EXPERIENCING
THE ACCOUNTING
PROFESSION IN

Russia

By Kimberly Charron, CMA, and Marilyn Young, CPA
Russia has been in the news a lot lately—some of it good news, some of it bad. The Winter Olympic Games, held in February in Sochi, showcased world-class athletes in a first-rate, picture-postcard setting. More recently, however, Russia’s conflict with Ukraine has cast a darker light on Russia and President Vladimir Putin, in particular, with tension continuing to build as of the end of May.

It’s against this backdrop that we reflect on a journey we took to Moscow and St. Petersburg to better appreciate the similarities and differences between the U.S. and Russian accounting professions. This eight-day trip, organized by People to People International’s Citizen Ambassador Programs for women accounting professionals (see the sidebar “How We Became Citizen Ambassadors”), included visits to a Big 4 accounting firm, a small local accounting firm, and the campus of St. Petersburg State University. How better, we thought, to expand and enrich our understanding of business practices of global entities in the United States and abroad—especially in light of the impact that the widespread implementation of International Financial Reporting Standards (IFRS) will have on our responsibilities as professionals.

In this article, we’ll describe what we learned about Russia’s business climate, Russian Accounting Principles (RAP), the status of IFRS implementation, and the regulation of local audit firms and accountants. We’ll also share what we discovered about Russia’s tax system, the education and certification process for accountants, and challenges facing the Russian accounting profession.

A Vast Economy Marked by Corruption

The Russian Federation is the world’s largest country in terms of territory, and it has a population of approximately 143.5 million. Russia has a tremendous wealth of natural resources, including roughly one-third of the world’s natural gas reserves and the eighth-largest oil reserves. In addition, Russia has a highly educated workforce, attributable in part to the free education that was provided by the former communist regime.

In the old Soviet Union, the widespread availability of post-secondary education, combined with a requirement that all women had to work, had an interesting impact on the development of the accounting profession in Russia. As women attended universities in the Soviet Union, they gravitated toward earning degrees in accounting. Consequently, accounting is a female-dominated industry in Russia. At the time of our visit, women comprised a whopping 78% of the accounting profession. In 2011, the Bureau of Labor Statistics estimated that women working in the U.S. represented 61% of all accountants.

Following the collapse of the Soviet Union in 1991, Russia began to slowly transform from a centrally planned economy to a free market system. The most significant piece of this transformation is privatization. Despite the fact that new business formation is hampered by a lengthy approval process that can take up to nine months to complete, more than 75% of the country’s economy is in private hands.

Perhaps the most troubling result of the transition to a free market system is the extensive corruption that plagues the Russian economy. While in Moscow, we visited Ernst & Young (EY) and discussed the firm’s 11th Global Fraud Survey (published in May 2010) with audit staff and managers. In the survey, the firm estimates that between 30% and 50%, or approximately $300 billion, of the Russian economy is attributable to fraudulent or corrupt activities. By comparison, in the same survey, the estimate of fraud and corruption in the U.S. economy is only 7%. The survey highlights comparisons in the responses of business managers in Brazil, Russia, India, and China (BRIC countries) and concludes that Russian businesses lag behind the other BRIC countries in their antifraud efforts. In the survey, only 26% of Russian respondents expressed confidence in the internal audit process, only 30% of respondents’ companies have established a hotline to report fraud, and only 28% have anti-corruption internal control procedures.

In EY’s most recent international survey, 2013 Europe, Middle East, India, and Africa (EMEIA) Fraud Survey, the
Russian responses continue to be troubling. A majority of Russian survey participants answered “yes” to the following statements: “Managers at our business are under increased pressure to deliver good financial performance over the next 12 months” (65%) and “Companies in this country often report their financial performance as better than it is” (61%).

In our discussions with Moscow-based EY accounting professionals, they identified fraud as a significant threat to the country’s opportunities for economic growth and recommended stricter legislation to punish fraudulent business practices. The success of stricter legislation, however, will depend largely on how effectively these rules are enforced. One Russian accounting professional shared with us a phrase that’s common in Russia: “The strictness of the Russian law is compensated by the ability not to follow it.”

Statements like this reveal that there’s much to overcome and that the willingness for enforcement will have to be matched by a willingness of the business community to report fraud. The common business practice in Russia is to treat fraud as an internal company matter that’s rarely reported to authorities. The lack of formal reporting practices partially accounts for the wide-ranging estimate (30% to 50%) in EY’s fraud survey. Moreover, the definition of fraud is a moving target. EY’s research reveals that in some areas traditional bribes to elected officials have been replaced with social requirements, such as building a road in exchange for being able to operate a business within the municipality.

In the area of accounting and financial services there are many instances where auditing firms have “bought” licenses to practice, resulting in questionable service and a loss of faith in the auditing system. On the other hand, since corruption is widespread, there’s also a growing interest in fraud investigation services, which is a new avenue of business for CPA firms. One caveat to this, though, as a professional in this area told us, is that many corporations seek fraud investigation services to determine the nature and extent of corruption but rarely act on the findings. This result is a testament to the difficulty and time it takes to truly transform a business culture.

Gearing Up for IFRS

In 2004, the Russian Ministry of Finance developed a plan to gradually adopt IFRS by 2015. In March 2011, however, then-President Dmitry Medvedev moved up the timeline and required all public-interest companies, including banks and insurance companies, to adopt IFRS

How We Became Citizen Ambassadors

Our eight-day adventure to Russia came courtesy of People to People International (PTPI), which was founded in 1956 by President Dwight D. Eisenhower with the mission to promote world peace and cultural understanding through meaningful direct personal exchanges. The Citizen Ambassador Programs offered by PTPI encourage a wide range of professionals to “get out of the workplace and into the world.”

The cost for each program varies based on the destination, and the Citizen Ambassadors pay out of their own pockets for the opportunity to join the delegation. In rare instances, an employer may pick up part or all of the tab. PTPI arranges all travel and site visits within the host country. Program itineraries are posted on the organization’s website, and anyone interested can contact PTPI to join a delegation. The application process is easy.

As space is limited, the programs are filled on a first-come, first-served basis, and each program description includes the deadline for applications. PTPI organizes trips for a wide array of professionals (business, law, healthcare, etc.), and each trip is led by a professional who acts as a liaison with the PTPI.

As you can tell from reading the article, our trip was very rewarding and greatly expanded our knowledge of Russia’s accounting profession. PTPI provided our 18-person delegation with an efficient way to experience another culture and talk with Russian accounting professionals. The inside view into their professional world was invaluable. We certainly appreciated the candor of the professionals who shared their work experiences with us and helped us develop a better sense of the global economy.

If you’re interested in an opportunity to move beyond reading books and articles and to join PTPI on an educational trip abroad, go to https://citizens.peopletopeople.com for more details.
been since July 7, 2010, that the State Duma approved a statement are prepared in Russian rubles. It has only reporting and functional currencies. Rather, all financial federal law that requires businesses to consolidate financial accounting concept. Further, there’s no definition of allocations, goodwill, the fair value concept, or the expense or depreciation, don’t exist in RAP because there’s no independent documentation to support the entry. In addition, RAP doesn’t include purchase price allocations, goodwill, the fair value concept, or the impairment concept. Further, there’s no definition of reporting and functional currencies. Rather, all financial statements are prepared in Russian rubles. It has only been since July 7, 2010, that the State Duma approved a federal law that requires businesses to consolidate financial statements. Under prior law, each business within a larger conglomerate reported separate financial statements, making it difficult for investors to get a true picture of the conglomerate as a whole.

In announcing the timeline for the transition to IFRS by 2018, Belousov stated that investors often complain that RAP reporting lacks transparency, and, consequently, users of financial statements find it hard to apply standard ratio analysis to Russian financial statements. Even after the mandatory use of IFRS for public-interest companies in 2012, many multinational firms that operate subsidiaries or branches within the Russian Federation and companies that trade on exchanges outside Russia were required to prepare financial information using both RAP and either IFRS or U.S. GAAP.

RAP also includes many industry-specific rules that further complicate financial reporting. For example, Russia’s oil and natural gas companies are largely multinational firms that are allowed to follow U.S. GAAP because that industry-specific standard exists in RAP. In fact, one accountant with experience in this industry told us that many Russian accountants have historically traveled to the U.S. to take the CPA exam and become licensed to further their careers in Russia’s oil and gas industry. As IFRS becomes the global common language of business, however, Russia’s adoption of IFRS will simplify things by eliminating the requirement for multinational firms to use multiple accounting standards to prepare multiple sets of financial statements.

If Russia is ever to enjoy a more open and transparent business environment, the country will need a robust auditing workforce within the accounting profession. Since 2007, audit firms and Russian Certified Professional Auditors are required to be members of a Self-Regulatory Organization (SRO). This is viewed as a positive step for the profession since the prior licensing procedure was plagued by corruption and licenses could be purchased without regard to actual qualifications. The SROs now develop professional standards, provide continuing education, register members, and control education requirements for membership. While this has been a major step forward, we were told there’s still work to be done in this area to combat corruption.

A Very Different Tax System

In nearly all of our visits with Russian accountants and business professionals, the conversation turned to taxes and tax audits. There’s a great deal of concern, especially about the tax system and the process of being audited by the taxing authorities.

Not surprisingly, the Russian tax system is very different from the U.S. system. For example, partnerships as legal entities don’t exist under Russian law, and the tax system doesn’t include S corporations. Rather, all business entities in Russia resemble C corporations and are classified as either Russian legal entities (RLE) or foreign legal entities (FLE). In addition, there’s no consolidation option for multiple entities with common ownership. Rather, each entity must file a separate tax return. RLEs are taxed on their worldwide income, and the tax base is a modified gross profits amount measured using the Russian definition of accrual accounting. While corporate tax rates include a 2% federal tax and an 18% regional tax, the combined maximum rate of 20% represents the lowest marginal tax rate among G8 countries.
One of the most difficult tax compliance issues is how to determine gross profits. As previously noted, under the Russian accrual accounting rules, all revenues and expenses must be supported by proper documentation. Moreover, the deductibility of expenses for tax purposes is based on whether or not the expense is “economically justified.” Unlike the U.S. tax code, where Congress has established an “ordinary and necessary” standard for the deductibility of business expenses and hasn’t provided a list of preapproved expenses, the Russian tax code contains a list of tax-deductible expenses. In practice, it’s very difficult to deduct an expense that isn’t included in this list.

**Fewer Income Tax Returns**
The Russian government maintains programs for pensions, healthcare, and the “social provision” (including unemployment, maternity leave, and daycare costs). These benefits are funded by an employer-paid unified social tax, which is based on workers’ salaries. The rate structure is progressive, with a maximum rate of 30% imposed on an employee’s wages, up to a wage limit of 512,000 rubles (roughly US$14,700). Those who earn more than the threshold are subject to a 10% tax on the excess, which goes into a government-administered retirement fund. Excluding the imposed tax on excess earnings, the structure of the unified social tax is similar to the U.S. Social Security tax, as the wage limit for determining the tax is set just slightly above the average annual salary for a Russian worker (approximately 475,766 rubles, or about US$13,657).

The social tax is paid entirely by the employer, with no employee-matching contributions. Individual taxpayers also are subject to a 13% flat rate income tax, which employers are required to withhold from wages and remit to the taxing authorities. Employees who are salaried and have no other source(s) of income aren’t required to file an income tax return. Rather, the individual’s income tax liability and reporting responsibility are completely satisfied through the employer’s remittance of the withholding amounts.

The system isn’t perfect, however, because a high percentage of income derived from fraud and corruption escapes the tax system each year. Consequently, the reduction in tax revenues has led to cuts in funding for social programs. For example, one accountant indicated to us that the amount paid for maternity leave is so low that most new mothers go back to work long before their allotted time to be at home with their newborns expires.

In an attempt to preserve the tax base, Russian authorities routinely perform tax audits. As one professional described it, audits can happen at any time—they’re common for Russian individuals and businesses. In EY’s 2010 Russia Tax Survey, 63% of respondents reported being assessed an additional tax liability from tax audits during 2009. Only 29% of these respondents agreed with the assessment of additional tax. The survey found that when the taxpayer disputed the assessment in court, fewer cases were being decided in the taxpayer’s favor. From 2006 to 2008, taxpayers prevailed 89% of the time. That figure fell to 67% in 2009. While taxpayers still prevailed in the majority of cases, the high incidence of tax audits and the shrinking number of successful challenges to the audit findings have created a negative perception of Russia’s tax regime among non-Russian multinational companies, which could hamper the country’s efforts to attract foreign investment.

**Shifts in Education and Certification**
As noted earlier, Russia has a highly educated workforce. In fact, prior to the fall of the Soviet Union the college attendance rate was approximately 80%. But as Russia has transitioned from communism to a free market economy, post-secondary education is no longer a completely state-funded benefit, and college attendance rates have fallen. In the Soviet Union, women pursuing careers in business primarily chose accounting as a major, while men pursued degrees in banking and finance. Because of the large number of women in the profession, the public perceives that women are the experts in the field. As one professional described to us, entrepreneurs who seek to start

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new businesses will place women in chief accounting roles to establish credibility with the banks and financial institutions and thereby increase their chances of getting funding.

As the transition to a free market economy continues, gender equity appears to be on the horizon within the Russian accounting profession. When we visited the St. Petersburg State University of Economics and Finance, there were 900 students majoring in accounting, approximately 40% of whom were men. As one professor described the program, accounting may not be trendy, but it’s popular with young people. Indeed, we were told that accounting was the second-most popular major at the University. St. Petersburg State University has the top-rated economics program in the country. Consequently, economics is the only major that attracted more students than accounting.

The Russian system of education isn’t that different from what students in the U.S. experience. Russian students complete general education requirements during the first two years. In the third year, they enter their major, taking classes in accounting theory, forensic accounting, financial accounting, and corporate accounting, along with other business courses in finance, statistics, and economics. In the fourth year, students study tax law, information systems, and auditing and complete their core business courses. They also spend one semester in a practicum or internship. In the fifth year, students have the option of earning a specialist designation within accounting (for example, audit, tax, information systems, or corporate) and must complete another practicum. To complete the degree, students must prepare and defend a thesis.

In general, the curriculum includes a combination of RAP and IFRS, with the goal of preparing students for the country’s planned adoption of IFRS. St. Petersburg State University also has made a strong effort to offer more foreign study programs or joint programs with universities in Germany, France, and Poland to better prepare students to compete in a global economy.

Certification is a challenge to new accountants in Russia. As we’ve already mentioned, in the past, students who entered the profession as auditors in public accounting firms or as accountants in large multinational companies would often travel to the U.S. to earn the CPA designation. The self-study and travel costs were high, but completing the certification process put these professionals in high demand back home. More recently, the trend is toward obtaining the ACCA (Association of Chartered Certified Accountants) designation because its centralized certification process is friendlier to international students than the state-specific licensure process for the CPA credential.

**Future Issues**

As Russia’s transition to a free-market economy continues, many challenges remain. The decline in college enrollment rates will impact the number of qualified accountants entering the profession. In addition, the Russian government is actively seeking ways to increase foreign investment to reduce the country’s reliance on the oil and gas industry and create a more diversified economy. These efforts have been hampered by the global economic downturn as the competition for foreign investment dollars has intensified.

The country also continues to combat the perception of an unfriendly business environment with widespread corruption, onerous regulations, and aggressive taxing authorities. Further, with deadlines looming, the transition to IFRS will be time-consuming and costly. But it may offer advantages in the long run. For example, the availability of IFRS-compliant consolidated financial statements for diversified businesses will provide investors with better information for decision making and will put Russian firms on more equal footing in the global marketplace.

Only time will tell if Russian leaders can implement effective policies to meet the country’s challenges and improve its business environment. As our trip inspired an enduring interest in the country’s future, we’ll be watching Russia’s efforts and interpreting the developments within the context of our own experiences.

For business professionals who want an adventure of their own, People to People’s Citizen Ambassador Program provides multiple opportunities each year to travel the world and learn about other cultures and business practices. **SF**

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