

Chapter 1

INTRODUCTION

Much of the information included in this book is based on the authors' experience of living and working in Eastern Europe and the former Soviet Union. Some data was gathered during the course of interviews with a variety of accounting practitioners and educators. Much of our research findings tended to confirm what was discussed in the existing literature. Thus, part of this book updates and expands on existing literature. However, new information was also uncovered that has not yet been discussed or addressed in the literature.

Most of the chapters in this book were first presented as conference papers, which improved the quality of the final product in several ways. When the various manuscripts were in the early draft stage a series of anonymous reviewers provided suggestions that led to improvements in subsequent drafts. Comments from participants at the conferences resulted in further changes. A few of the chapters won the conference *best paper* award.

This book examines not only accounting reforms but also other aspects of financial system reform, in the broad sense of that term. Issues relating to corporate governance, foreign direct investment, taxation and public finance, accounting education and accounting and finance certification are also discussed.

Reformers of accounting and financial systems in transition economies encounter several common problems regardless of the country. We have found that translation is a common problem. Sometimes terms simply do not exist in the target language for certain accounting and finance concepts. Translators have to somehow overcome these problems. Another problem relating to translation is finding translators who know both English and the target language as well as accounting. In some countries, such people are difficult or impossible to find. What one must do in such cases is find good translators, then train them in accounting terminology.

Another common problem we have encountered, regardless of the country being examined, is the quality of materials that have already been translated into the target language. First editions are especially prone to mediocre translation. One particularly interesting example comes to mind. When the first edition of the Russian translation of the International Accounting Standards (IAS) was issued during the late 1990s, the translators left out the word "not" in one place. It was in a section that gave a list of things not to do. But because that word was missing, readers of that page were led to believe that everything on the list were things that *should* be done, when in fact they were things that should *not* be done. Thus, readers of the

Russian edition were prone to do exactly the wrong thing for a half decade or so, until the second Russian edition was published. It is not clear whether the second edition corrected this mistake, either, so perhaps current Russian readers continue to be misled by this omission.

Although translation is a common problem that must be faced and dealt with in any transition economy, it was not the only problem we found. There is also a problem of what might best be called inertia. Many accountants in the transition economies we studied simply do not want to change what they are doing. In some cases it is because they do not see the need for change. In other cases it is because they are afraid, or even terrified of change. Whenever there is change, there are winners and losers. Those who perceive themselves as being losers tend to resist change. The older generation of accountants, especially those who are approaching retirement age, also tend to resist change. There is a certain logic to this position. Why go through the considerable effort of learning the new rules if you are only a few years away from retirement? But problems result when the people who think this way also try to prevent changes from taking place. It is one thing to decide not to upgrade your own skills. It is quite a different thing to work toward maintaining the status quo, which is what some older accountants who are also in positions of power have done in some transition economies.

Another common problem of implementing accounting reforms that we have found to be common to the transition economies we have studied is education. Accountants who are already in practice need to learn the new rules. The new generation of accounting students need to be taught the new rules. But there is a shortage of professors who are capable of teaching the new rules, especially in the early years of reform. Professors have to be trained before students can become exposed to the new rules that their country has adopted.

Another problem that is common to all of the countries we have studied is the credibility of accounting certification. In some transition economies it is possible to buy an accounting certification. In other cases accounting certification is not credible because the examinations are too easy to pass and do not test on international accounting and auditing standards.

International investors do not place much credibility in the financial statements of companies that are audited by local audit firms. Sometimes this lack of credibility is because of the widespread perception that audit opinions can be bought. Another reason is because many individuals who work for local audit firms have little or no knowledge of international accounting and audit standards. However, this lack of knowledge has not always proven to be a problem for the local accountants and auditors because there is a general lack of demand for the preparation of financial statements that are based on international financial reporting standards.

Most companies that have such statements have them because they want to attract foreign capital. They prepare U.S. GAAP statements if they intend to list their shares on an American stock exchange or if they intend to

borrow from a bank in the United States. They prepare IFRS statements if they want to raise capital in London or another European city. Enterprises that do not intend to raise foreign capital have little or no incentive to go through the time, trouble, effort and expense of issuing IFRS statements because there is little or no demand for such statements. In many countries, the statements are prepared for the tax authorities, since financial accounting tends to be tax driven.

This book discusses the process of accounting and financial system reform in several East European and former Soviet countries. Chapter two examines the problems Russia faces in adopting and implementing International Financial Reporting Standards (IFRS), which many Russian companies are now required to follow. Chapter three discusses accounting reform in Ukraine. Chapter four discusses Armenia, a former Soviet republic.

Part two looks at accounting education and certification. Although the emphasis is on accounting education in universities, some time is also spent discussing accounting education for practitioners. One chapter is devoted to private sector accounting education in Russia.

Accounting certification is the subject of another chapter. One of the main problems of accounting certification throughout the former Soviet Union and the former centrally planned economies of Eastern Europe is the lack of credibility. There is a new regional accounting certification program aimed at overcoming this pervasive lack of credibility. It started in Central Asia a few years ago and is now spreading to some of the other former Soviet republics. Certification is at two levels and all exams are given in the Russian language, which makes the exams accessible to a wide audience. Prior to this program, any accountant in the former Soviet Union or centrally planned East European country had to take a certification exam in English in order to have a credible accounting certification.

Part three examines recent changes in corporate governance in various East European countries. Companies need good corporate governance practices not only to run efficiently but also to attract foreign investment. Yet present corporate governance practices leave much to be desired. Transparency and shareholder rights are relatively new concepts in Eastern Europe and the former Soviet Union. Traditionally, there has been a tendency to hide relevant facts rather than disclose them. This view must change if companies in transition economies are to have good corporate governance practices.

Part four presents a comparative study of Russia and some other transition economies in the area of taxation and public finance. Prior to the collapse of the former Soviet Union, tax systems were much different. There were no private corporations to tax and the government owned all assets. As enterprises began to become privatized and as new enterprises were formed in the private sector, tax systems had to be developed to raise the funds needed by government. This section compares some transition economies to some more developed economies in the area of public finance.

The final chapter addresses the issue of tax evasion and presents the results of a survey taken of Romanian students and professors. This volume is the second volume in a series that addresses problems of accounting and financial system reform in transition economies. The first volume focused on Russia. Other volumes will look at other transition economies, or specific areas, such as public finance.



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