness if their bid is accepted. It is submitted during the bid stage (technical and financial proposal submission) and usually takes the form of a percentage of the bid amount.

• **Performance Guarantee:**
Required before receiving any advance payment or issuing the first work statement. The performance guarantee is a **bank guarantee** intended to ensure the execution of the project. It represents a commitment from a bank or public procurement guarantee fund to cover the contractor's contractual obligations (e.g., delivery and conformity).
Its value typically ranges from **1% to 5%** for contracts up to DZD 1 billion, and between **5% to 10%** for contracts exceeding DZD 1 billion. Contracts with a duration of less than or equal to three months, as well as contracts related to the restoration of cultural facilities, are exempt from this requirement.

• **Retention of the Performance Guarantee:**
Applied during the preparation of work progress statements.

- Specification of the date for the release of guarantees, usually one month after the final delivery date and after preparing the project handover report;
- Inclusion of subcontracting or delegation arrangements;
- Specification of penalties and compensations in the case of delayed project delivery;
- Inclusion of what is known as **change orders** in the contract annexes, which allow the contractor to incorporate modifications if additional work is required.

4. Characteristics of Contracting Contracts:

The contracting activity is characterized by several features that impact the nature and structure of the financial accounting system. These characteristics can be summarized as follows:

- **Long Execution Periods:**
  The project implementation period often extends beyond a single fiscal year, starting from the date the contract is signed to the final project delivery date. This creates several issues concerning the accounting treatment of revenues and expenses.

- **Diversity of Activities and Specific Operational Requirements:**
  Contracts are governed by specific technical specifications detailed in the tender documents.
- **Stage-Based Project Delivery:**
  Projects are delivered in predefined stages, with each stage invoiced separately through a system known as the **work progress statement** (*Situation des travaux*).
- **Possibility of Subcontracted Work:**
  Certain tasks may be delegated to subcontractors to carry out complementary activities within the overall project. In such cases, the **main contractor** remains fully responsible for those tasks.
- **Subject to Additional Insurance Schemes:**
  In addition to the national social security system (**CNAS**), companies operating in the construction and public works sector are subject to an additional social insurance system known as the Regional Fund for Annual Leave and Weather-Related Work Stoppages (CACOBATPH). This fund is responsible for paying workers' annual leave and compensating for days of inactivity due to adverse weather conditions.
- **Access to Advance Payments and Security Retentions:**
  Contractors may receive advances and be subject to guarantee deductions and sureties that are designed to protect the rights of all stakeholders within the sector.

Section Two: The Adapted Financial Accounting System for the Construction and Public Works Sector

1. Definition of the Adapted Financial Accounting System for the Construction, Public Works, and Hydraulics Sector (SCF-BTPH)

In general, the accounting system aims to provide a set of financial and non-financial information necessary for decision-making by users of financial reports. However, understanding the nature of the accounting system for construction, public works, and hydraulics companies necessarily requires understanding the specific characteristics of these companies' activities.

The adapted financial accounting system for the construction and public works sector, issued under Ministerial Decision No. 203 dated June 1, 2023, and derived from the provisions of Law No. 07-11 dated November 25, 2007, which instituted the Financial Accounting System (SCF) and its implementing regulations, defines and explains the specific operations and activities carried out by companies operating in the construction, public works, and hydraulics sector.

2. Scope of Application of the Adapted Financial Accounting System for the Construction and Public Works Sector

The adapted financial accounting system (SCF-BTPH) applies to all economic entities within the economic and commercial sectors, whether public, private, or mixed-capital, that operate in the following fields:

- Conducting studies, especially in architectural engineering;
- Building and constructing facilities, including residential buildings (collective or individual housing), commercial, industrial, and service premises, as well as social, educational, and cultural structures;
- Urban development (internal and external works), renovation, or demolition depending on the nature of the building;
- Public works, including infrastructure projects such as roads, railways, ports, airports, etc.;
- Hydraulics, which mainly concerns the construction and maintenance of hydraulic works and networks, such as dams, water reservoirs, protective barriers, and infrastructure related to pumping stations, water treatment plants, water supply networks, sanitation, and irrigation systems.

3. Accounting Disclosure for Construction and Public Works Contracts

To ensure the reliability and credibility of financial statements for construction and public works companies, a set of important elements must be disclosed, either within the financial statements or in the accompanying notes. These include:

- Construction contracts concluded by the company during the fiscal year;
- Construction contracts completed by the company during the fiscal year;
- The amount of contract revenue recognized as income during the reporting period;
- The methods used to determine the percentage of completion for recognized contract revenue during the period;
- Total recognized or expected costs and revenues during the reporting period;
- Advance payments received from the project owner during the period;
- Retention amounts withheld by the customer (project owner) related to completed and invoiced work;
- Construction contracts that were halted by the company, along with explanations for the suspension;
- Disclosure of any contingent and/or potential losses related to the contract that were borne by the company during the period;
- Any other relevant information deemed necessary by the company, based on the materiality and usefulness of the information.

4. Accounting Measurement and Valuation Methods for Construction and Public Works Contracts

Due to the specific nature of the contracting sector, several accounting challenges arise in tracking and determining the expenses and revenues of each construction contract to calculate the profitability of each profit center. This is especially significant since such contracts often extend over long periods—usually exceeding one accounting period—requiring a continuous flow of information to enable the accountant to identify and allocate project costs during each fiscal period until the contract is completed.

This requires the use of an appropriate accounting approach to allocate contract revenues and expenses across the necessary accounting periods, while adhering to established accounting principles, particularly:

- The periodicity principle;
- The prudence principle;
- The matching principle (matching revenues with associated costs).

According to the requirements of the adapted accounting system for the sector (SCF-BTPH) and **IFRS 15 "Revenue from Contracts with Customers"**, the following two methods are used for the measurement and valuation of construction and public works contracts:

- **The Percentage of Completion Method (Progress Method)**

- **The Completed Contract Method**

I. The Percentage of Completion Method (Progress Method)

This is the most commonly used method, as it adheres to accounting principles, aligns the legal reality with the economic reality of the company, and requires an effective and accurate information system to measure the volume of work completed, determine the percentage of completion, and forecast potential price variations. However, if estimates are deemed inaccurate, the Completed Contract Method is used to recognize project revenues.

According to Article 2.133 bis of the SCF-BTPH, the progress method facilitates ongoing project accounting throughout the year. It involves recording the revenue and annual profit or loss progressively as the work advances. Once the contractor fulfills their contractual obligations, they must gradually transfer the project management responsibility based on a mutually signed progress report (*Attachement des travaux signé contradictoire*) for the preparation of a work statement (*Situation des travaux*).

At the end of each financial year, the revenue recognized is calculated on a cumulative basis, based on the percentage of work completed under long-term contracts, using the following formula:

Recognized Revenue = Contract Value (excluding tax) × Percentage of Completion

The revenue to be recorded for each fiscal year is determined by:

Revenue to be Recorded = (Contract Value × Percentage of Completion) − Previously Recorded Revenues

Determining the Percentage of Completion

According to IFRS 15, the percentage of completion can be measured using two methods:

A. Input Method (Cost-Based Method)

This method estimates the percentage of completion based on the actual inputs consumed during the execution period, as follows:

Percentage of Completion = Cumulative Actual Costs for Year N / Total Estimated Costs

B. Output Method

This method estimates the percentage of completion based on the number of actual units completed.
For example, if 20 km of a 100 km road project have been paved, the percentage of completion is:

Percentage of Completion = Actual Units Completed / Total Units in the Contract

Example:

A construction project for building a **mosque** was launched by the ETA construction company from January 2, 2020, to November 30, 2022.

- Expected Contract Revenue: 2,000,000 DZD
- Estimated Total Cost: 1,850,000 DZD
- Costs Incurred in 2020: 370,000 DZD
- Cumulative Costs by the end of 2021: 925,000 DZD

Required:

Calculate the project result for fiscal years 2020 and 2021.

2020 Fiscal Year Result:

Step 1: Percentage of Completion (2020)
= 370,000 / 1,850,000 = 20%

Step 2: Revenue to be Recorded
= 2,000,000 × 20% = 400,000 DZD

Step 3: Result for 2020

= 400,000 − 370,000 = 30,000 DZD profit

2021 Fiscal Year Result:

Step 1: Percentage of Completion (2021)

= 925,000 / 1,850,000 = 50%

Step 2: Total Revenue at 50% Completion

= 2,000,000 × 50% = 1,000,000 DZD

Step 3: Revenue to be Recorded in 2021

= 1,000,000 − 400,000 = 600,000 DZD

Step 4: Costs Incurred in 2021

= 925,000 − 370,000 = 555,000 DZD

Step 5: Result for 2021

= 600,000 − 555,000 = 45,000 DZD profit

Debit A/C No.	**Credit A/C No.**	**Date**	**Account Description**	**Debit Amount (DZD)**	**Credit Amount (DZD)**

6XX	512	During 2020	Various Expenses / Bank To record various project expenses	370,000	370,000
417	704	31/12/2020	Payables on Work-in-Progress Work Sales To record 2020 revenue	400,000	400,000
704	417	Beginning of 2021	Work Sales / Payables on Work-in-Progress To reverse 2020 revenue	400,000	400,000
6XX	512	During 2021	Various Expenses Bank To record various project expenses 2021	555,000	555,000
417	704	31/12/2021	Payables on Work-in-Progress / Work SalesTo record 2021 revenue	1,000,000	1,000,000

Important Note:

Actual costs incurred are to be recorded according to their nature in Class 6 accounts during each accounting period. The revenue corresponding to the percentage of completion should be recognized in Account 704. Since the percentage of completion is cumulative, the revenue recognized in previous years must be reversed at the beginning of the subsequent year to ensure accurate accounting of the current year's progress.

II. The Completed-Contract Method

According to the financial accounting system, Article 3.133, this method is also known as the completed-contract method. If the company is unable to apply the percentage-of-completion method to determine revenue from long-term contracts in each accounting period, due to the lack of a precise information system to estimate costs, this method is .used

Under this method, no part of the revenue is recognized until the contract is completed. The company records the contract-related expenses by nature on their respective dates, and at the end of the year, it recognizes the amount of revenue for a specific accounting period equal to the expenses incurred during that period. Thus, costs equal revenues, and the result is zero, with no margin recognized during the early years of execution. This method allows the project result to be recognized at once upon completion, which is why it is referred to as the completed-contract method. The project's result is therefore charged to its final year.

Example:

A mosque construction project was initiated on January 2, 2020, and completed on November 30, 2022, by the contracting company (ETA).

- The expected cost for completing this project was 1,850,000 DZD.
- In 2020, the recorded costs amounted to 370,000 DZD.
- In 2021, the cumulative recorded costs reached 925,000 DZD.
- Upon completion of the project on November 30, 2022, the actual cumulative costs amounted to 1,700,000 DZD.
- According to the contract terms, the contract price is determined based on cost plus a profit margin of 20%.

Required: Necessary accounting entries

Solution:

Contract price = Actual cumulative cost + (0.2 × Actual cumulative cost)

Contract price = 1,700,000 + (0.2 × 1,700,000) = **2,040,000 DZD**

Profit = 2,040,000 − 1,700,000 = **340,000 DZD**

(This effect appears in the final year)

Debit	Credit	Date	Account Name	Debit Amount	Credit Amount

6XX	512	During 2020	Various Expenses / Bank	370000	370000
33	723	31/12/2020	Work-in-Progress Inventory / Change in Work-in-Progress Inventory	370000	370000
6XX	512	During 2021	Various Expenses / Bank 925000-370000=555000	555000	555000
33 	 723	31/12/2021	Work-in-Progress Inventory / Change in Work-in-Progress Inventory	555000	555000
6XX	512	During 2022	Various Expenses / Bank 1700000-925000=775000	775000	775000
723 	 33	30/11/2022	Change in Work-in-Progress Inventory / Work-in-Progress Inventory	925000	925000
411 	 704 4457	30/11/2022	Clients / Revenue from Works / VAT on Sales	2427600	 2040000 387600

Section Three: Accounting Entries According to the Procedures of Contract Execution in Construction Projects

In this section, we will address the accounting treatment of operations specific to the construction and public works sector, excluding other routine operations common to enterprises across various sectors. This will be presented following the chronological sequence of these operations through a series of accounting entries.

1- Purchase of the Tender Document (Cahier des Charges):

The tender document includes the technical specifications and financial proposals of the project. It is offered for sale by the project-owning entity, either directly or through a design office responsible for supervising the works, to any party interested in executing the project. These expenses are considered administrative in nature and are charged to the company as a whole, given that the project has not yet been awarded.

This stage is followed by the deposit of **a bid bond to confirm** the seriousness of participation in the tender. Once the bid evaluation process is completed, the contractor is reimbursed for the deposited amount.

The related accounting entries are recorded as follows:

Debit	**Credit**	**Account Name (Debit / Credit)**	**D/A**	**C/A**
618	53	Documentation Expenses / Cash Purchase of the tender specifications document		
617 4456	512	Studies and Research Recoverable VAT / Bank Payment of expenses for technical & financial bid		
467 2752	512	Other Receivables & Payables Paid Deposits / Bank Submission of the bid bond		

After the contract is signed by the contractor who has been awarded the project, the initial bid bond is refunded following the issuance of a release document (*La main levée*) by the project owner. Upon the reimbursement of the bond amount, the following accounting entry is recorded:

Debit	Credit	Account Name	Debit Amount	Credit Amount
512		Bank Account		
	467	Other Payables and Receivables	DZD (amount)	DZD (amount)

2- Establishment of the Accounting Unit for the Contract:

After the project is awarded to the contractor and a contract is signed between the two parties, a dedicated accounting unit is opened for the project. This is done by assigning a specific accounting code to the project in order to distinguish between the revenues and costs of each project separately. Subsequently, the previously recorded expenses related to the contract, which were initially entered in the institution's general journal, are transferred to the specific account of the project under execution. For example, the sub-code **01** may be assigned to the project.

Debit A/C No.	Credit A/C No.	Account Name	Debit Amount	Credit Amount
61801		Documentation Expenses – Project 01	[amount]	
61701		Studies and Research – Project 01	[amount]	
	618	Documentation Expenses		[amount]
	617	Studies and Research		[amount]

3-Provision of Guarantee or Bond:

In some projects, the submission of a Performance Bond (Caution de bonne exécution) is required from the contractor awarded the project. This is done after signing the contract and prior to the commencement of work, as a guarantee of the contractor’s intention to deliver quality services and works in accordance with the specifications.

The guarantees are recorded based on their duration and the method of provision—whether it is a deposit of funds into a bank account, or a bank guarantee letter, or a guarantee issued by the Public Procurement Fund, which acts as a surety for the contractor before the project owner.

This bond is usually calculated as a percentage of the contract value excluding tax.
The accounting entries depend on the following cases:

Debit A/C No.	**Credit A/C No.**	**Account Name**	**Debit Amount**	**Credit Amount**
467	512	Other Payables and Receivables / Bank	[amount]	[amount]
2752	512	Paid Deposits and Guarantees / Bank	[amount]	[amount]
275		Paid Deposits and Guarantees	[amount]	
627		Bank Charges (Fees)	[amount]	
4456		VAT on Fees	[amount]	
	512	/Bank		[amount]

At the end of the project, and after signing the final acceptance report (without reservations), the bid bond guarantee **is** recovered, following the issuance of the**" Release of Guarantee " or "main levée"** document by the project owner.

The recovery is recorded in the accounts by reversing the initial accounting entry**.**

Debit	Credit	Account Name	Debit Amount	Credit Amount
512	2752	Bank / Cr: Paid Deposits – Performance Bond	[amount]	[amount]

It is also possible, by mutual agreement between both parties, to convert the nature of the bid bond into a performance bond, provided this is explicitly stipulated in the contract specifications (cahier des charges).

4- Recording of Advances (Avances, Acomptes Reçus):

In some projects, the project owner may pay **advances** to the contractor in order to provide the necessary liquidity and facilitate the start of work, in accordance with the contractual terms.

The percentages related to advances, guarantees, and penalties are defined in the contract, and they are applied to the contract price or part of it, excluding VAT.

- The standard VAT rate is 19%.
- A reduced VAT rate of 9% is applied if the project involves the construction of residential housing.

The accounting entries for the invoice related to the collection of advances are recorded as follows:

Debit	Credit	Account Name	Debit Amount	Credit Amount

4111 / 4112 / 4116/		Public Institutions / Local Authorities / Regular Customers	[amount]	
	4191 4457	/ Advances and Payments Received VAT Collected		[amount]
512	4111 / 4112 / 4116	Bank / Public Institutions / Local Authorities / Regular Customers	[amount]	[amount]

The advance amount is recovered by deducting it from the value of the invoiced works, through the work progress statement (Situation de travaux), which is prepared and agreed upon by both parties.

5- Civil Liability Insurance in the Construction Sector:

According to Article 175 of Ordinance 95-07 related to insurance,

"Every architect, contractor, technical inspector, or any stakeholder—whether a natural or legal person—must subscribe to an insurance policy covering their professional civil liability that may arise from construction work, building renovation, or repairs."

The accounting entries are recorded as follows:

Debit	**Credit**	**Account Name**	**Debit Amount**	**Credit Amount**

616 486		Insurance Premiums (Current Year's Expenses) Prepaid Expenses	[amount]	[amount]
	4012	Service Providers	[amount]	[amount]
4012	512 / 53	Service Providers /Bank or Cash	[amount]	[amount]

6- Payroll Processing

The processing of wages in the construction and public works sector follows the same procedures as in other sectors, with the addition of a special insurance scheme under the authority of the Regional Fund for Paid Leave and Weather-related Work Interruptions (CACOBATPH).

According to Executive Decree No. 97-46, published in the Official Gazette No. 08 dated February 4, 1997, the following contribution rates are applied:

- The contribution for paid leave is 12.21%, fully borne by the employer.
- The contribution for weather-related unemployment is 0.75%, shared equally between the employer and the employee (i.e., 0.375% each).

Thus, the total contribution rate of the employer to the CACOBATPH is 12.585%.

As for the National Social Security Fund (CNAS) contributions:

- The employee contributes 9%.
- The employer contributes 26.13%, which is slightly higher than the 26% in other sectors, due to an additional 0.13% allocated to the Occupational Risk Prevention Agency (OPERBATPH) in the public works sector.

All social contributions are calculated based on:

- The individual wage for the employee's share.
- The total payroll for the employer's share.

The accounting entries for monthly wages are recorded at the end of each month as follows:

Debit	**Credit**	**Account Name**	**Debit Amount**	**Credit Amount**	**Transaction Description**
63X		Employee Salaries			Recording gross monthly wages
	431	Social Security Fund – Employee (9%)			Employee's CNAS contribution withheld from salary
	432	Cr: CACOBATPH Fund – Employee (0.375%)			Employee's CACOBATPH contribution withheld from salary
	442	Cr: Income Tax Withholding (IRG)			Income tax withheld from employee salary
	421	Cr: Net Salary			Net amount payable to employee after deductions
635		Social Security Contributions – 26.13%			Recording the employer's contribution

637	431 432	Other Social Charges – 12.585% To /Social Security Fund – 26.13% To/CACOBATPH Fund – 12.585%			
431	512	Social Security Fund (9% + 26.13%) To /Bank			Payment of social security contributions
432	512	CACOBATPH Fund To /Bank			Payment of paid leave and bad weather unemployment contributions (0.375% + 12.585%) = 12.96%

7-Recording the Preparation of the Work Progress Statement (Situation de Travaux):

When preparing the *work progress statement*, which serves as an invoice recording the sales in the revenue account, it reflects the project's progress until completion and the issuance of the final invoice or final progress statement. The value of the statement, excluding VAT, is recorded on the credit side of account **7**04 – Sales of Construction Works (e.g., 7041 – Sales of Building Works, 7042 – Road and Path Paving, 7043 – Civil Engineering and Other Hydraulic Works, 7046 – Handling Works, 7048 – Other Works). It is matched on the debit side with the customer accounts:

- **4111 – Public Institutions and Administrations**,
- **4112 – Local Authorities**,
- **4116 – Ordinary Customers**.

Given the long duration of construction contracts extending over multiple financial periods, and in accordance with accounting principles such as the *periodicity principle* and the *matching principle*, revenue is recognized progressively even if the project is not yet fully delivered. Recognition is based on the portion completed, as defined in the contract, through the preparation of the work progress statement (*Situation de Travaux*).

At the time of preparing the statement, account 4458 – VAT Adjustment Account is used due to the particular nature of VAT recognition in this sector, where the taxable event is *cash receipt* rather than *transfer of ownership*. VAT is then reclassified to the collected VAT account once payment for the statement is received from the client.

The accounting treatment for the preparation of the work progress statement is as follows:

Debit	**Credit**	**Account Name**	**Debit Amount**	**Credit Amount**	**Transaction Description**

411X	704	Clients /Sales of Construction Works (various subaccounts)	[amount]	[amount]	Recording the progress statement excluding VAT
	4458	/VAT Adjustment Account		[amount]	VAT to be settled upon collection
512	411X	Bank / Clients (Public Administrations and Bodies	[amount]	[amount]	Collection of the work progress statement
4458	4457	VAT Adjustment Account /VAT Collected	[amount]	[amount]	Reclassification of VAT upon receipt

In the case of advances with retention deductions, the accounting entry for the work progress statement is as follows:

Debit A/C No.	Credit A/C No.	Account Name	Debit Amount	Credit Amount	Transaction Description
411X		Clients (Public Administrations and Bodies	TTC		Work progress statement issuance
4191		Advances Received	HT		Deduction of advance from progress statement
4117		Retentions	HT		Retention withheld from work performed

	704 4458	/Sales of Construction Work VAT Adjustment		HT VAT	VAT calculated but deferred until payment
512	411X	Bank / Clients (Public Administrations and Bodies	Amount Collected	Amount Collected	Collection of work progress payment
4458	4457	VAT Adjustment / VAT Collected	VAT Amount	VAT Amount	Settlement of VAT upon receipt of payment

Account 411 = (Account 704 + Account 4458) – (Account 4191 + Account 4117)

Account 4458 – VAT Adjustment = (Progress statement amount excluding VAT – Advance amount excluding VAT – Retention amount excluding VAT) × VAT rate
Upon collection of the invoice amount, it is settled with Account 4457 – Collected VAT.

8-Accounting for Transactions Carried Out Under Subcontracting:
Construction companies often resort to subcontractors. The main contractor records subcontracted work under **Account 611 – General Subcontracting**, which is subdivided according to the nature of the assigned work:

- **Account 6111: Subcontracting within all construction works**
- **Account 6112: Subcontracting within major works**

- **Account 6113: Subcontracting within secondary construction works**

8-1 Advance Payment to the Subcontractor:

The main contractor may provide an advance to the subcontractor, which will later be deducted from the value of the executed work as part of the progress statement. The accounting entry is recorded as follows:

Debit	Credit	Account Description	Debit Amount	Credit Amount
409		Account Payable – Advances		
4456		Recoverable VAT		
	512	Bank **Advance payment to subcontractor**		

8-2. Retention of Performance Guarantee in Subcontracting Operations (Subcontractor)

The main contractor deducts a portion of the subcontracting contract value as a guarantee for the proper execution of the works performed by the subcontractor, to ensure maintenance and quality of execution. This guarantee is reimbursed after the completion of the agreed-upon works and verification of their proper execution through subcontracting. The journal entries are recorded in the main contractor's books as follows:

A/C No. (Dr/Cr)	Account Description (Dr / Cr)	Debit Amount	Credit Amount
611 4456/ 4017 4013	On the date of receiving the work statement: General subcontracting Recoverable VAT TO/Retention account / Subcontractors Recording the receipt of the work statement from the subcontractor and the deduction of the retention amount.		
4017 4456 /4013	On the date of receiving the retention release invoice: Suppliers – Retention Recoverable VAT / Subcontractors		

	Recording the receipt of the retention release invoice.		
4013/ 512	On the date of payment: Subcontractors / Bank Payment of the retention release invoice.		

9- Accounting for Contract Penalties and Late Payment Interest:

According to Article 147 of Presidential Decree No. 15-247, which governs public procurement and public service delegation, financial penalties may be imposed in the event of failure by the contractor to meet contractual obligations within the agreed deadlines, or if the work is not in conformity with the specifications, without prejudice to other legal penalties provided for by applicable legislation.

The contractual terms of the agreement specify the penalty rate and the conditions for its application or exemption, in accordance with the terms of reference (Cahier des Charges).
The decision to exempt the contractor from paying penalties due to delays lies with the contracting authority (project owner) in the following cases:

- If the delay was not caused by the contractor (the party responsible for execution);

- In the case of force majeure (e.g., unexpected natural disasters such as earthquakes, volcanic eruptions, etc.), within the limits defined by the orders to suspend and/or resume work.

The financial penalties are calculated (if the rate is specified in the contract per month of delay) as follows:

Financial Penalty = (Value of the delayed work statement (or contract value) × Penalty Rate %) × (Number of delay days / 30 days)

Note:
The delay period is the time between the contractual due date for submitting the work statement or project handover, and the actual date of submission or handover, as applicable.

9-1 Recording Penalties for Delays in Contract Deadlines or Non-Compliance with Contract Specifications

The contractual financial penalties imposed on the contractor (responsible for execution) are deducted from the value of the work progress statement that is due to be paid—meaning they are withheld at the source during the settlement process, as follows:

A. Recording the Executed Work Progress Statement

Debit	Credit	Account Name	Debit Amount	Credit Amount	Transaction Description
411X 419 4117	 704 4458	Clients Received Advances Guarantee Retention Deduction /Sales of Works A/C /VAT Adjustment A/C	TIT ET ET	 ET VAT	Preparation of the Work Progress Statement
 411X	 512	**On the Date of Collection** Clients / Bank			Collection of the Work Progress Statement
4458	 4457	VAT Adjustment /Collected VAT			VAT Adjustment upon Collection

TIT (*Total Including Tax*) / **ET** (*Excluding Tax*)

B- **Upon Recording the Collection Entry**, and in the Case of Financial Penalties Related to the Contractual Deadline or Non-Compliance with the Specifications, the Entry is Recorded as Follows:

Debit	Credit	Account Name	Transaction Description

		On the Date of Collection	Collection of Work Progress Statement No. .....
512		Bank	
419		Received Advances	
6561		Penalties on Contracts and Late Payment Interest	
	411	/ Clients	

9-2 Recording of Late Payment Interest:

The payment deadlines are defined in the contract. The project owner shall inform the contractor in writing of the payment date, i.e., the date the payment order or check is issued.

Failure to make payment within the deadlines specified in the contract entitles the contractor to claim late payment interest, calculated based on the key interest rate set by the Bank of Algeria plus one (+1) point, starting from the day following the end of the contractual payment deadline.

It is recorded in the accounts as follows:

Debit	Credit	Account Name	Transaction Description
		On the Date of Collection	Collection of Work Progress Statement No. .....
512		Bank	
419		Received Advances	
	411X		

	758	/ Clients (Public Administrations and Bodies /Other Revenues	

10-Comprehensive Case Study

In 2021, the Public Works Contracting Company (ETPE) signed a public contract with the AADL Agency for the construction of 1,000 housing units in one of the municipalities. The contract value was 300,000,000 DZD excluding VAT, and the relevant contract information is as follows:

- Contract number: 245/2021 dated 15/02/2021
- Start of execution: 01/04/2021
- Project delivery date: 30/03/2024
- Project to be delivered in 4 phases through the preparation of work progress statements at the end of each fiscal year.
- Advance payment: 10% of the contract value excluding VAT
- Guarantee withholding (Retenue de Garantie – RG): 5%
- Possibility of converting the bid bond into a performance bond

In the course of executing the project, the company carried out the following operations:

- On 01/02/2021: The company purchased the project's specifications document (Cahier des charges) for 25,000 DZD in cash.

- On 05/02/2021: It paid the expenses for the technical and financial proposal for the project amounting to 35,000 DZD in cash.
- On 08/02/2021: It paid a bid bond (Caution de soumission) equivalent to 5% of the contract value excluding VAT.
- On 01/03/2021: After winning the contract and signing it with the client, the bid bond was converted into a performance bond (Caution de bonne exécution) in accordance with the conditions stated in the specifications and the contract.
- On 20/04/2021: The company paid civil liability insurance for workers to an insurance company, under insurance policy number 2021/05, amounting to 180,000 DZD, covering the project period from 01/04/2021 to 30/03/2024. The payment was made by bank cheque.
- On 01/06/2021: The company received an advance payment from the AADL agency equivalent to 10% of the contract value excluding VAT, which is to be recovered through the submitted work progress statements, in accordance with the signed contract.
- On 02/07/2021: The company purchased raw materials (cement) for 4,800,000 DZD via bank cheque No. 0025. Transportation costs were 35,000 DZD, and VAT at 19% was paid in cash.
- On 05/07/2021: As part of project execution, the company signed a subcontract with a subcontractor responsible for sanitary plumbing,

gas, and electrical heating works for an amount of 12,000,000 DZD.

- On 25/09/2021: The company prepared the monthly payroll for workers and transferred salaries to their bank accounts. It also paid various social security institutions and the tax authority. The gross salary base amounted to 1,450,000 DZD, and the individual income tax (IRG) was 190,000 DZD.
- On 30/09/2021: The company paid water and electricity expenses for Q3, amounting to 15,000 DZD and 4,500 DZD respectively, in cash, with VAT at 19%.
- On 01/11/2021: The subcontractor submitted work progress statement No. 01 for the year 2020, for 7,000,000 DZD excluding VAT (with VAT at 19%). The guarantee withholding (RG) was 5% of the total amount including VAT. Payment to be made after one month.
- On 31/12/2021: The first project phase was completed, representing 15% of the contract value, as per work progress statement No. 01. The guarantee withholding was 5% of the total amount including VAT, and payment was to be made after 15 days.
- On 28/02/2022: The second phase was completed, representing 45% of the contract value, as per work progress statement No. 02, with a 5% guarantee withholding on the total including VAT. Payment after 15 days.

- On 31/12/2023: The third phase was completed, representing 30% of the contract value, as per work progress statement No. 03, with 5% RG on the total including VAT. Payment after 15 days.
- On 30/03/2024: The official project delivery date. However, the final work progress statement was not submitted.
- On 01/05/2024: The fourth and final phase was completed, representing 10% of the contract value, as per work progress statement No. 04, with 5% RG on the total including VAT. Payment to be made after 15 days.
  (*Note: The contract states that in case of late completion, a penalty of 1% per month will be applied to the value of the delayed work progress statement.*) On the same date, the provisional acceptance report was signed by both parties.
- On 01/05/2025: The final acceptance report was signed by both parties. The company recovered the retained guarantee amount (5%) after verifying proper execution and the release of the performance bond.

Required: Record all necessary accounting entries for the company (ETPE)

Solution:

- **Contract value (excluding VAT)** = 300,000,000 DZD

- **Value-added tax (VAT) for construction at 9%** = 27,000,000 DZD
- **Contract value including VAT** = 327,000,000 DZD

Debit	**Credit**	**Account Name**	**Debit Amount**	**Credit Amount**
		01/02/2021		
618		Documentation Expenses	25000	
	53	Cash		25000
		Purchase of the specifications booklet		
		05/02/2021		
617		Research and Studies Expenses	35000	
	53	Cash		35000
		Settlement of technical and financial offer expenses		
		08/02/2021		
467		Payables	15.000.000	
	512	Bank		15.000.000
		Deposit of bid bond amount		
		01/03/2021		
2752		Paid Deposits – Performance Guarantee	15.000.000	
	467	/Payables		15.000.000
		Reclassification of the nature of the guarantee		
		02/04/2021		

616 486	 512	Insurance Premiums (180,000 × 9/36) /Prepaid Expenses A/C (2022 + 2023 + 2024) /Bank A/C Civil liability insurance under the insurance contract	45000 135000	 180000
 512	 419	01/06/2021 Bank /Received Advances Receipt of advances for project commencement	 30.000.000	 30.000.000
 381 4456	 401	02/07/2021 Raw Materials Purchases Value Added Tax (VAT) /Goods and Services Supplier	 4.800.000 912.000	 5.712.000
31	 381	Raw Materials /Raw Materials Purchases Receipt of raw materials	4.800.000	 4.800.000
401	 512	Goods and Services Suppliers /Bank Payment of raw materials by bank cheque	5.712.000	 5.712.000
624	 53	Transportation Expenses /Cash Payment of transportation expenses in cash	35000	 35000
		25/09/2021		

631		Employee Expenses	1.450.000	
	431	/Social Security Fund (CNAS) 9%		130.500
	432	/CACOBATPH Fund 0.375%		543.750
	442	/Personal Income Tax (IRG)		190.000
	421	/Accrued Salaries		585.750
		Recording of September salaries		
		(This entry is repeated monthly if no changes occur)		
635		Social Security Contributions 26.13%	378.885	
637		Other Social Charges 12.585%	182.482,50	
	431	/Social Security Fund 26.13%		378.885
	432	/CACOBATPH Fund 12.585%		182.482,50
		Recognition of employer's contributions for the month of September		
431		Social Security Fund	509.385	
	512	Bank		509385
		Payment of social security contributions (9% + 26.13%)		
432		CACOBATPH Fund	187920	
	512	/Bank		187920
		Payment of CACOBATPH contributions (12.585% + 0.375%)		
421		Accrued Salaries	585750	
	512	Bank		585750
		Payment of employees' salaries		
		30/09/2021		

607 4456	 53	Non-Stockable Purchases /Recoverable Value Added Tax Cash Payment of water and electricity expenses	19500 3705	 23205
 611 4456	 4017 4013	01/11/2021 General Contracting (Subcontracting) Recoverable Value Added Tax /Suppliers – Retention /Service Suppliers Recording of the subcontractor's invoice	 7.000.000 1.263.500	 416.500 7.847.000
 4013	 512	01/12/2021 Service Suppliers /Bank Payment of subcontractor’s works invoice	 7.847.000	 7.847.000
 4111 4117	 704 445	31/12/2021 Clients (Public Administrations and Bodies Retention 5% /Works Sales Value Added Tax 9% Recording of Work Progress Statement No. 01	 46.597.500 2.452.500	 45.000.000 4.050.000
 512 419	 4111	15/01/2022 Bank Received Advances /Clients	 42.097.500 4.500.000	 46.597.500

		Work Progress Statement No. 01 Collection		
4111 4117	 704 445	31/12/2022 Clients (Public Administrations and Bodies) Retention 5% /Works Sales Value Added Tax 9% Recording of Work Progress Statement No. 02	139.792.500 7.357.500	 135.000.000 12.150.000
512 419	 411	15/01/2023 Bank Received Advances Clients Work Progress Statement No. 02 Collection	126.292.500 13.500.000	 139.792.500
4111 4117	 704 445	31/12/2023 Clients (Public Administrations and Bodies Retention 5% / Works Sales Value Added Tax 9% Recording of Work Progress Statement No. 03	93.195.000 4.905.000	 90.000.000 8.100.000
512		15/01/2024 Bank	84.195.000	

419	4111	Received Advances /Clients Collection of Work Progress Statement No. 03	9.000.000	93.195.000
4111 4117	 704 445	01/05/2024 Clients (Public Administrations and Bodies Retention 5% / Works Sales Value Added Tax 9% Recording of Work Progress Statement No. 04	30.065.000 1.635.000	 30.000.000 2.700.000
512 419 656	 4111	15/05/2024 Bank Received Advances Penalties for Delay /Clients Collection of Work Progress Statement No. 04	27.765.000 3.000.000 300.000	 31.065.000
512	4117	01/05/2025 Bank /Retention 5% Recovery of the 5% retention (300,000,000 × 1.09) × 0.05 = 16,350,000 DZD	16.350.000	16.350.000

512	2752	01/05/2025 Bank /Paid Deposits – Performance Guarantee Recovery of the performance guarantee	15.000.000	15.000.000

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