

Problems and Prospects of Adaptation of Russian Accounting to International Accounting and Reporting Standards

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Introduction

Recently, despite the global financial crisis, significant development of organizations' foreign economic activity and a growth of foreign capital share on national markets can be observed. Even if the crisis has strongly shattered the globalization basis³, the tendency of general internationalization of economic activities is evident, which defines the need for information exchange between business entities. As a result, the need to create a common "economic language" which could be understood by all interested foreign users and the demand for developing common approaches to accounting which are the main informational basis for making investment decisions are arising.

International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) have become an effective instrument for the above-mentioned problems solving. They represent a body of rules for preparation and representation of unified financial (accounting) reporting, which is clear and useful for users across the globe.

For a relatively short period of existence (starting from 1973) international standards have widely spread in many countries: Kazakhstan, Greece, Kuwait, China, Lebanon and many others. They are used in organizations included into the European stock listing: London, New York and Tokyo stock exchange bind

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³ According to Italian daily economic newspaper "IlSole24Ore", after the crisis the enormous outflow of foreign capital has been observed all over the world. In 2008 the USA financial institutions reduced the abroad-oriented investments by 587 milliards of dollars and the European investors had to withdraw 483,5 milliards of dollars from American deposits: "Effetto crisi finanziaria, il mondo si deglobalizza" ("*Financial crisis effect, the world is deglobalizing*"), IlSole24Ore, March 8, 2008.

companies to provide information prepared according to IAS and IFRS requirements. The FASB (Financial Accounting Standards Board) of the USA and the IASB (International Accounting Standards Board) stated their intention to harmonize GAAP (General American Accounting Principles) and IFRS⁴. The famous scandal with the Enron Corporation is not of the least importance in this. The point is that according to GAAP of the USA, Enron was allowed not to include into consolidated reporting the data of its losing subsidiary companies (the so-called “special-purpose companies”), which made it possible to conceal its liabilities and losses. This wouldn’t have been possible if the reporting had been made according to IFRS.

In August 2008 United States Securities and Exchange Commission (SEC) submitted a plan of transition to IFRS and abandoning GAAP during the next 6 years. According to this plan, as early as in 2010, transnational American companies (it is expected that there will be more than 110 of them by that time) will be obliged to submit reporting according to IFRS. Starting from 2014 accounting according to IFRS will be obligatory for all American companies.

What does the Russian Federation undertake in this situation? What is the value of international standards in our country? Is the full transition to international standards possible in Russia? What difficulties are going to arise? Our work is devoted to the analysis of these issues.

1. The History of the Subject

Historically the beginning of Russian accounting reformation process refers to 1992 – the year when the “State Program of the Russian Federation transition to the internationally accepted system of accounting and statistics in accordance with

⁴ «Norwalk» agreement (signed in September 2002) – FASB and IASB agreed to achieve a full coordination of their standards and coordinate their work in future.

the demands of the market economy development” was adopted⁵. In 1994 the Methodological Board of accounting at the Ministry of Finance of the Russian Federation approved the program of accounting system reformation, according to which the transition to IAS and IFRS had to be completed by 2000.

However, by 1998 it had already become clear that the given document needs to be seriously adapted what defined adoption of the new program of accounting reformation in accordance with the international system of financial statements (ratified by the Russian government resolution, 06.08.1998 № 283). That was the time when a lot of new conceptual principles of international practice, such as accrual method, substance over form, materiality, prudence, etc. entered the theory and practice of national accounting in Russia.

A new step in accountancy reformation in Russia became the Conception of Accounting and Reporting Development in Russia for a medium-term perspective, ratified by the order of the Ministry of Finance, 01.07.2004 №180. This Conception defined the following main stages of adaptation of the Russian accounting to international rules and standards:

The first stage - 2004-2007 The following actions were planned for this period of time:

- obligatory transition to IFRS of consolidated financial reporting of socially important business entities (public limited companies and other organizations which have publicly placed (traded) paper holdings, as well as financial organizations working with means of physical and legal bodies) ;
- approval of the main set of Russian standards of individual accounting on the basis of IFRS;
- improvement of the principles of and requirements to the organization of accounting process, as well as the basic rules of accounting providing information forming for creating individual and consolidated financial reporting;

⁵ Ratified by the Supreme Soviet resolution № 3708-1 dated 23.10.1992.

- creation of a special organ within the framework of the system of accounting and reporting standards approval;
- creation of the main elements of IFRS application infrastructure;
- approach of tax accounting rules to accounting rules;
- activation of professional public associations' participation in accounting and auditing professions regulation and development;
- reinforcement of control over consolidated financial reporting publicity on the part of socially important business entities;
- improvement of the system of staff training, including accounting users;
- development of international cooperation in accounting, reporting and auditing area.

The second stage - 2008-2010 Its essence consists in realization of the following measures:

- obligatory transition to IFRS of consolidated financial reporting of all organizations;
- estimate of the possibility of individual accounting directly according to IFRS (instead of Russian standards) on the part of some certain number of business equities;
- reinforcement and expansion of the scope of activities of a special organ within the framework of accounting and reporting standards approval system;
- further promotion of the role of professional public associations in development and regulation of accounting and auditing professions;
- development of the system of control over accounting reporting publicity provided by business entities;
- expansion of the control sphere to the quality of accounting reporting, including that prepared according to IFRS.

With the aim of realization of the considered Conception of Accounting Development a document called “Plan of Measures for 2004-2007”⁶ was adopted by the Ministry of Finance of the Russian Federation. The main measures listed in this regulatory document were:

- adoption of the necessary legislative acts for adaptation of the Russian accounting to the principles and rules of international standards;
- improvement of the quality of financial information formed in accounting and reporting;
- transformation of the accounting and reporting regulation system;
- organization of constantly active system of IFRS translation into Russian
- establishment of special organs for IFRS adjustment and adaptation in Russia;
- creation of the system of formation of national standards adequate to IFRS
- reinforcement of accounting and reporting control;
- accounting and auditing staff training and professional development.

Thus, the government of the Russian Federation set a task of creating an adequate infrastructure promoting application of international accounting and reporting standards in our country. In this connection, the increase of trust to reporting made according to the principles and rules of IAS and IFRS, and, as a result, their introduction into the practice of the majority of Russian companies, have gained primary importance.

A lot of the above-mentioned measures have already been implemented. Let's name the main results of the actions taken within the framework of reformation of the Russian system of accounting and reporting.

2. Current Condition

⁶ Ratified by the Order of the Ministry of Finance of Russia № 263 dated 06.09.2004.

Starting from 2004, all Russian loan institutions make their accounting reporting according to IFRS.

According to the data of the Federal Statistics Agency, more than 42 large Russian companies have been forming financial (accounting) reports in accordance with IFRS for a period of more than 5 years. They are such organizations as AvtoVAZ, Aeroflot, KamAZ, Norilskiy Nickel, Rostelekom, Severstal, Transneft, Alrosa, Rossiyskiye Zheleznnye Dorogyy (RZD), Lukoil, and many others.

Out of 400 companies included into the “Expert-400⁷” rating, 94 prepare consolidated reporting according to IFRS; all the rest keep to the rules defined by the Russian (277 organizations) and American (29 enterprises) legislation.

As for the large companies, according to the data received at the end of 2008, 56% of them make reporting according to the international standards. Compared to this, the figures were different in 2006: only 33% of large companies had their reporting according to the international standards. (fig.1)

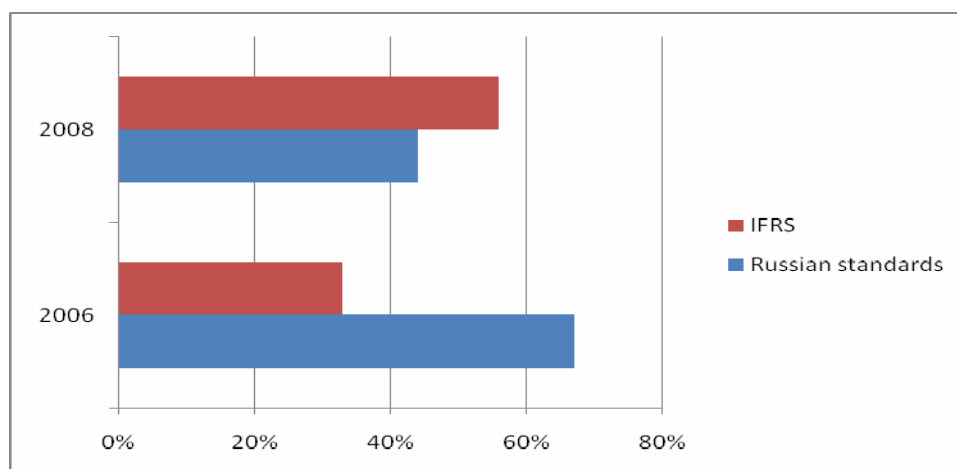


Fig. 1. Large Russian organizations, forming their reporting in accordance with IFRS.

However, if we consider all organizations registered in the Russian federation, including large, medium-sized and small ones, the share of enterprises applying IAS and IFRS in their practice is substantially reduced – 16%. (fig.2)

⁷ “Expert” is one of the most prestigious weekly economic magazines in Russia published in Moscow since 1995.

The majority of enterprises applying IFRS operates in such areas of economics as finance and insurance (37%), industry (15%), service industry: public catering, hotels, etc. (13%), trade (12%) and medicine (11%). The major part of these companies is situated in North-West (19%) and South (17%) federal districts⁸.

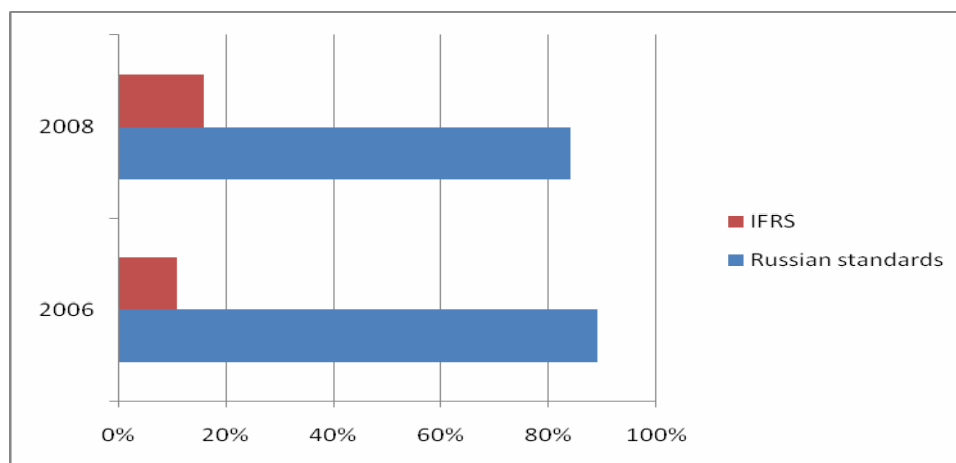


Fig. 2. Russian organizations, forming their reporting in accordance with IFRS

As it is seen from the data given above, IFRS is gradually spreading in the practice of Russian companies. According to experts' estimate more than half (61%) of accountants and auditors of commercial organizations agree with the fact that Russian accountancy must be based on IFRS. As their main reasons they name the following advantages of international standards (fig.3):

- management data quality improvement - 38%,
- investment attraction increase - 28%,
- increases opportunities for debt financing 27%,
- other (increasing the degree of shareholders' demands satisfaction, entrance to the international market, simplicity of reports preparation, quickness

⁸ According to the Law «On the Authorized Representative of the President of Russian Federation in the Federal District» dated May 13, 2000, the territory of Russian Federation was divided into seven federal districts: Central (with the capital in the city of Moscow), North-West (Saint-Petersburg), Ural (Ekaterinburg), Southern (Rostov-on-Don), District-on-Volga (Nizhni Novgorod), Siberian (Novosibirsk), Far East (Khabarovsk).

and convenience of IFRS application, pithiness, high accuracy of prepared data). – 7%.

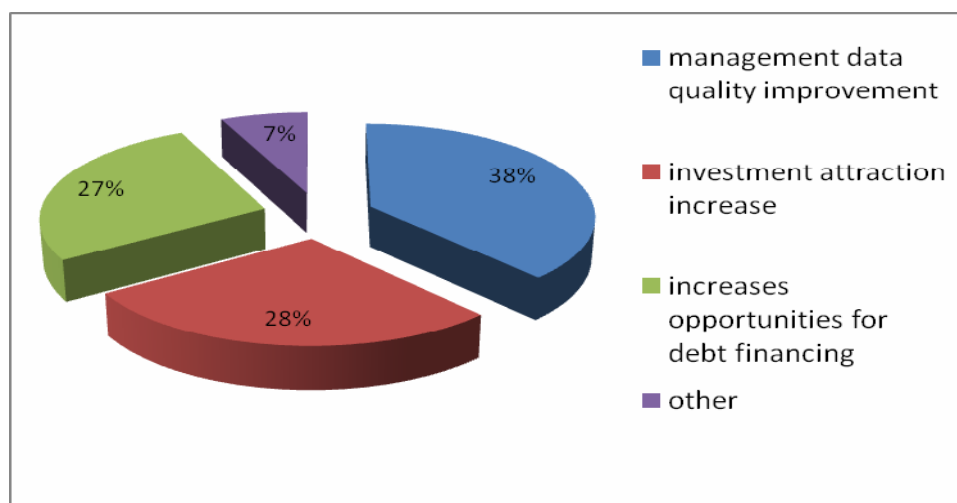


Fig.3. IFRS advantages according to Russian accountants and auditors

Only 18% of Russian specialists consider it to be absolutely useless to transform accounting into the format corresponding to the international standards. 21% of accountants are neutral in their estimate of IFRS application effectiveness. Approximately the same opinion is expressed by university students and teachers of economic specialties of Russian higher educational institutions. Among them 71% highly estimate the effectiveness of IFRS application; 20% of teachers and students cannot find their position; only 9% consider reporting transition into the format corresponding to the international rules (standards) to be ineffective.

All the above listed figures are evidence for understanding by Russian specialists the usefulness of international standards, their importance while entering foreign markets. There is no doubt that reporting made up according to IFRS contains more information directed at the demands of external and internal users: investors, owners, creditors, managers and many others.

3. Development problems and prospects

However, the process of adaptation of the Russian accounting with IRAS and IFRS is not as simple. Naturally, introduction of new rules into practice in the

country with stable traditions and norms require considerable time and financial costs⁹. It is evident that time constraints set by the Accounting Development Concept in the Russian Federation for a mid-term prospect for consolidated accounting of all organizations obligatory transition to IFRS (2010) will be broken. So, what are the main difficulties which arise while introducing IFRS in Russia:

- Russian accounting and audit specialists single out diverse problems and obstacles while introducing international standards (fig.4):

- inconsistency between IFRS methods and principles and the Russian norms (use of professional judgment and estimates in IFRS and norms and rules in Russian Accounting Regulations which are prescribed in detail),

- lack of official translation of IFRS into Russian,
- lack of qualified personnel and necessary training centers,
- lack (expensiveness) of software allowing transforming Russian accounting into the IFRS format,

- some other (absence of exact requirements for IFRS introduction in Russia, the necessity to expand the accounting staff, constant changes of international accounting and reporting standards, etc.)

⁹ The process of accounting rules harmonization is also the aim of European Commission where since '70s different Regulations like 78/660/CEE, 83/349/CEE, 86/635/CEE, 91/674/CEE were published. The goal was the same: to reinforce comparison and permit stakeholders to analyze and understand the balance sheets of businesses operating in different countries, but even in this case there were many elements that did not allow the effective harmonization of documents, although in these rules the postulates like fair value, liability, and consistency of balance sheets and the introduction of a Supplementary note, as their inseparable part were present. Until then these principles had been only partially implemented by European countries. The most important recent events in this field were the Lisbon conference (March, 2000) and, later, First of all, the regulations of immediate application within the European states (n. 1606/2002/CEE) called on the IAS to draw up balance sheets from January 2005, together conceding and extending them to be applied to other forms of businesses.

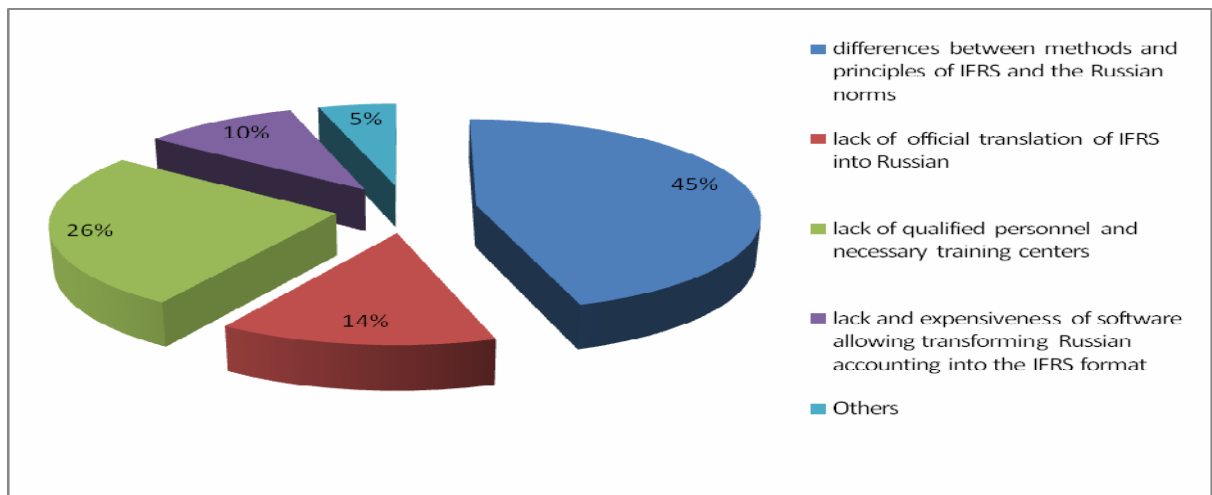


Fig.4. The main obstacles to IFRS introduction in the Russian Federation (according to accountants' and auditors' opinions)

The main problem hindering adaptation of Russian accounting and reporting into the format corresponding to IAS and IFRS is inconsistency between the principles and rules of Russian legislation and the requirements of international standards. Modern companies have to prepare several formats of accounting: firstly, reporting made up according to the rules of Russian accounting regulations, secondly, tax accounting prepared according to the requirements of tax law, and thirdly, accounting based on international rules and standards. Naturally, it considerably increases expenses on preparation of high quality financial information.

Besides, accounting prepared in accordance with IFRS differs from the Russian accounting reporting by a bigger information content and analytical aspect of the provided data. It also increases expenses of the organization (both financial and time) for collecting necessary information and its check.

The way out of this situation can be the integration of the mentioned accounting systems, their maximum approach to each other. It should be noted that a lot of steps have been made by the Government of the Russian Federation in this direction. New editions of the following accounting regulations which are maximally close to the international practice have been accepted: AR (accounting regulation) 1/2008 "Organizational Accounting Policy", AR 2/2008 "Building

Contracts Registration”, AR 14/07 “Non-Material Assets Registration”, AR 15/2008 “Loans and Credits Expenses”, AR 21/2008 “Estimate Values Alterations” and some others.

One more problem of IFRS introduction in Russia is a lack of qualified personnel. As it is known, according to international accounting standards the basis for making up accounting is professional judgment and estimate of accountants, financiers and other organization staff, while Russian accounting regulations are built on the norms and rules which are registered in details. Naturally, such discrepancies in the way of reporting formation require additional qualification of organization staff and adequate skills acquisition.

Besides, a problem of external and internal control of reliability of the information prepared according to IFRS is also an acute one. According to the International Standards Principles and Rules, the main goal of reporting formed according to IFRS is preparation of quality, neutral, clear and useful information for all interested users. However, the subjectivity of estimates caused by professional judgments of specialists, and the possibility to apply to a considerable number of alternatives while reflecting the facts of financial-economical activity allows varying the size of financial indicators, making the financial position of the organization look better (or worse depending on the set task)¹⁰.

Unfortunately, today the number of auditing organizations able to audit such accounting is not enough. First of all, they are large international companies of the “Big Four”: Pricewaterhouse-Coopers, KPMG, Ernst&Young, Deloitte&Touche, as well as some Russian companies, who have obtained a certain international recognition and become full members of international organizations: BKR Intercomaudit (Moscow), Rusaudit - Baker Tilly International, Top-Audit (RSM)

¹⁰ Naturally, in such a case reporting doesn't fulfill the requirements set before it, and its content misleads the users, and, as a result, wrong managerial, investment and other economical decisions may be made. In this situation only qualified specialists of financial control, such as internal and external auditors can help.

and other. The number of internal auditors who are able to plan and fulfill the check of information prepared according to IFRS is also not very big.

A survey of accountants and auditors showed that only 3% of specialists evaluate their level of knowledge in the area of international standards as “excellent”, the majority admit that they have “minimal (basic)” knowledge – 61%. The situation among the teachers of Russian higher education institutions is slightly better. About 10% see their knowledge as “excellent”, about 60% - as “middle”, and 30% - as “minimal (basic)” one.

Naturally, it is not enough to teach IAS and IFRS principles to a certain number of accountants and auditors of our country. Due to the constant change of the international standards content, reformation of them, a system approach to Russian specialists’ qualification improvement, creation of special counseling and training centers is required. Besides that, there is a demand for a special organ, whose competence will be to prepare official translation of IFRS into Russian, its continuous specification connected with the appearance of new standards editions, as well as training of interested specialists, such as external and internal auditors, office accountants, accountants, financial managers and many others.

One more problem that arises while adapting the Russian accounting system to international standards of financial reporting is the absence, and, consequently, cost of adequate software. Those organizations who have made a decision to form their accounting according to IFRS, must either modernize the accounting systems they already have or obtain new ones. Modernization of the existing software initially requires less financial investment; however, it often leads to errors in program operation, which in the long run will become inefficient as it will define the necessity of constant corrections in order to satisfy accounting requirements.

On the other hand, new software introduction is always connected with substantial expenditures, and not every organization can afford it. Besides, computerized systems have just started appearing on the Russian market, allowing keeping records corresponding to both national and international standards, and the process of their adaptation to a concrete economic subject, as a rule, takes a lot of

time. It should be noted, that both the first and the second choice will inevitably lead to a necessity of personnel training, which will again increase financial and time expenses connected with IFSR and IAS introduction.

Conclusion

Russian companies are confronted with a number of problems while preparing reporting in accordance with the international accounting and financial reporting standards. These problems substantially hinder the process of accounting reformation in our country and contribute to the appearance of a great number of opponents. However, in our opinion, the dispute over the necessity of IAS and IFRS use in our country is pointless. It is obvious that reporting prepared according to the principles and rules of international standards is in demand across the globe, and their adoption substantially increases the chances of foreign capital formation for Russian companies: it is an efficient means of protecting the interests of the relevant parties.

However, all the above-listed advantages immediately disappear without proper control over the prepared information, without checking it by internal and external audit specialists. Besides, while developing new Accounting Regulations in our country, characteristic features of Russian accounting system, traditions and rules shouldn't be forgotten. Only a compromise that combines current international best practices with the set national approaches can allow preparation of reliable, neutral, complete, analytical accounting adequate to the set goal: providing all stakeholders with useful information.

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