Chapter 2

PROBLEMS OF IMPLEMENTING INTERNATIONAL FINANCIAL REPORTING STANDARDS IN A TRANSITION ECONOMY: A CASE STUDY OF RUSSIA*

Abstract

International Financial Reporting Standards (IFRS) and their predecessor, International Accounting Standards (IAS) are gaining in worldwide recognition. All publicly traded companies in the EU must adopt them by 2005 and many other countries either have adopted them or plan to do so in the near future. In 2002, the Russian Prime Minister announced that all Russian companies and banks must prepare their financial statements in accordance with international standards starting January 1, 2004. Implementing that decision will not be easy, for a variety of reasons. Not all international standards have been translated into Russian. Many Russian accountants are not sufficiently familiar with international standards to implement them. Some Russian universities have only recently started teaching international standards and the continuing education programs of the various Russian accounting associations are not yet prepared to offer comprehensive courses on international standards. Current Russian accounting standards conflict with international standards in several important ways and these conflicts will not be resolved in the near future.

This paper reviews the literature on this subject and incorporates the results of interviews conducted of Russian accounting firms, enterprises and university professors in July and August 2003.

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INTRODUCTION

As transition economies go through the process of shedding their centrally planned accounting model and replacing it with a market oriented model that uses international standards they face a number of problems. Very few people know the new rules, since the international standards must first be translated into their language. Accountants who can read the international standards promulgated by the International Accounting Standards Board and its predecessor, the International Accounting Standards Committee in the original English have a competitive advantage in this regard, but trying to fully exploit this advantage may be frustrating if potential clients or employers do not place much value on international standards.

There is also an inertia barrier to overcome. It is difficult to change the status quo (Friedman & Friedman 1984). Accountants and managers who have been using the old system for 20 or 30 years do not want to change because they feel comfortable with the system they learned in school or on the job when they were young. Those individuals also happen to be the people who are now in charge of enterprises and accounting departments, so their approval must be had before any new system can be adopted and implemented.

A number of countries that have started this conversion process have experienced similar problems. No one knows the new rules but there is nowhere to go to take classes to learn the new rules because no one can be found to teach the new knowledge. Most universities do not have qualified professors and most accounting firms do not have anyone who has been trained in the new rules. Yet the governments in these countries often pass laws with deadlines, stating that the new rules must be adopted by some certain date.

What results when this happens is that the new rules cannot be implemented according to the government's schedule because nobody knows how to implement them. A new set of problems result from this top-down approach to accounting reform. Various ways have been tried to alleviate or solve the problems that result from adopting new accounting rules. Some have worked better than others. This paper examines the Russian case, which is still in the process of transformation.

REVIEW OF THE LITERATURE

Much has been written about International Accounting Standards (IAS), International Standards on Auditing (ISA), accounting harmonization, accounting education and accounting reform in transition economies in recent years. A few books and articles have focused on accounting reform in Russia.

The classic book in the sub field of accounting reform in Russia is by Enthoven et al (1998). This book discusses the Russian accounting system, management accounting, auditing, taxation and accounting education. A few years before that, Enthoven et al (1992) published a book on doing business in Russia and other former Soviet republics that dealt with accounting issues. This latter book was very popular among accounting practitioners who were doing business in the former Soviet Union, since it was one of the few major sources of accounting information on Russia at the time it was published.

Bailey (1982) published a long historical study of Russian accounting going back to the thirteenth century. Shama and McMahan (1990) discuss the historical development of accounting in Russia from Tsarist times to communism and also how perestroika will change the nature of accounting in Russia and other East European countries. Motyka (1990) discusses the impact of Western Europe on accounting development in tsarist Russia prior to 1800. Lebow and Tondkar (1986) discuss the development of accounting in the Soviet Union and its effectiveness. Two decades before that, Campbell (1963) published a book containing a series of essays on Soviet accounting problems. Campbell (1956) also did a long and detailed study of depreciation under the Soviet accounting system. Horwitz (1963) discusses some of the philosophical and historical literature on accounting in a socialist regime and focuses his attention on depreciation and cost.

An early study by Mills and Brown (1966) discusses how shifting from a production model to a profitability accounting model would help Soviet enterprise managers make decisions that would increase the efficiency of their firms and help them to better allocate resources. In a similar vein, Thornton (1983) discusses changes in the way the Soviets accounted for factor costs over a twenty-five year period. A study by Scott (1969) states that Soviet accounting after the 1965 reforms started to place more emphasis on enterprise profitability, which helped move the Soviet economy closer to a Western market model.

Other authors have also touched on this theme. Horwitz (1970) discussed the effect that decentralization has on the management accounting control system. Chastain (1982) described how the Soviet accounting system was not able to keep up with the needs of enterprise managers. He also assesses the implications of that inability for the accounting profession.

Gorlick has done several studies on the Soviet accounting system. In one study he discusses the historical development and problems of uniform accounting (1974a). In another he discusses planning and control (1974b). In an earlier study he discussed the difference in accounting measurements between the Soviet Union and the United States and the advantages and disadvantages of their profitability measurements (1971).

Richard (1998) wrote a book chapter that discussed communist accounting systems in Eastern Europe in general and in the Soviet Union in particular. Garrod and McLeay (1996) edited a book on accounting in transition economies, which provides a good introduction to many of the issues involved in attempting to convert the accounting system from a central planning model to a market model. One of the chapters in that book (Jaruga 1996) describes the changing accounting function in socialist countries, which is now mainly of historical interest.

Turk and Garrod (1996) discuss the lessons Slovenia learned when it began the process of changing to International Accounting Standards. The Slovenian experience is not unlike the Russian experience in many ways. Preobragenskaya and McGee did research on the relationship between IAS and foreign direct investment (FDI) in Russia (2003a) and on the state of auditing in Russia (2003b). Their FDI study concluded that the lack of credibility of Russian financial statements was hampering inflows of foreign capital. Their audit study found that the state of auditing in Russia is not yet up to western standards.

A few studies have been made on accounting education in Eastern Europe or the former Soviet Union. According to one scholar, Houghton Mifflin's 1300-page Principles of Accounting was the first Western accounting text sold in the Soviet Union (Collingwood 1991). It was translated and distributed by Finansy I Statistika, Moscow's government owned publisher. Kobrack and Feldman (1991) speculated whether the reform process in the Soviet economy could create a new market for accounting textbooks. McGee has written about educating accounting professors in Bosnia & Herzegovina (2003a) and reforming accounting education in Armenia (2003b).

There are several sources of information on recent developments in accounting reform in Russia. The International Center for Accounting Reform in Moscow [www.icar.ru/] publishes the *ICAR Newsletter.* The World Bank publishes *Transition Newsletter,* which gives current information about various aspects of market reforms in transition economies, including accounting reform in Russia. The Russian websites of the Big-Four accounting firms also have current information and, in some cases, publications.

The Deloitte & Touche Russian website has an e-library link that contains a variety of items on various aspects of doing business in Russia. It has a *Doing Business in Russia Online Guide,* which includes much information on accounting and tax topics. It has several newsletters that address accounting, tax and legislative issues on various countries, including Russia. *Russia - Legislative News* is a monthly newsletter that contains accounting and tax items. Legislative Tracking is a daily publication that keeps readers abreast of Russian pending legislation.

Ernst & Young publishes *An EYe on Russia,* a monthly newsletter on current business, accounting and tax issues. It also has a Russian Legislation website that contains downloadable documents on Russian accounting, tax and related legislation that have been translated into English.

The KPMG Russian website has several good publications, including *Doing Business in Russia* and *Russia – Tax Overview.* It also has the GAAP 2001 and 2002 studies.

The PricewaterhouseCoopers website has several publications pertaining to Russia, including *Doing Business in the Russian Federation* (2003). There are also a number of short articles by PWC partners and others on various aspects of accounting reform in Russia, including an excellent article by Leonid Schneidman (2003) on the long road to IAS adoption. The PWC site also has the GAAP reports for 2002, 2001 and 2000 available for downloading in several languages.

Some publications have compared the accounting standards in various countries to IAS. The most thorough study is GAAP 2001, a joint publication of several large international accounting firms, which makes comparisons for 62 countries, including Russia. Several of the Big-Four accounting firm websites have a link to this study. The International Forum of Accountancy Development website [www.ifad.net] has published this study in interactive format. There is also a *GAAP Comparison 2000* study that provides comparisons for 52 countries and a small 2002 update titled *GAAP 2002 Convergence* that provides data on 59 countries. Street (2002) has written a summary of the GAAP 2001 study.

The internet also has information on corporate governance in Russia. One good source is the Independent Directors Association website, which contains much up to date information on corporate governance in Russia. It publishes *Independent Director,* a quarterly review and has also published *The Code of Conduct of Independent Directors* and *The Independent Directors Association Charter,* both of which are published in the Spring 2003 issue. The Organisation for Economic Cooperation and Development (OECD) website also has current and relevant information on corporate governance in Russia. *The Russian Code of Corporate Conduct* can be accessed from several websites, including the Deloitte & Touche Russian website. The Corporate Governance Code can be obtained from the Russian Institute of Directors website [www.rid.ru].

METHODOLOGY

The first stage in the preparation of this paper was a thorough review of the literature on accounting reform in general and accounting reform in Russia and other transition economies in particular, with special attention being paid to the literature that discussed the adoption and implementation of IFRS. As the literature was being reviewed, the authors started compiling a tentative list of questions to ask Russian accounting experts on various aspects of accounting reform in Russia. This list was sent to the individuals to be interviewed several weeks prior to the interviews.

After the list of questions was compiled, the next step was to identify and contact individuals who were experts in some aspect of the present state of Russian accounting, which was done through a combination of website searches, telephone calls in both Russia and the United States and e-mail communications. It was difficult to contact some individuals, especially at Russian universities, because they were away on summer holiday. However, a sufficient number of experts with diverse backgrounds on various aspects of accounting reform in Russia were able to be contacted and interviewed to make the project worthwhile. Once experts were identified, initial contact was made and interviews were scheduled. On-site interviews took place during July and August 2003 in St. Petersburg, Moscow and Omsk. Telephone interviews were also conducted with individuals located in Washington, DC and Geneva, Switzerland. Individuals from the following institutions participated in the on-site interviews:

Deloitte & Touche, Moscow office [www.deloitte.ru]
KPMG, Moscow office [www.kpmg.ru]
KPMG, St. Petersburg office [www.kpmg.ru]
PricewaterhouseCoopers, Moscow office [www.pwcglobal.com/ru]
Ajour, a Russian auditing and consulting firm, Moscow [www.ajour.ru]
PKF (MKD), a Russian audit and consulting firm, St. Petersburg office [www.mcd-pkf.com]
Independent Directors Association, Moscow [www.independentdirector.ru]
MDM Group, Moscow [www.mdmgroup.ru]
St. Petersburg State Polytechnical University [www.spbstu.ru]
St. Petersburg State Railway University (a.k.a. Petersburg State Transport University) [www.pgups.ru]
Timiryazev Agricultural Academy, Moscow [www.timacad.ru]
Hock Accountancy Training, Moscow office [www.hocktraining.com]
Omsk State University [www.omsu.omskreg.ru]
Omsk State Institute of Service [www.omsk.net.ru/education/vuz/service/main.htm]

The information gathered from these interviews was combined with information that was already published and available. While much of the information gathered during the course of the interviews confirmed what the existing literature already said, much new information was gathered that filled in the gaps in the existing literature and extended and updated prior studies in several important ways.

PROBLEMS OF IMPLEMENTING INTERNATIONAL STANDARDS

Accounting in Russia

Accounting has a long history in Russia (Bailey 1982; Shama and McMahan 1990), going back at least to the thirteenth century, through the time of the tsars and through the communist era. The Russian accounting system started shifting away from the centrally planned, socialist model as early as the 1960s (Mills and Brown 1966; Scott 1969; Jaruga 1996; Thornton 1983). The pace accelerated with perestroika and the collapse of the Soviet Union, which began in the late 1980s. A critical year for Russian accounting was 1989. It was in that year that the Soviet government introduced legislation for joint ventures using foreign capital. This decision created a real need to modify the Russian accounting system and led to the introduction of new Western accounting concepts like audits, intangible assets, capital, etc.

Some scholars have gone on record as saying the reason for the collapse of the Soviet Union was because of the inability to allocate resources efficiently under a socialist accounting system (Sennholz 2002; Rothbard 1991). Ludwig von Mises, an Austrian scholar who later taught at New York University, predicted the collapse as early as the 1920s (Mises 1920; 1922; 1923; 1935). His prediction sparked the socialist calculation debate of the 1930s (Hayek 1935; Lange 1936; 1937; Lerner 1935; Lippincott 1938; Hoff 1981). Polanyi (1923) agreed with Mises that the problem of economic calculation is insoluble in a centrally planned economy but proposed to solve the problem by means of "a functionally organized socialist transition-economy."

Whatever the reason(s) for the collapse of the Soviet Union, there has been a worldwide movement on the part of formerly centrally planned economies to move away from the top-down, centrally planned accounting model and toward a bottom-up market model. Russia started to make the transition by deciding to adopt and implement international standards. Although Russia chose to adopt and implement international standards several years ago, there are still some glitches in the system.

Until recently, deducting the cost of an IAS audit was not allowed by the Russian tax code (Ermakova 2003), which took some of the incentive away from having such an audit. Russian accountants and auditors are not sufficiently well versed in international standards to implement them, with a few exceptions. There is a widespread perception on the part of accountants who work for the large international accounting firms that none of the Russian accounting firms, even the biggest ones, are able to provide high quality service regarding international standards. The large international accounting firms, mostly the Big-Four, have rushed in to fill the gap to provide the services and expertise that the local Russian firms cannot provide. This capturing of market share by the big firms has caused some resentment on the part of the smaller Russian firms. It has also given some Russian accounting firms an inferiority complex, since they know they do not have the resources or expertise to compete against the international firms. Russian accounting firms have lost some large clients to the Big-Four. However, some of their big clients later returned, partly because of cost considerations.

Russian accountants and auditors who were trained under the old system need to learn the new system and many of them have not. Some of them, especially the older ones, are actively resisting the change. Some Russian accountants and professors, even at the top, insist that they use or teach international standards, even though they have never read them. There is the widespread perception that Russian Accounting Standards (RAS) either are the same as the international standards or are just as good. In fact, there are major differences. RAS are more form over substance, whereas the international standards are more substance over form.

There is also the perception that international standards are not needed, either because the RAS are just as good as the international standards or because there is no demand for international standards. There is a grain of truth to the lack of demand argument. Until a few years ago, the only reason most firms prepared financial statements was to provide information to the tax authorities. Some firms still prepare financial statements just for the tax authorities. However, the trend now is away from having a monopsony (single user) of accounting information, especially with the large Russian firms, since they need to go to the international capital markets for funds to expand or stay afloat. Foreign investors demand to see financial statements prepared using either IFRS or U.S. GAAP as a condition of talking seriously about investing in a Russian company.

It would not be an overstatement to say that companies prepare statements using either IFRS or U.S. GAAP only because they need to in order to obtain a listing on some foreign stock exchange or because their creditors or investors demand it. The demand for such statements is therefore limited, especially when companies prepare such statements at the consolidated level. It is typical that subsidiaries prepare statements based on RAS and that GAAP adjustments are made at the top, even though the people who provide the information used for consolidation are further down the organization and know nothing about GAAP principles. Top corporate managers seldom use consolidated information for management decision making purposes, since such information has no value to them. This valuelessness of IFRS or U.S. GAAP consolidated financial statements is especially true for tax managers, since they use only the RAS statements for computing the company's tax liability.

Although the trend is to place more emphasis on the needs of shareholders and potential investors and less on the needs of tax authorities, not all Russian accountants and managers feel this way. Most accountants who work for the big international accounting firms, and many of their clients, now recognize the goal of financial statements is to provide information to shareholders, not the tax authorities. This change in attitude and perception started to take place around 1999 or 2000.

This change in attitude has not yet filtered down to the smaller firms and enterprises. Although the big accounting firms and an increasing number of large enterprises now recognize that the main audience for the financial statements they prepare are shareholders, the smaller Russian companies still think that accounting information is only for the tax authorities. Some CEOs at larger companies still think this way.

This attitude is reinforced by the Russian tax authorities themselves, who often could not care less to see any financial statements based on international standards. The Russian tax rules are different from IFRS, so why bother to look at financial statements that are prepared using IFRS? They want to look only at statements prepared using RAS. One of the partners interviewed at one of the international accounting firms said he was tired of having to sign off on two sets of financial statements, one based on RAS and one based on either IFRS or U.S. GAAP. He longed for the day when he would need to sign off on only one set of statements. He also confided that such a day is likely far off, since statutory accounting still requires the use of RAS and this rule is unlikely to change any time soon.

Not all Russian enterprises that are trying to attract foreign capital are using IFRS. Some of them are using U.S. GAAP. One of the deciding factors that enters into the decision to use one or the other set of internationally recognized financial reporting standards has to do with which capital market the enterprise wants to tap into. If they are targeting the United States capital market, they often decide to use U.S. GAAP. Those who decide to tap into the European capital market often choose IFRS. Russian enterprises used to prefer U.S. GAAP to IFRS because they wanted to list their shares in New York. The trend is now toward IFRS because of the Enron and Arthur Andersen scandals. However, not all firms are shifting to IFRS. The subsidiaries of the many U.S. firms in Russia prefer GAAP, so it appears that there will be a need for GAAP-trained accountants for the foreseeable future.

The interviews revealed that there is a bit of standards shopping going on on the part of some Russian enterprises. In one case, an enterprise would have had a multimillion deferred tax liability using one set of standards, whereas their tax liability using the other set of standards would have been zero. One set of rules would have treated the book tax difference as a permanent difference whereas the other standards would have treated the difference as a timing difference, and thus subject to deferral. Not surprisingly, the enterprise chose to use the set of standards that did not result in a tax liability.

Some Russian audit firms will agree to sign anything, including an audit report, lest they lose a client. Or at least that is the perception. Unfortunately, there may be some truth to this perception. Russian business culture is different than Western business culture in this respect. Three generations of communist governments and the accompanying corruption that went with it have made people cynical. Many people simply do not believe that financial statements signed by a Russian audit firm are as credible as statements signed by a Western audit firm (Rozhnova 2000).

One solution to this dilemma would be to establish a strong private sector accounting organization like the American Institute of Certified Public Accountants (AICPA) or one of its British counterparts that is capable of policing its members and giving much needed moral support to the Russian audit firms that do not want to give into the pressure to sign audit opinions when financial statements are not of sufficiently high quality. This solution was proposed both by the Russian firms that were interviewed and by some members of the Big-Four. Unfortunately, no such private sector accounting organization currently exists and none are on the horizon. There are a number of small, politically weak accounting organizations, but they do not have the authority, power or incentive to do the policing job or to provide the moral authority needed to support the honest Russian audit firms that want to do the right thing.

It is encouraging that Russian accountants have identified the problem and have a good idea of where the solution might lie. The next step is to find a way to achieve the desired result. That will not be easy, at least for the immediate future, since the Russian accounting profession, in the Western sense of that term, is in its infancy stage. There is no recent history of private sector institution building in Russia and the other former communist countries. The only institution was the State, and in some cases, the church. Private sector institutions will need to be created and grow in size and strength, and that process will take time, perhaps a generation or more. One individual from a Big-4 accounting firm expressed pessimism about the possibility of a strong and independent accounting association coming into existence in the near future. He did not think it was realistic to expect such an independent organization to be established and function in Russia because it is against the Russian management culture to have such organizations.

Some of the individuals interviewed pointed out that part of the problem is that the professional accounting organizations that do exist have a bias in favor of the status quo. So do Russian bureaucrats. Milton Friedman discussed this inertia problem in theoretical terms several years ago

(Friedman and Friedman 1984). One of the interviewees said that these people do not know anything about international standards, that they do not have the required skills and that changing to international standards could put them out of a job.

Outside help is available for strengthening these private sector accounting associations. George Soros and his various foundations have recognized the need to build and strengthen private institutions and have allocated millions of dollars toward this goal. The various USAID and Tacis accounting reform projects include an institution building component in their projects. The problem with some of these institution building projects is that they turn out to be top-down. The local accountants and existing accounting organizations need to be convinced that they need to build such institutions. The institution building process would go faster and smoother and would be more successful if the process were demand driven, with the demand emanating from the grass roots rather than from some international organization that offers to drop money and consultants on the problem.

Another structural problem with Russian accounting is the Russian mindset. Under the old centrally planned system, accountants were really bookkeepers. They didn't have to make decisions. Their job was just to make journal entries. There was no such thing as exercising professional judgment. Where a decision had to be made, their solution was to look for some rule that told them what to do. The new rules, whether IFRS or GAAP, require the exercise of professional judgment and many Russian accountants do not feel comfortable making decisions on their own. They would prefer to find some rule in a book that instructs them on how to do everything and they resist adopting the new rules. This structural bump in the road to the adoption and implementation of market based accounting rules will be worn down with time, but it will take perhaps a generation or more before Russian accountants think the same way as Western accountants in regard to this approach to decision making.

Several government ministries are involved in accounting reform. Unfortunately, they do not always think the same way. In fact, their approaches to accounting reform are drastically different. The Ministry of Economic Development and Trade is strong on policy formation but does not have much power over policy implementation. Its approach is bottom-up. The Finance Ministry, on the other hand, prefers a top-down approach, similar in structure to the old centrally planned Soviet system. Westerners feel more comfortable dealing with the Ministry of Economic Development and Trade, since Western accountants also prefer a bottom-up approach.

However, these two ministries are not the only government agencies that are involved in accounting reform. The Russian Securities Commission and the Central Bank also play a role. In 2002 the Association of Russian Entrepreneurs also became involved in accounting reform. But no one is in charge. There is no leadership. There is no central direction to accounting reform. It is almost like all of these institutions are groping in the dark. While some government ministries demonstrate an interest in accounting reform, they are unable to answer questions because of a lack of expertise.

There is no force driving accounting reform, from an organizational perspective. No organization wants to protect both accounting and the public interest. The pressure to reform accounting in Russia is coming from the market. Russian enterprises that want to raise capital, either by debt or equity financing, need to have statements prepared either according to IFRS or GAAP. Potential investors demand it. That is the factor that is causing the change, not some government bureaucracy that dictates policy and rules from on high.

Most of the largest companies, like Gasprom, Aeroflot, metallurgical plants, electricity plants, etc., including 80 percent of the biggest companies and 95 percent of banks prepare financial statements based either on IFRS or U.S. GAAP. The real driver of accounting reform is the large companies. They are doing it in spite of government inaction. The market is solving the problem without government.

International Standards in Russia

Accounting is part of the legislative system. That is a problem because Russia will never have true international standards if government has to legislate it. There will always be a lag and style and language problems. The original plan by the Russian Finance Ministry in 1998 was to adopt all IAS by 2000. That did not happen. The new target for full adoption and implementation was 2004, at least in the case of banks and publicly traded companies. However, that target is also has not been met. In fact, not a single accountant interviewed thought that international standards would be fully adopted and implemented by 2004. One accountant estimated that full implementation would take ten years.

Even though Russia is in the process of adopting international standards, it has not adopted all of the international accounting standards, and it has no immediate plans to adopt the standards it has not already adopted. It has not adopted the standards on impairment, financial instruments or hyperinflation. There are good reasons for not adopting each of these standards.

In the case of the standard on impairment, many Russian companies and their accountants do not want to apply the impairment rules because many companies have assets that are overvalued. Applying the impairment standard would cause the asset side of the balance sheet to shrink, considerably in many cases, and they do not want that to happen. In extreme cases, a company that appears healthy could appear to be insolvent if the impairment rules were applied. This hesitancy is not unique to Russia. The same situation exists in Republika Srpska, the Serbian part of Bosnia, and in other formerly centrally planned economies.

Perhaps the main reason why the standard on financial instruments has not been adopted is lack of demand. Very few Russian enterprises use complex financial instruments, and the ones that do are already applying the IFRS or U.S. GAAP on this topic. Also, this standard is difficult to understand and many Russian accountants are not eager to make the effort to learn a standard that they probably will not use in the foreseeable future.

The standard on hyperinflation is not needed, or at least that is the perception of many Russian accountants, because Russia's inflation rate has fallen below the threshold needed to trigger the hyperinflation standard. Russia's cumulative inflation over the most recent three years (2001-2003) has been about 90 percent, and the threshold for using the hyperinflation standard is 100 percent. But the 100 percent test is only one of five items on the IFRS list of possibilities. To be more compliant with IFRS it is necessary to look not only at quantitative factors but also qualitative factors. For example, Russian companies do their planning in dollars, not rubles. If the ruble is not being used to make management decisions, a strong argument can be made that the hyperinflation accounting rules should be used even if the inflation rate does not hit the 100 percent minimum threshold.

Another point that could be made about Russia's adoption of international standards is that even the standards that have been adopted may not always be international standards. For example, the Russian standard on income taxes is based on the old version of the IAS income tax standard, not the new one. This fact is known within much of the Russian accounting community but may not be as well known outside of Russia. Another, less well known fact about Russia's accounting standards is that the Russian version of the standards that have been adopted are not mere translations of the English language originals. In many cases they are abbreviated, simplified versions of the original English language IAS. RAS tend to be much shorter, more detailed and conceptual. They cover a fraction of the content of IAS. In short, it may not be accurate to state that Russia has adopted IFRS. It would be more descriptive to say that Russian accounting standards are merely based on IFRS. Often the differences between RAS and IFRS are not large or important. However, the difference may be substantial, such as in the area of accruals principles.

Many studies have been made that compare RAS to IAS, or that list the Russian accounting standards that are on the same topics as the IAS. The GAAP 2000 and GAAP 2001 studies are perhaps the most famous and most accessible, since they were done by reputable firms and since they are available on the internet in several languages. PricewaterhouseCoopers updated the GAAP 2001 study in its *Doing Business in the Russian Federation* publication (2003). A summary of that update is shown in Table 1. This table compares the rules that were in force on March 15, 2003.

Table 1
Differences between Russian Accounting Standards and International Accounting Standards

Russian accounting may differ from that required by IAS because of the absence of specific Russian rules on recognition and measurement in the following areas:	
- the classification of business combinations between acquisitions and unitings of interest	IAS 22.8
- provisions in the context of business combinations accounted for as acquisitions	IAS 22.31
- consolidation of special purpose entities	SIC 12
- the restatement of financial statements of a company reporting in the currency of a hyperinflationary economy in terms of the measuring unit current as of the balance sheet date	IAS 29.8
- the translation of the financial statements of hyperinflationary subsidiaries	IAS 21.36
- the treatment of accumulated deferred exchange differences on disposal of a foreign entity	IAS 21.37
- derecognition of financial assets	IAS 39.35
- the recognition of operating lease incentives	IAS 17.25; SIC 15
- accounting for defined benefit pension plans and some other types of employee benefits	IAS 19.52
- accounting for an issuer's financial instruments	IAS 32.18/23
- hedge accounting for derivatives	IAS 39.142
- the treatment of exchange differences resulting from severe devaluation or depreciation of a currency	IAS 21.21; SIC 11
There are no specific rules requiring disclosures of:	
- a primary statement of changes in equity	IAS 1.7
- a primary statement of cash flows; and the notion and definition of cash equivalents, and detailed guidance on the preparation of cash flow statements	IAS 7
- the FIFO or current cost of inventories valued on a LIFO basis	IAS 2.36
- the fair values of financial assets and liabilities	IAS 32.77
- the fair values of investment properties	IAS 40.69
- related parties information except by certain reporting companies with a specific legal form (joint stock companies); the definition of a related party is a narrower one, based on legislation	IAS 24.1-4
- certain segment information (e.g. a reconciliation between the information by reportable segment and the aggregated information in financial statements, significant non-cash expenses, other than depreciation and amortization, that were included in segment expense and, therefore, deducted in measuring segment result – for each reportable segment)	IAS 14.61/67

There are inconsistencies between Russian rules and IAS that could lead to differences for many enterprises in certain areas. Under Russian rules:	
- goodwill is calculated by reference to the book values of acquired net assets	IAS 22.40
- proportionate consolidation may be used for subsidiaries in which the parent has 50 percent or less of the voting power	IAS 27.15
- revaluation of property, plant and equipment is allowed but gives different results than IAS and need not be kept up-to-date	IAS 16.29
- the useful life of property, plant and equipment is usually determined using periods prescribed by the government for tax purposes, which are longer than those for which the assets are expected to be used, but in practice the management of a company sets the periods in the accounting policy	IAS 16.6/41
- if investment properties are revalued, they are still depreciated	IAS 40.27
- if investment properties are revalued, the gains and losses are not required to be taken to the income statement	IAS 40.28
- finance leases are generally defined in legal terms and the right of capitalization is given to a lessor or a lessee by the Contract	IAS 17.3/12.28
- lessors recognize finance lease income differently	IAS 17.30
- the completed contract method can be used for the recognition of revenues on construction contracts when the outcome of a construction contract can be estimated reliably	IAS 11.22
- trading, available-for-sale and derivative financial assets are not recognized at fair value	IAS 39.69
- trading and derivative liabilities are not recognized at fair value	IAS 39.93
- any financial investments are not required to be carried at fair value	IAS 39
- provisions can be established more widely or less widely than under IAS, and there is no requirement for discounting	IAS 37.14/45
- own (treasury) shares are shown as assets	SIC 16
- classification of cash flows between investing and financing activities in the cash flow statement may be different from IAS	IAS 7.6/16/17
- cash flow statements reconcile to cash rather than to cash and cash equivalents	IAS 7.45
- the correction of fundamental errors is included in the determination of the net profit or loss for the reporting period, but separate disclosure and pro-forma restated comparative information are not required	IAS 8.34/38
- revenue recognition rules do not differentiate between exchanges of goods of similar nature and value and exchanges of dissimilar goods, and do not discuss adjustment for the amount of cash or cash equivalents transferred in exchanges for dissimilar goods	IAS 18.12; IAS 16.21/22
- the definition of extraordinary items is broader	IAS 8.6/12
In certain enterprises, these other issues could lead to differences from IAS:	
- some parent companies do not prepare consolidated financial statements	IAS 27.7/11
- in the definition of control, it is not required that the ability to govern decision-making be accompanied by the objective of obtaining benefits from the entity's activities	IAS 27.6
- certain subsidiaries may be excluded from consolidation beyond those referred to in IAS	IAS 27.13

- a subsidiary that is a bank may be excluded from consolidation if it is dissimilar from the rest of the group	IAS 27.14
- certain set-up costs that have been paid by a company's founder can be capitalized	IAS 38.57
- internally generated brands and similar items can be capitalized if the enterprise has an exclusive legal right	IAS 38.51
- inventories are generally carried at cost rather than at the lower of cost and net realizable value; this is often not an important difference because of inflation	IAS 2.6
- the realizable value of inventories can be measured without deduction of selling costs	IAS 2.6
- certain overheads in addition to those related to production can be capitalized	IAS 2.7

Source: PricewaterhouseCoopers: Doing Business in the Russian Federation (2003)

These studies list the differences between RAS and IAS. The problem with these lists, which is not revealed in any of these publications but was discovered during the course of the interviews, is that these compiled lists of differences do not include mention of any RAS that is an abbreviated, simplified version of the English language IAS. For example, if the English version of IAS 99 is 80 pages long and the RAS on that topic is 10 pages long, IAS 99 is not included in the list of differences, even though the Russian standard is clearly not identical to the international standard. Thus, these comparative lists are deceptive because they do not reflect the true and total differences between RAS and IAS. The list is relatively short, and many items on the list are for items that are inconsequential, leading an unsophisticated reader to believe that the differences between RAS and IAS are small, when in fact the differences can be quite large for certain standards. It was pointed out during the interviews that there are really no detailed comparisons between IAS and RAS but only the superficial kind of comparisons like the one above.

Another problem with making comparisons between RAS and IAS or U.S. GAAP is historical. IAS has a historical base. International standards are based on more than 100 years of Anglo accounting evolution. Because of that, much is understood but not stated. The Russian accounting system has no such long history. So making such lists and comparisons is dangerous, in the sense that it can be misleading.

There are differences of interpretation and emphasis even within the Western market economies that have adopted IFRS or some similar set of rules. For example, a German accountant and a British accountant could interpret the same rule differently for cultural reasons. Germans are more conservative and would tend to make provisions that British accountants might not make. Germans provide for everything; British and Russian accountants provide for fewer things.

Some of the individuals interviewed stressed the point that RAS will never be identical to the international standards. They will never be a mere translation, even if every word in every international standard is translated directly into Russian. That is because Russian culture and Russian thought processes come into play. The way Russian accountants interpret the rules will always be different than the way an English accountant will interpret the language contained in the various international standards. One Russian accounting executive who worked for a Big-Four accounting firm emphasized that the problem is with interpretation, not with the translation itself, although the translation creates some complicated problems such as terminology, etc.

One reason for the differing interpretations is because of conflicts in definitions. IAS contains definitions for a great many terms. So does the Russian Civil Code. But the Civil Code definitions are often different from the IAS definitions. What is a Russian accountant to do when confronted with these differences? These differences have caused arguments with clients in the past. These definitional problems will not go away in the near future if for no other reason than because the Russian Duma (Parliament) has more important things to do than expend a lot of effort harmonizing accounting definitions with the already existing Civil Code definitions. This problem would be nonexistent if the accounting rules were formulated in the private sector, but they are not. When this possibility was mentioned to one of the partners of a Big-Four accounting firm in Russia, his reply was that he did not believe that having the private sector harmonize definitions would be better than having the Duma do it. Then, rather cynically, he added that the Duma is very much an extension of the private sector.

Another reason why RAS will never be identical to the international standards is because there is a timing lag between the time a new international standard is issued in the UK and the time that new standard is translated into Russian and adopted as part of the Russian accounting rules. This lag could be overcome if the Russian Duma made it a rule that all new international accounting standards will automatically and immediately become part of the Russian rules. However, the Duma will never make such a rule, for reasons of national pride and sovereignty. So the lag will be permanent, even though there is a theoretical solution that would correct this lag.

The degree to which the Russian accounting community understands the international standards depends on several factors. The Russian translation of the original English version of the standards was not available until late 1998. The translation was mediocre, in some respects. Part of the problem was because there were no Russian terms to convey some of the concepts. In other cases, the Russian translators simply used the wrong word or said things in such a way as to make the sentence or phrase unintelligible. In at least one case, the translator left out the word “not,” with the result that the Russian version of the standard instructed the reader to do something, when in fact the

English version of the rule said *not* to do something. These kinds of mistakes and imperfections are to be expected the first time a technical document is translated, especially in cases where no terms exist for some of the words and ideas that need to be translated.

The Russian accountants who cannot read English are limited to reading the Russian translation of the international standards. That places them at a competitive disadvantage, for the reasons mentioned above. The Russian translation is mediocre in some places and in other places is downright incorrect. The Russian speaking accountant has no way of knowing how accurate the reading of a particular sentence or paragraph might be, but must rely on what is written because there is no other alternative. Russian accountants who were educated in a university that did not teach the international standards have a problem reading the international standards in any language because the standards contain concepts that the Russian accountant was never exposed to during the years at the university. Such accountants must learn the new rules as best they can, either by self-study or by attending some lectures or seminars on the various topics.

The interviews revealed that the Big-Four accounting firms have found a way around this translation problem, which gives them another competitive advantage over the local Russian firms. The Big-Four have a tendency to hire people who speak English, and at least one of the Big-Four will not hire anyone who does not speak, read and write English. The accountants who work for these firms refer to the original English version of the international standards and do not even read the Russian version, except perhaps as a secondary reference. Thus, they avoid all of the problems that are inherent in relying on the Russian translation.

Another advantage that the Big-Four firms have over their Russian-only brethren is the materials on international standards their various affiliate firms have developed over the years. The Big-Four branches in the United States, the UK and elsewhere have, over the years, developed a great deal of reading materials and some case studies that address many of the questions and problems that pop up when accountants try to apply the international standards. These materials are available to the employees of the accounting firm and also to their clients. The Big-Four firms also have regularly scheduled educational programs for their employees and clients, whereas the other Russian firms may or may not have such programs.

This wealth of educational material gives the Big-Four accounting firms an additional advantage over their Russian competitors. They can offer their clients an education that most Russian accounting firms cannot compete with. Much of the client training they provide is free. The training that they do charge for is offered at a very reasonable price. One reason for the low price is because many Russian enterprises cannot afford to pay New York or London prices. Another reason has to do with Russian culture. Russians are accustomed to getting free education. They do not see the need to pay high prices for education. This attitude affects the ability of the large accounting firms to charge a price that is high enough to meet their costs.

Another problem with the implementation of international standards that the interviews revealed is that the Russian accounting community operates as a two-tier system. The accountants who work in Moscow, St. Petersburg and a few of the other large cities are more knowledgeable about the international standards than the accountants who do not work in the large metropolitan centers. The big city accountants have more and better access to accounting materials and courses that will help them to keep current with recent developments, or even to become familiar with the basics of IAS. Accountants in the outlying regions do not have this kind of resource at their disposal. Perhaps they have internet access, which would enable them to tap into some pertinent information that is available on the net, but even internet access is not as good outside of the big cities as it is within them and it is expensive by Russian standards. However, much of the information available on the internet is useless if the accountant cannot read English, since there is much information available in English that is not available in Russian. Also, the Big-Four accounting firms do not have offices in the smaller Russian cities, so the infrastructure they carried with them to Moscow and St. Petersburg is almost totally absent outside of those two cities.

Another reason why the accountants in the outlying regions are not as knowledgeable about international standards as are the big city accountants is due to differences in demand. Most clients that need statements prepared according to international standards are in Moscow or St. Petersburg. A few big enterprises are scattered around other parts of Russia, mostly in the bigger cities. The accountants who service smaller clients have little or no need to know the international standards, so they do not take the time to learn them. The result is a two-tier system where the accountants and the employees who work for their clients in Moscow or St. Petersburg know at least something about international standards, whereas their counterparts in the outlying regions know less, or perhaps nothing about international standards.

This situation is unlikely to change soon. Some accountants, and even university professors who live in the regions have never seen the Russian translation of IAS and have not seen any Russian accounting books that discuss IAS.

The drive to adopt and implement international standards is coming more from the market than from the Russian government. Although the government is pushing for adoption and implementation of international standards, the force that is really motivating Russian enterprises to use international standards is the carrot of foreign capital. Foreign investors simply refuse to consider making loans or investing in a Russian company that does not prepare its financial statements using either IFRS or GAAP.

Russian enterprises are also under pressure from the international investing community to have their statements audited by a large foreign audit firm such as one of the Big-Four. So the process of adopting and implementing international standards is more of a bottom-up system than a top-down system. The market is causing the changes to be made where they need to be made and it is doing it faster and better than what could be accomplished by mere government decrees.

Another interesting facet of Russian accounting that the interviews revealed was how Russian accounting firms and enterprises are dealing with the new disclosure requirements. IFRS and GAAP both require much more disclosure than what Russians are accustomed to providing. Many Russian executives and accountants feel uncomfortable providing so much disclosure. Russian culture, even before the communist era, produced a closed mouth society, at least as far as revealing information to bureaucrats, government officials and the general public was concerned (Figes 2002).

Disclosure is new to the Russians and some of them do not know how to deal with it. Financial statement disclosure is sometimes more detailed than in the West, but the quality is often lower. Russian accountants tend to disclose information that has little or no value. They sometimes report extraneous information because they do not understand what is relevant for disclosure purposes. They do not always know what information is important to potential foreign investors, so they report what they are most familiar with. They provide financial statement ratios, disclose the number of employees, and so forth but sometimes leave out information that foreign investors might want to know. Some Russian financial statements are flooded with information that is of little or no use for investment decision making purposes.

Corporate Governance in Russia

As Russian firms became privatized, they went to foreign capital markets in search of investment capital. Their initial attempts at raising investment capital were extremely difficult, for a variety of reasons, some of which had to do with the accounting methods they used (Preobragenskaya and McGee 2003a). In the early stages of transition, the vast majority of Russian firms used Russian accounting standards to prepare their financial statements. That made sense when Russia was using the centralized, socialist accounting model, but western investors were not familiar with RAS and did not trust them. The main function of RAS was to provide information to the government under the old centralized system and to tax authorities under the new market system. But foreign investors require a much different focus. They are more interested in profits, disclosure and transparency. RAS did not provide sufficient information in a format that foreign investors needed, which made it very difficult for Russian firms to obtain the foreign capital they needed.

The Russian firms that wanted to raise foreign capital started issuing two sets of financial statements, one based on RAS and the other based either on IFRS or on U.S. GAAP, depending on which capital market they targeted. This dual set of financial statements presented several problems. For one, the cost of preparing two sets of financial statements greatly increased the cost of preparing financial statements. Firms could not issue just IFRS or GAAP based statements because the law and the tax authorities required RAS based statements.

Another problem they encountered was increased confusion on the part of financial statement readers. Potential investors and creditors were confronted with two different sets of financial data. Which set could they rely on? Profits, assets and a number of other items differed between the RAS based statements and the IFRS or GAAP based statements. Financial statement readers in the United States faced a similar dilemma when FASB 33 was issued in the late 1970s. That Statement required some firms to provide a full set of regular financial statements as well as supplementary statements using two different kinds of inflation accounting. The result was three different valuations for assets, which led to confusion within the accounting community.

Auditing such financial statements was another obstacle to obtaining the needed capital. Practically none of the Russian audit firms knew or used International Standards on Auditing (ISA) when they performed their audits (Preobragenskaya and McGee 2003b). The only audit firms able to perform such audits were foreign firms, mostly the Big-Five (now four) accounting firms and a few second-tier firms that were able to gain a foothold in the Russian market. This lack of ISA audits is complicated by the fact that many chief corporate accountants want an audit to be a tax audit, which is what many (but not all) audits of local companies really are.

There is also a problem of transparency, or the lack of it. A survey conducted by PricewaterhouseCoopers of transparency in 35 countries ranked Russia number 34, just ahead of China (Haigh 2001). With such a lack of transparency it is little wonder why Russian firms find it so difficult to raise foreign capital. Russia is attempting to overcome this problem by instituting good corporate governance principles such as the appointment of independent directors, establishing audit committees and insisting on more financial disclosure. However, it should be pointed out that transparency is not the only thing that drives foreign direct investment (FDI). If that were the case, Russia would be receiving more FDI than China, which is clearly not the case. Transparency is an important factor in attracting FDI, but other factors also need to be considered.

A number of detailed publications on corporate governance in Russia have been issued in recent years. One of the most frequently referred to publications is the OECD *White Paper on Corporate Governance in Russia* (2002). This publication provides detailed guidance on a number of corporate governance topics, including shareholder rights, the role of stakeholders in corporate governance, disclosure and transparency, the responsibilities of the board, and implementation and enforcement. The appendices also contain useful information on the relevant organizations and corporate governance initiatives in Russia between 1999 and 2001 and the Russian regulatory acts on corporate governance.

Upgrading Accounting Education

Part of the problem with accounting education in Russia is the perception by some bureaucrats, practitioners and educators that there is no need to upgrade accounting education. That is a stumbling block to change, since the first step in implementing any change is the recognition that change is needed. Some members of the accounting establishment in Russia have not yet reached this initial stage. The speed with which accounting education is upgraded is slowed as a result. However, the number of individuals who hold this view is decreasing with each passing year.

The people who called themselves accountants under the old Soviet system were actually bookkeepers, since practically all they did was make journal entries. In fact, there was no Russian word for accountant. They borrowed the German word for bookkeeper. Accountants were held in low esteem before 1990. Accounting was not a prestigious profession. Enthoven et al (1998) report that secondary school graduates ranked accounting 91st out of 92 occupations in terms of desirability. Changes started occurring in accounting education in 1989, but very few people were able to teach the new accounting. That is still the case, according to some of the individuals interviewed.

Another problem with upgrading accounting education is the lack of high quality educational materials. When Russia first started converting from a centralized reporting system based on a socialist model to a more decentralized market model, practically no educational materials on international standards or GAAP existed in the Russian language. The main reason for such lack of materials was because there was no need. All firms were state owned and all accounting rules and regulations were issued directly from Moscow. Even as this paper is being written not much IFRS or GAAP educational materials are available to university students in Russia.

The demand for market model accounting educational materials increased rapidly as the Russian government decided to switch to a market economic model. As state owned firms began to be privatized, they started adopting market oriented accounting models. The big firms were the first to make the changes, as they needed financial statements based either on IFRS or GAAP in order to convince foreign investors to invest in their companies.

Russian universities sometimes offered accounting courses, but when they did, it was as part of the economics faculty. There were no departments specifically devoted just to accounting at many universities, although some universities did offer accounting within a special accounting department. That is changing. Universities that never offered accounting before are now offering whole accounting programs. Some universities offer four-year programs and others offer five-year programs. Universities are trying to meet the demand for accounting by offering more courses. One constraint on offering courses to meet the demand is the difficulty of finding people to teach the courses. This problem is being solved by hiring practitioners to teach some of the courses. The Institute of Professional Accountants also runs courses to train professors in the new rules, which helps to upgrade the skills of existing professors and also increase the pool of qualified accounting professors.

Another problem Russian universities face is inertia. Most of the top professors who teach accounting are experts in the old Soviet accounting system. They have accumulated a vast knowledge of the old system and have long ago memorized the Soviet chart of accounts that all enterprises had to use to keep their books. But they need to teach the new accounting and many of them have not had any experience actually working as accountants in the new system.

Moscow State University, perhaps the best university in Russia, has very few accounting professors who are under 45 years old. The head of the accounting department is in his 70s. Perhaps these professors know the new accounting rules and methods, but if they do, it is because they learned by reading on their own and by consulting. They cannot merely parrot what they learned when they attended the university 20 or 50 years ago because the material they need to teach students today was not taught when they were students.

The interviews brought out some other interesting tid bits about university accounting education. While the professors and university administrators that were interviewed thought that the professors at their universities and in Russia in general were well qualified and up to date on the new accounting rules, the practitioners who took their courses felt differently. They felt that professors were not sufficiently trained in IFRS and that there were not enough professors to teach accounting in the universities.

The interviews also revealed that not all universities are restructuring their accounting course offerings at the same rate of speed. The universities that do the best job of teaching the new accounting are the entrepreneurial universities. There are some universities in Russia that make every effort to offer the courses demanded by the market, even though they are government institutions. As government financial support for university education is cut back, some universities are bridging the financial gap by offering a range of accounting courses and charging for them. These are the universities that offer the best programs, while other, more traditional universities are content to implement changes to their curriculum at a much slower speed.

Some of the professors who were interviewed revealed that university accounting courses are still based on RAS rather than international standards. Courses offered on the international standards explain only general concepts. One professor made the suggestion that the international standards should become the base for the entire accounting curriculum.

The course materials that Russian university students have leave something to be desired. According to one professor, there are only two books available on IAS in Russian, and neither of them is of high quality. Many Western textbooks have been translated into Russian, but some of the translations are not good and most of the books are at least one, and perhaps as many as three editions behind their English language counterparts. For example, the Russian language text may be the fourth edition, with a 1994 copyright date, whereas the same book is now available in the seventh edition in English with a 2003 copyright date.

Another problem Russian students face is the ability to get their hands on actual textbooks. Many Russian students cannot afford to buy their own copy, so they must use library copies. In some cases, this problem is alleviated by subsidizing the cost of printing the texts, but occasional subsidies are not sufficient to place books in the hands of every Russian accounting student. One of the accounting professors interviewed pointed out that the professors give students a sufficient number of handouts during class to make up for the lack of textbooks, and that these handouts are the main source of materials for exams. So perhaps the lack of textbooks is not such a big problem, assuming that the materials the professors distribute in class are of the same or higher quality than the textbooks.

The quality of accounting education is higher in Moscow and St. Petersburg than in other Russian cities for several reasons. For one, most professors outside of these two cities do not have much opportunity to practice. They just read books. Having practical experience is considered to enhance their classroom skills.

Another reason for the higher quality of education in Moscow and St. Petersburg is because the universities in the regions cannot afford to subsidize the textbook purchases of their students and their libraries cannot afford to buy a sufficient number of texts. Also, the demand for accounting professionals is less outside of the two big Russian cities, so fewer resources are used to train accounting experts. The attitude toward the accounting profession is also different in the regions. The demand for high quality is mostly in the big cities. Where the demand for high quality is low, the quality of service provided will also likely be low.

Accounting education in Russia is also being provided by several different private groups. The large international accounting firms give regular training to their staffs and also give training and seminars to their clients. Russian accounting firms also provide training to their staffs, and sometimes to their clients, but the interviews revealed that that quality of the education the smaller Russian firms provide is not at the same quality level as that provided by the big international firms.

One reason for the qualitative difference is because the large international firms have more resources to draw on than do the smaller Russian firms. The large international firms have been training their staffs and clients in international standards, modern auditing techniques and procedures for a much longer time and their various offices all over the world have developed and fine tuned their educational materials. A firm in New York or Sydney might very well develop a course or manual that can be adapted for use in Russia. The large firms have a large pool of case studies to choose from, whereas the smaller Russian accounting firms have to develop their case studies and other materials from scratch.

Another advantage the large international firms have over the smaller Russian accounting firms is that the large firms are not limited to using Russian language course materials. In fact, most of the materials they use are in English. They can use such materials because their employees know how to read English. Materials that are used to educate their non-English speaking clients can be translated into Russian as demand warrants. The Russian firms, on the other hand, are more or less limited to using available Russian language materials. The quality of these materials may be lower than what is available in English. As was previously mentioned, the 1998 Russian translation of IAS is not at the same standard as the English language original, and the Russian accounting firms tend to use the Russian version, or educational materials that are spun off of the Russian version, in their seminars and classes.

The amount and variety of the accounting training the large international accounting firms provide to their employees and clients is also larger than what most Russian firms provide. One of the Big-Four firms interviewed provides at least 40 hours a year of training for their employees, and in many cases much more than that. It gives five days of training per year just on international standards and another 6 to 12 days on various technical accounting topics, which might include international standards. It also publishes a newsletter, which is available for both employees and clients, which contains articles on recent developments. All of their employees are also involved in some kind of international certification training.

An interview with a Russian accountant who works for one of the Big-Four accounting firms revealed that the quality of international standards education in the smaller firms is of a distinctly lower quality. Each firm makes its own course materials. In smaller firms, it is often the interpretation of the instructor that is taught rather than international standards. The instructor's interpretation may be much different than reality. Most instructors do not have access to real IAS materials. They must rely on translations, many of which leave something to be desired. One Russian firm teaches a course on the IAS Chart of Accounts, which is really amusing to those who are knowledgeable about IAS, since IAS has no chart of accounts.

This problem will be solved with time, as more English speaking Russian professors write their own texts and course materials. There is a joint Tacis PricewaterhouseCoopers project that is developing course materials in the Russian language, too, so that will also help to alleviate the problem of inadequate course materials.

One question that was asked of both the large international accounting firms and the smaller Russian firms was whether the new university graduates they hired were adequately prepared. The response generally was that they were adequately prepared for entry level positions. Interestingly enough, many American accounting firms, both large and small, think that recent graduates are not adequately prepared, even though the accounting education provided by universities in America is perceived as being better than that given by universities in Russia and other Eastern European countries. Some commentators have even referred to the situation in the United States as being in crisis (Gabbin 2002; Albrecht and Sack 2000).

Perhaps one reason for the difference in perception is because the educational system in Russia and other East European countries is more rigorous than the system in the United States. Russians get more math, starting in elementary school. By the time they reach the university, their level of knowledge in math may be better than that of a junior college graduate of an American two-year college.

Another possible reason for the view that recent Russian accounting graduates are adequately prepared for entry level positions is because of the training they receive in Russian universities. The top Russian professors earn about 7,000 rubles a month ($230), so they all have to do other things to make ends meet. Many of them engage in consulting. Others work as accountants, either for a firm or on their own. This outside work exposes them to the real world of accounting and provides them with a wealth of information that is not available in textbooks. Much of what they learn in the outside world is disseminated to their students in their lectures and case studies.

Accounting Certification

Russian certification has a credibility problem because of the perception that it is not of the same standard as international certification. This perception is being reinforced by the proliferation of private accounting clubs that "travel to cities and villages selling certificates."

Russians who take the official Russian government certification exam have a higher pass rate. Pass rates on foreign exams like the American Certified Public Accountant (CPA) or Certificate in Management Accounting (CMA) or the British Association of Chartered Certified Accountants (ACCA) exams are much lower. The Russian certification exams are perceived as being more like a university exam than a western certification exam.

These foreign exams are not recognized by the Russian government, but they are recognized and highly regarded in the marketplace. Almost all of the noncertified accountants who work at the Big-Four accounting firms in Moscow and St. Petersburg are studying for one or more of these foreign certification exams, even though the exams are given only in English. This English-only option precludes a large number of Russian accountants from taking these foreign certification exams. However, it also insures that high quality will be maintained, since these exams are proctored by the sponsoring organizations or their representatives.

As the interviews were being conducted, there was a rumor that the ACCA, the largest provider of international accounting certification exams, was going to start offering at least some of the exams in Russian. Several Russian speaking countries have been pressuring the ACCA to offer the exam in Russian for a number of years. Latin American countries have been pressuring the ACCA to offer its exams in Spanish as well. That is because ACCA certification is recognized in more than 160 countries, which gives its certificate holders immediate international recognition. ACCA has been hesitant to offer its exams in languages other than English for a variety of reasons, including cost and security. Offering the ACCA exams in Russian, or in other languages, would go a long way toward spreading knowledge about IFRS, since the ACCA exams test on IFRS. Several months after the interviews were concluded, the ACCA announced that it would offer some exams in the Russian language.

One private organization has started a 400 hours program to make certified accountants. A few centers prepare people for the certification exams in Moscow, St. Petersburg and the Urals. Accountants in other locations have to learn either from their employers or on their own. Hock Accountancy Training is perhaps the largest private provider of accounting certification training in Russia. It has training facilities in several cities and also has distance education programs available to help accountants pass the American

CPA, CMA and CFM exams. Hock also does IFRS training to a lesser extent. A number of private firms offer ACCA training.

There will be a demand for foreign certification exams in Russia as long as there is no credible Russian qualification. Russian certification is in statutory accounting. There is a movement to adopt an international certification model but it will be some time before such a movement has a finished product to offer to the Russian accounting community. Until Russia restructures its certification and shifts toward something that resembles international certification, the demand for foreign certification will remain strong.

Both of the Russian audit firms that participated in the interviews indicated a desire to establish a relationship with accountants who had foreign certification so that they could better serve their clients and so that they could expand their business into new markets. Perhaps the best way for Russia to approach certification would be to fully recognize truly international certification such as the CPA or ACCA and merely require those who want to be certified in Russia to pass exams on Russian business law and taxation. A similar method is being used in the EU and seems to be working well.

There is a movement to obtain outside assistance to establish an internationally recognized certification. Tacis and USAID have attempted to establish a regional certification in Central Asia and they want to open an office in Russia. The Central Asian model is based on CIMA, so it is likely that the Russian model will at least take a look at the CIMA model.

CONCLUDING COMMENTS

As a partner in one of the large international accounting firms stated, the three most important factors that international investors consider are who their partner is, whether the financial statements are transparent and whether the statements were prepared using either international standards or GAAP. Foreign investors are not at all interested in reading statements prepared using RAS, not only because they are not well versed in RAS, but also because they do not believe that the Russian statutory accounting rules provide good accounting information. Accounting reform is an essential ingredient of economic independence (Ichizli & Zacchea 2000)

Then there is the problem of what is called black cash. Not all transactions are recorded. The Russians have devised ingenious ways to evade taxes. Applying the international standards or GAAP to a company's books will not solve this problem if some important transactions are never included in the books. President Putin has instituted a low flat corporate (24%) and individual (13%) income tax, which will take away some of the incentive for playing tax evasion games, but tax rates that are low by European standards will not totally end the practice, since tax evasion is seen as not only a way to reduce taxes but also as a game.

Another question is how long it will take the rest of Russia to catch up to Moscow and St. Petersburg, in terms of the level of sophistication of financial reporting and in terms of accounting education. The only thing that can be said for sure is that it will take a long time. The process is market driven. Specific enterprises and regions will catch up as the market demands quality financial information. The speed with which the various regions will approach the Moscow – St. Petersburg standard will depend on whether international investors have an interest in investing in a particular enterprise or region, and on whether that enterprise is interested enough in attracting foreign capital to prepare its financial statements using some internationally accepted standard like IFRS or GAAP.

Another structural problem that needs to be overcome is the lack of knowledge of international standards on the part of the clients that retain the services of the large accounting firms. One partner who was interviewed revealed that only two of the accountants at one of the top Russian enterprises had any knowledge of the international standards whatsoever. This low level of knowledge makes it more difficult for any accounting firm to provide the proper services. Over time, this problem will shrink in importance, as the accounting firms train their clients and as a new crop of accounting graduates take their places in the accounting departments of these enterprises. But this process takes time.

There was some disagreement as to whether the level of accounting education would improve faster in accounting firms or in universities. The professors who were interviewed in St. Petersburg and Moscow thought that accounting education would improve faster in the universities. The reason they gave is that their professors are also engaged as outside consultants and they bring their knowledge into the classrooms.

But practitioners responded differently to this question. Especially in the case of the large international firms, there was the perception that the materials they provided for instruction and the resources they had to draw upon were of superior quality to those available in universities. Also, it could be mentioned again that the materials the international firms use for their training are often in English, whereas university materials are in Russian, so the universities have a translation problem to deal with that the big firms do not have to face. When this point was raised in the course of the interviews with university professors, they replied that this inherent weakness could be overcome by the professors, who would correct any mistakes in the course materials. But while this may be true in some cases, it probably is not true in all cases, especially in those cases where the professor is not able to read the international standards in the original English. In such cases, the professors will have to rely on the Russian translation, and they are likely to repeat the mistakes that are contained in the translated materials.

It will take a long time to fully implement international standards in Russia. The process is ongoing. However, it will happen, at least to some extent. If government continues to dominate the rulemaking process, RAS will never be identical to the international standards, for the several reasons mentioned above. But if the market takes over, Russian enterprises that want to attract foreign capital will prepare their financial statement using the international standards anyway. Government involvement in the standard setting process will merely serve to complicate accounting and make it more expensive.

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